

Halkbank AD Skopje

Financial Statements
for the year ended
31 December 2011

Contents

Independent Auditors' report

Financial Statements

Statement of financial position	1
Statement of comprehensive income	2
Statement of changes in equity	3
Statement of cash flows	5
Notes to the financial statements	7



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Independent auditor's report to the shareholders of Halkank AD Skopje

We have audited the accompanying financial statements of Halkbank AD Skopje ("the Bank"), which comprise the statement of financial position as at 31 December 2011, the statements of comprehensive income, changes in equity and cash flows for the year then ended, and notes, comprising a summary of significant accounting policies and other explanatory information.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with International Financial Reporting Standard, and for such internal control as management determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditors' Responsibility

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

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on 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 policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

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



Opinion

In our opinion, the financial statements give a true and fair view of the financial position of the Bank as at 31 December 2011, and of its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards.

KPMG Macedonia Ltd

KPMG Macedonia Ltd

28 March 2012

Skopje

Statement of financial position

As at 31 December

<i>In thousands of denars</i>	<i>Note</i>	2011	2010
Assets			
Cash and cash equivalents	15	2,174,409	986,600
Trading assets	16	174,422	178,895
Loans and advances to banks	17	396,947	758,037
Loans and advances to customers	18	5,781,590	4,485,329
Investment securities	19	167,526	768,870
Property and equipment	20	504,872	549,011
Intangible assets	21	37,889	56,950
Other assets	22	212,995	188,937
Total assets		<u>9,450,650</u>	<u>7,972,629</u>
Liabilities			
Deposits from banks	23	10,238	630,845
Deposits from customers	24	5,478,398	4,488,934
Other borrowed funds	25	1,429,259	1,797,604
Provisions	26	2,270	17,533
Other liabilities	27	92,958	81,794
Total liabilities		<u>7,013,123</u>	<u>7,016,710</u>
Equity			
	28		
Share capital		1,884,150	418,700
Share premium		325,854	325,854
Other reserves		80,214	121,313
Retained earnings		147,309	90,052
Total equity		<u>2,437,527</u>	<u>955,919</u>
Total liabilities and equity		<u>9,450,650</u>	<u>7,972,629</u>

The notes on pages 7 – 73 are an integral part of these financial statements.

These financial statements set out on pages 1 to 73 were approved by the Supervisory Board on 28 March 2012 and were signed on its behalf by:

Mr. Tomce Tasevski
Executive Manager

Mr. Erturk Sumer
Executive Manager

Statement of comprehensive income

For the year ended 31 December

<i>In thousands of denars</i>	<i>Note</i>	2011	2010
Interest income	8	557,367	418,986
Interest expense	8	<u>(243,526)</u>	<u>(232,164)</u>
Net interest income		313,841	186,822
Fee and commission income	9	119,314	95,913
Fee and commission expense	9	<u>(49,240)</u>	<u>(35,349)</u>
Net fee and commission income		70,074	60,564
Net trading income	10	7,012	27,132
Net foreign exchange gain		17,018	13,498
Other operating income	11	<u>42,093</u>	<u>28,848</u>
		66,123	69,478
Operating income		450,038	316,864
Net impairment loss on financial assets	18,22	23,733	25,797
Personnel expenses	12	(174,401)	(151,352)
Depreciation and amortisation	20,21	(71,069)	(76,922)
Other expenses	13	<u>(208,567)</u>	<u>(206,103)</u>
		(430,304)	(408,580)
Profit /(Loss) for the period		<u>19,734</u>	<u>(91,716)</u>
Other comprehensive income, net of income tax			
Fair value reserve (available-for-sale financial assets)		<u>(3,323)</u>	<u>1,930</u>
Other comprehensive income for the period, net of income tax		<u>(3,323)</u>	<u>1,930</u>
Total comprehensive income for the period		<u>16,411</u>	<u>(89,786)</u>
Basic and diluted (loss)/earnings per share (MKD)	14	197	(2,190)

The notes on pages 7 – 73 are an integral part of these financial statements

Statement of changes in equity

For the year ended 31 December

<i>In thousands of denars</i>	Share capital	Share premium	Statutory reserve	Fair value reserve	Retained earnings	Total
Balance at 1 January 2010	418,700	325,854	318,828	7,188	(24,872)	1,045,698
Total comprehensive income for the year						
Profit or loss	-	-	-	-	(91,716)	(91,716)
Other comprehensive income, net of income tax						
Fair value reserve (available-for-sale financial assets)						
Net change in fair value	-	-	-	1,930	-	1,930
Total comprehensive income for the year	-	-	-	1,930	(91,716)	(89,786)
Transactions with equity holders, recognized directly in equity						
Appropriation to retained earnings	-	-	(206,640)	-	206,640	-
Other	-	-	7	-	-	7
Total contributions by and distributions to equity holders	-	-	(206,633)	-	206,640	7
Balance at 31 December 2010	418,700	325,854	112,195	9,118	90,052	955,919

Statement of changes in equity (continued)

<i>In thousands of denars</i>	Share capital	Share premium	Statutory reserve	Fair value reserve	Retained earnings	Total
Balance at 1 January 2011	418,700	325,854	112,195	9,118	90,052	955,919
Total comprehensive income for the year	-	-	-	-	19,734	19,734
Profit or loss						
Other comprehensive income, net of income tax						
Fair value reserve (available-for-sale financial assets)						
Net change in fair value	-	-	-	(3,323)	-	(3,323)
Total comprehensive income for the period	-	-	-	(3,323)	19,734	16,411
Transactions with equity holders, recognized directly in equity						
Appropriation to retained earnings	-	-	(37,776)	-	37,776	-
Paid share capital	1,465,450	-	-	-	-	1,465,450
Total contributions by and distributions to equity holders	-	-	(37,776)	-	37,776	-
Balance at 31 December 2011	1,884,150	325,854	74,419	5,795	147,562	2,437,780

The notes on pages 7 - 73 are an integral part of these financial statements.

Statement of cash flows

For the year ended 31 December

<i>In thousands of denars</i>	<i>Note</i>	2011	2010
Cash flows from operating activities			
(Loss) for the period		19,734	(91,716)
<i>Adjustments for:</i>			
Depreciation and amortization	20,21	71,069	76,922
Capital gain on sale of investment securities available-for-sale	11	-	-
Capital gain on sale of property and equipment	11	(12,774)	-
Capital gain on sale of assets acquired through foreclosure procedure	11	(1,270)	(859)
Capital loss on sale of investment securities available-for-sale	13	-	-
Capital loss on sale of assets acquired through foreclosure procedure	13	-	202
Capital loss on sale of property and equipment		19	689
Impairment provision for off balance sheet items	11,13	458	(2,952)
Impairment provision for court-cases	13	(15,329)	12,771
Net interest income	8	(313,841)	(186,822)
Net trading income	10	(7,012)	(27,132)
	16,		
Net impairment loss on financial assets	18,22	(23,733)	(25,797)
Impairment losses on assets acquired through foreclosure procedures	13	1,668	4,362
Dividend income	11	(2,957)	(2,144)
Income tax expense	14	-	-
		<u>(283,968)</u>	<u>(242,476)</u>
Change in financial assets held for trading		-	398,232
Change in loans and advances to banks		361,090	(460,498)
Change in loans and advances to customers		(1,262,012)	(1,180,861)
Change in other assets		(26,718)	(37,780)
Change in deposits from banks		(624,143)	307,544
Change in deposits from customers		977,859	1,426,498
Change in other liabilities and impairment provision related to off balance sheet items		<u>10,772</u>	<u>28,473</u>
		<u>(847,120)</u>	<u>239,132</u>
Interest received		560,754	433,387
Interest paid		(231,978)	(217,613)
Income tax returned/(paid)		-	255
Net cash from operating activities		<u>(518,344)</u>	<u>455,161</u>

Statement of cash flows (continued)

For the year ended 31 December

In thousands of denars

	<i>Note</i>	2011	2010
Cash flows from investing activities			
Acquisition of property and equipment	20	(29,876)	(15,043)
Proceeds from the sale of property and equipment		37,928	-
Acquisition of intangible assets	21	(3,166)	(14,757)
Acquisition of investment securities		597,865	(430,410)
Dividends received		2,957	2,144
Net cash used in investing activities		<u>605,708</u>	<u>(458,066)</u>
Cash flows from financing activities			
Proceeds from other borrowed funds		896,744	791,142
Repayment of other borrowed funds		<u>(1,261,496)</u>	<u>(477,767)</u>
Net cash from/(used in) financing activities		<u>1,100,445</u>	<u>313,375</u>
Net increase/(decrease) in cash and cash equivalents			
		986,600	310,470
Cash and cash equivalents at 1 January		<u>2,174,409</u>	<u>676,130</u>
Cash and cash equivalents at 31 December	15	<u>1,187,809</u>	<u>986,600</u>

The notes on pages 7 – 73 are an integral part of these financial statements.

Notes to the financial statements

1. Reporting entity

Halkbank AD Skopje (“the Bank”) is a joint stock company incorporated and domiciled in the Republic of Macedonia.

The address of the Bank’s registered office is as follows:

Ul. “Mito Hadzivasilev - Jasmin“ bb
1000 Skopje
Republic of Macedonia

In 2011 the Bank changed its name from Export and Credit Banka AD Skopje to Halkbank AD Skopje, as a result of a change in the shareholders structure of the Bank.

The Bank is licensed to perform all banking activities in accordance with the law. The main activities include commercial lending, receiving of deposits, foreign exchange deals, payment operation services in the country and abroad and retail banking services.

The shares of the Bank are traded on the free market on the Macedonian Stock exchange with trade symbol IKB and ISIN CODE (MKIKBA101015).

2. Basis of preparation

(a) Statement of compliance

The financial statements have been prepared in accordance with International Financial Reporting Standards (IFRSs), as issued by the International Accounting Standards Board (IASB).

(b) Basis of measurement

The financial statements have been prepared on the historical cost basis except for the following:

- financial instruments at fair value through profit or loss are measured at fair value;
- available-for-sale financial assets are measured at fair value.

(c) Functional and presentation currency

These financial statements are presented in Macedonian denar (“MKD” or “denars”), which is the Bank’s functional currency. Except as indicated, financial information, presented in MKD has been rounded to the nearest thousand.

(d) Use of estimates and judgments

The preparation of financial statements in conformity with IFRSs requires management to make judgments, estimates and assumptions that affect the application of accounting policies and the reported amounts of assets, liabilities, income and expenses. Actual results may differ from these estimates.

Notes to the financial statements

2. Basis of preparation (continued)

(d) Use of estimates and judgments (continued)

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 and in any future periods affected.

Information about significant areas of estimation uncertainty and critical judgments in applying accounting policies that have the most significant effect on the amount recognized in the financial statements are described in note 5.

3. Significant accounting policies

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

(a) Foreign currency transactions

Transactions in foreign currencies are translated into Macedonian denars at the exchange rates at the dates of the transactions. Monetary assets and liabilities denominated in foreign currencies at the reporting date are retranslated into Macedonian denars at the exchange rate at that date. The foreign currency gain or loss on monetary items is the difference between amortised cost in Macedonian denars at the beginning of the period, adjusted for effective interest and payments during the period, and the amortised cost in foreign currency translated at the spot exchange rate at the end of the period. Non-monetary assets and liabilities denominated in foreign currencies that are measured at fair value are retranslated into Macedonian denars at the exchange rate at the date that the fair value was determined. Foreign currency differences arising on retranslation are recognised in profit or loss, except for the differences arising on the retranslation of available-for-sale equity instruments, which are recognised directly in equity. Non-monetary assets and liabilities that are measured in terms of historical cost in a foreign currency are translated using the exchange rate at the date of the transaction.

The foreign currencies the Bank deals with are predominantly Euro (EUR) and United States Dollars (USD). The exchange rates used for translation at 31 December 2011 and 2010 were as follows:

	2011	2010
	MKD	MKD
1 EUR	61.50	61.51
1 USD	47.53	46.31

Notes to the financial statements

3. Significant accounting policies (continued)

(b) Interest

Interest income and expense are recognised in the profit or loss using the effective interest method. The effective interest rate is the rate that exactly discounts the estimated future cash payments and receipts through the expected life of the financial asset or liability (or, where appropriate, a shorter period) to the carrying amount of the financial asset or liability. When calculating the effective interest rate, the Bank estimates future cash flows considering all contractual terms of the financial instrument but not future credit losses.

The calculation of the effective interest rate includes all fees and points paid or received, (transaction costs, and discounts or premiums) that are an integral part of the effective interest rate. Transaction costs include incremental costs that are directly attributable to the acquisition or issue of a financial asset or liability.

Interest income and expense presented in the statement of comprehensive income include:

- interest on financial assets and liabilities measured at amortised cost calculated on an effective interest rate basis;
- interest on available-for-sale investment securities calculated on an effective interest rate basis.

Interest income and expense on all trading assets and liabilities are considered to be incidental to the Bank's trading operations and are presented together with all other changes in the fair value of trading assets and liabilities in net trading income.

Fair value changes on other financial assets and liabilities carried at fair value through profit or loss, are presented in net income from other financial instruments at fair value through profit or loss in the statement of comprehensive income.

(c) Fees and commission

Fees and commission income and expenses that are integral to the effective interest rate on a financial asset or liability are included in the measurement of the effective interest rate.

Notes to the financial statements

3. Significant accounting policies (continued)

(c) Fees and commission (continued)

Other fees and commission income, including financial services provided by the Bank in respect of foreign currency settlements, guarantees, letters of credit, domestic and foreign payment operations and other services, are recognised as the related services are performed. When a loan commitment is not expected to result in the draw-down of a loan, the related loan commitment fees are recognised on a straight-line basis over the commitment period.

Other fees and commission expense relates mainly to transaction and service fees, which are expensed as the services are received.

(d) Net trading income

Net trading income comprises gains less losses related to trading assets and liabilities, and includes all realised and unrealised fair value changes, interest, dividends and foreign exchange differences.

(e) Dividends

Dividend income is recognised when the right to receive income is established.

(f) Lease payments made

Payments made under operating leases are recognised in profit or loss on a straight-line basis over the term of the lease. Lease incentives received are recognised as an integral part of the total lease expense, over the term of the lease.

(g) Income tax expense

In the Republic of Macedonia a new tax regime had become effective according which the base for income tax computation had been shifted from the profit before taxes to the income “distribution” concept. “Distributions” are split into two components:

- Tax on any dividend distribution – i.e. the tax base is the dividend paid;
- Tax on non deductible items – i.e. the tax base is the non deductible items specified in the tax rulebook less any allowable tax credits. The tax on non deductible items is paid each month in monthly advance installments based on the previous fiscal year computation of such non deductible differences. At year end a final tax computation is prepared with a final tax settlement (see note 23).

As such, the new income tax regime provokes certain implications on the presentation of the tax in the financial statements which are summarized below:

Notes to the financial statements

3. Significant accounting policies (continued)

(g) Income tax expense (continued)

(i) Tax on dividend distribution:

Tax on dividend distribution is considered to be income tax within scope of International Accounting Standards - Tax on Income ("IAS 12").

The timing of recognition of this type of income tax is to be consistent with the underlining dividend liability recognition (i.e., recognized when the dividend is paid and/or declared). As such no provisions are required for income tax arising from dividend distribution until the dividend is declared and/or paid.

When the tax on dividend distribution arises on interim (advance) dividend paid before the year end, the income tax charge is recognized and presented in the Statement of comprehensive income after profit and loss before tax as income tax expense.

When the tax on dividend distribution arises from retained earnings, it is recognized and presented in the Statement of changes in equity.

(ii) Tax on non deductible items:

Tax on non deductible items is not income tax and is out of scope of IAS 12. Accordingly, such tax expense is presented within the operating results see note 12, and related tax payable/receivable is presented within the other assets/other liabilities in the statement of financial position.

Recognition of tax provisions:

In case of tax contingencies, provisions are made in line with International Accounting Standards – Provisions, Contingent Liabilities and Contingent Assets adopted in the Republic of Macedonia ("IAS 37").

Such provisions are not presented as deferred tax assets or deferred tax liabilities, but as other assets or other liabilities.

Recognition/reversal of such tax provisions (that is not income taxes) is presented within the other expenses/other income.

Notes to the financial statements

3. Significant accounting policies (continued)

(h) Financial assets and liabilities

(i) *Recognition and initial measurement*

The Bank initially recognises loans and advances, deposits and borrowed funds on the date at which they are originated. Regular way purchases and sales of financial assets are recognised on the trade date at which the Bank commits to purchase or sell the asset. All other financial assets and liabilities are initially recognised on the trade date at which the Bank becomes a party to the contractual provisions of the instrument.

A financial asset or financial liability is initially measured at fair value plus, for an item not subsequently measured at fair value through profit or loss, transaction costs that are directly attributable to its acquisition or issue.

(ii) *Classification*

See accounting policies 3(i), (j), (k) and (l).

(iii) *Derecognition*

The Bank derecognises a financial asset when the contractual rights to the cash flows from the financial asset expire, or when it transfers the financial asset in a transaction in which substantially all the risks and rewards of ownership of the financial asset are transferred or in which the Bank neither transfers nor retains substantially all the risks and rewards of ownership and it does not retain control of the financial asset.

Any interest in transferred financial assets that qualify for derecognition that is created or retained by the Bank is recognised as a separate asset or liability in the statement of financial position. On derecognition of a financial asset, the difference between the carrying amount of the asset (or the carrying amount allocated to the portion of the asset transferred), and consideration received (including any new asset obtained less any new liability assumed) is recognised in profit or loss.

In transactions in which the Bank neither retains nor transfers substantially all the risks and rewards of ownership of a financial asset and it retains control over the asset, the Bank continues to recognise the asset to the extent of its continuing involvement, determined by the extent to which it is exposed to changes in the value of the transferred asset.

The Bank derecognises a financial liability when its contractual obligations are discharged or cancelled or expire.

Notes to the financial statements

3. Significant accounting policies (continued)

(h) Financial assets and liabilities (continued)

(iv) *Offsetting*

Financial assets and liabilities are offset and the net amount presented in the statement of financial position when, and only when, the Bank has a legal right to set off the recognised amounts and it intends either to settle on a net basis or to realise the asset and settle the liability simultaneously.

Income and expenses are presented on a net basis only when permitted under IFRSs, or for gains and losses arising from a group of similar transactions such as in the Bank's trading activity.

(v) *Amortised cost measurement*

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

(vi) *Fair value measurement*

Fair value is the amount for which an asset could be exchanged, or a liability settled, between knowledgeable, willing parties in an arm's length transaction on the measurement date.

When available, the Bank measures the fair value of an instrument using quoted prices in an active market for that instrument. A market is regarded as active if quoted prices are readily and regularly available and represent actual and regularly occurring market transactions on an arm's length basis.

If a market for a financial instrument is not active, the Bank establishes fair value using a valuation technique. Valuation techniques include using recent arm's length transactions between knowledgeable, willing parties (if available), reference to the current fair value of other instruments that are substantially the same, discounted cash flow analyses and option pricing models.

The best evidence of the fair value of a financial instrument at initial recognition is the transaction price, i.e., the fair value of the consideration given or received, unless the fair value of that instrument is evidenced by comparison with other observable current market transactions in the same instrument (i.e., without modification or repackaging) or based on a valuation technique whose variables include only data from observable markets.

Assets are measured at a bid price; liabilities are measured at an asking price.

Notes to the financial statements

3. Significant accounting policies (continued)

(h) Financial assets and liabilities (continued)

(vii) *Identification and measurement of impairment*

At each reporting date the Bank assesses whether there is objective evidence that financial assets not carried at fair value through profit or loss are impaired. A financial asset or a group of financial assets is (are) impaired when objective evidence demonstrates that a loss event has occurred after the initial recognition of the asset(s), and that the loss event has an impact on the future cash flows on the asset(s) that can be estimated reliably.

Objective evidence that financial assets (including equity securities) are impaired can include significant financial difficulty of the borrower or issuer, default or delinquency by a borrower, restructuring of a loan or advance by the Bank on terms that the Bank would not otherwise consider, indications that a borrower or issuer will enter bankruptcy, the disappearance of an active market for a security, or other observable data relating to a group of assets such as adverse changes in the payment status of borrowers or issuers in the group, or economic conditions that correlate with defaults in the group. In addition, for an investment in an equity security, a significant or prolonged decline in its fair value below its cost is objective evidence of impairment.

The Bank considers evidence of impairment for loans and advances and investment securities at both a specific asset and collective level. All individually significant loans and advances and investment securities are assessed for specific impairment. All individually significant loans and advances found not to be specifically impaired are then collectively assessed for any impairment that has been incurred but not yet identified. Loans and advances that are not individually significant are collectively assessed for impairment by grouping together loans and advances with similar risk characteristics.

Impairment losses on assets carried at amortised cost are measured as the difference between the carrying amount of the financial asset and the present value of estimated future cash flows discounted at the asset's original effective interest rate. Impairment losses are recognised in profit or loss and reflected in an allowance account against loans and advances. Interest on the impaired asset continues to be recognised through the unwinding of the discount. When a subsequent event causes the amount of impairment loss to decrease, the decrease in impairment loss is reversed through profit or loss.

Notes to the financial statements

3. Significant accounting policies (continued)

(h) Financial assets and liabilities (continued)

(vii) *Identification and measurement of impairment (continued)*

Impairment losses on available-for-sale investment securities are recognised by transferring the cumulative loss that has been recognised in other comprehensive income to profit or loss as a reclassification adjustment. The cumulative loss that is reclassified from other comprehensive income to profit or loss is the difference between the acquisition cost, net of any principal repayment and amortisation, and the current fair value, less any impairment loss previously recognised in profit or loss. Changes in impairment provisions attributable to time value are reflected as a component of interest income.

If, in a subsequent period, the fair value of an impaired available-for-sale debt security increases and the increase can be objectively related to an event occurring after the impairment loss was recognised in profit or loss, the impairment loss is reversed, with the amount of the reversal recognised in profit or loss. However, any subsequent recovery in the fair value of an impaired available-for-sale equity security is recognised in other comprehensive income.

The Bank writes off certain loans and advances and investment securities when they are determined to be uncollectible (see note 4).

(i) Cash and cash equivalents

Cash and cash equivalents include cash balance on hand, demand deposits with banks, cash deposited with the National Bank of the Republic of Macedonia (“NBRM”) and highly liquid financial assets with original maturities of less than three months, which are subject to insignificant risk of changes in their fair value, and are used by the Bank in the management of its short-term commitments.

Cash and cash equivalents are carried at amortised cost in the statement of financial position.

Notes to the financial statements

3. Significant accounting policies (continued)

(j) Trading assets and liabilities

Trading assets and liabilities are those assets and liabilities that the Bank acquires or incurs principally for the purpose of selling or repurchasing in the near term, or holds as part of a portfolio that is managed together for short-term profit or position taking.

Trading assets and liabilities are initially recognised and subsequently measured at fair value in the statement of financial position, with transaction costs recognised in profit or loss. All changes in fair value are recognised as part of net trading income in profit or loss. Trading assets and liabilities are not reclassified subsequent to their initial recognition, except that nonderivative trading assets, other than those designated at fair value through profit or loss upon initial recognition, may be reclassified out of the fair value through profit or loss (i.e., trading) category if they are no longer held for the purpose of being sold or repurchased in the near term and the following conditions are met:

- If the financial asset would have met the definition of loans and receivables (if the financial asset had not been required to be classified as held for trading at initial recognition), then it may be reclassified if the Bank has the intention and ability to hold the financial asset for the foreseeable future or until maturity.
- If the financial asset would not have met the definition of loans and receivables, then it may be reclassified out of the trading category only in 'rare circumstances'.

(k) Loans and advances

Loans and advances are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market and that the Bank does not intend to sell immediately or in the near term.

Loans and advances to banks are classified as loans and receivables.

Loans and advances are initially measured at fair value plus incremental direct transaction costs, and subsequently measured at their amortised cost using the effective interest method.

Notes to the financial statements

3. Significant accounting policies (continued)

(1) Investment securities

Subsequent to initial recognition investment securities are accounted for depending on their classification as either held to maturity, fair value through profit or loss, or available-for-sale.

(i) Held-to-maturity

Held-to-maturity investments are non-derivative assets with fixed or determinable payments and fixed maturity that the Bank has the positive intent and ability to hold to maturity, and which are not designated as at fair value through profit or loss or as available for sale.

Held-to-maturity investments are carried at amortised cost using the effective interest method.

A sale or reclassification of a more than insignificant amount of held-to-maturity investments would result in the reclassification of all held-to-maturity investments as available for sale, and would prevent the Bank from classifying investment securities as held to maturity for the current and the following two financial years. However, sales and reclassifications in any of the following circumstances would not trigger a reclassification:

- sales or reclassifications that are so close to maturity that changes in the market rate of interest would not have a significant effect on the financial asset's fair value;
- sales or reclassifications after the Bank has collected substantially all of the asset's original principal;
- sales or reclassifications attributable to non-recurring isolated events beyond the Bank's control that could not have been reasonably anticipated.

(ii) Available-for-sale

Available-for-sale investments are non-derivative investments that are designated as available for sale or are not classified as another category of financial assets. Unquoted equity securities whose fair value cannot reliably be measured are carried at cost. All other available-for-sale investments are carried at fair value.

Interest income is recognised in profit or loss using the effective interest method. Dividend income is recognised in profit or loss when the Bank becomes entitled to the dividend. Foreign exchange gains or losses on available-for-sale debt security investments are recognised in profit or loss.

Other fair value changes are recognised in other comprehensive income until the investment is sold or impaired, whereupon the cumulative gains and losses previously recognised in other comprehensive income are reclassified to profit or loss as a reclassification adjustment.

Notes to the financial statements

3. Significant accounting policies (continued)

(l) Investment securities (continued)

(ii) *Available-for-sale (continued)*

A non-derivative financial asset may be reclassified from the available-for-sale category to the loans and receivables category if it otherwise would have met the definition of loans and receivables and if the Bank has the intention and ability to hold that financial asset for the foreseeable future or until maturity.

(m) Property and equipment

(i) *Recognition and measurement*

Items of property and equipment are measured at cost less accumulated depreciation and accumulated impairment losses.

Cost includes expenditures that are directly attributable to the acquisition of the asset. The cost of self-constructed assets includes the cost of materials and direct labour, any other costs directly attributable to bringing the assets to a working condition for their intended use, the costs of dismantling and removing the items and restoring the site on which they are located, and capitalised borrowing costs. Purchased software that is integral to the functionality of the related equipment is capitalised as part of that equipment.

When parts of an item of property or equipment have different useful lives, they are accounted for as separate items (major components) of property and equipment.

The gain or loss on disposal of an item of property and equipment is determined by comparing the proceeds from disposal with the carrying amount of the item of property and equipment, and are recognised within other income or other expenses in profit or loss.

(ii) *Subsequent costs*

The cost of replacing part of an item of property or equipment is recognised in the carrying amount of the item if it is probable that the future economic benefits embodied within the part will flow to the Bank and its cost can be measured reliably. The carrying amount of the replaced part is derecognised. The costs of the day-to-day servicing of property and equipment are recognised in profit or loss as incurred.

(iii) *Depreciation*

Depreciation is recognised in profit or loss on a straight-line basis over the estimated useful lives of each part of an item of property and equipment since this most closely reflects the expected pattern of consumption of the future economic benefits embodied in the asset.

Notes to the financial statements

3. Significant accounting policies (continued)

(m) Property and equipment (continued)

(iii) Depreciation (continued)

Depreciation rates, based on the estimated useful lives for the current and comparative periods are as follows:

	%
Buildings	2.5
Furniture and equipment	10 - 25

Depreciation methods, useful lives and residual value are reviewed at each financial reporting date and adjusted if appropriate.

(n) Intangible assets

(i) Recognition and measurement

Intangible assets acquired by the Bank are stated at cost less accumulated amortisation and accumulated impairment losses.

(ii) Subsequent expenditure

Subsequent expenditure on intangible assets is capitalised only when it increases the future economic benefits embodied in the specific asset to which it relates. All other expenditure is expensed as incurred.

(iii) Amortisation

Amortisation is recognised in profit or loss on a straight-line basis over the estimated useful life of the intangible assets, from the date that it is available for use since this most closely reflects the expected pattern of consumption of the future economic benefits embodied in the asset.

The amortisation rates based on the estimated useful lives for the current and comparative periods are as follows:

	%
Software	25
Licences	25

Amortization methods, estimated useful lives and residual values are reviewed at each financial reporting date and adjusted if appropriate.

Notes to the financial statements

3. Significant accounting policies (continued)

(o) Leased assets – lessee

Leases in terms of which the Bank assumes substantially all the risks and rewards of ownership are classified as finance leases. Upon initial recognition the leased asset is measured at an amount equal to the lower of its fair value and the present value of the minimum lease payments. Subsequent to initial recognition, the asset is accounted for in accordance with the accounting policy applicable to that asset.

Other leases are operating leases and the leased assets are not recognised on the Bank's statement of financial position.

(p) Impairment of non-financial assets

The carrying amounts of the Bank's non-financial assets, are reviewed at each reporting date to determine whether there is any indication of impairment. If any such indication exists then the asset's recoverable amount is estimated.

An impairment loss is recognised if the carrying amount of an asset or its cash-generating unit exceeds its recoverable amount. A cash-generating unit is the smallest identifiable asset group that generates cash flows that largely are independent from other assets and groups. Impairment losses are recognised in profit or loss. Impairment losses in respect of cash-generating units are allocated to reduce the carrying amount of the other assets in the unit (group of units) on a *pro rata* basis.

The recoverable amount of an asset or cash-generating unit is the greater of its value in use and its fair value less costs to sell. 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.

Impairment losses recognised in prior periods are assessed at each reporting date for any indications that the loss has decreased or no longer exists. An impairment loss is reversed if there has been a change in the estimates used to determine the recoverable amount. An impairment loss is reversed only to the extent that the asset's carrying amount does not exceed the carrying amount that would have been determined, net of depreciation or amortisation, if no impairment loss had been recognised.

(q) Deposits and borrowed funds

Deposits and borrowed funds are the Bank's sources of debt funding.

The Bank classifies capital instruments as financial liabilities or equity instruments in accordance with the substance of the contractual terms of the instrument.

Notes to the financial statements

3. Significant accounting policies (continued)

(q) Deposits and borrowed funds (continued)

Deposits and borrowed funds are initially measured at fair value plus incremental direct transaction costs, and subsequently measured at their amortised cost using the effective interest method, except where the Bank chooses to carry the liabilities at fair value through profit or loss.

(r) Provisions

A provision is recognised if, as a result of a past event, the Bank has a present legal or constructive obligation that can be estimated reliably, and it is probable that an outflow of economic benefits will be required to settle the obligation. Provisions are determined by discounting the expected future cash flows at a pre-tax rate that reflects current market assessments of the time value of money and, where appropriate, the risks specific to the liability.

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

(s) Employee benefits

(i) *Defined contribution plans*

The Bank contributes to its employees' post retirement plans as prescribed by the national legislation and will have no legal or constructive obligation to pay further amounts. Contributions, based on salaries, are made to the national organisations responsible for the payment of pensions.

There is no additional liability in respect of these plans. Obligations for contributions to defined contribution pension plans are recognised as an expense in profit or loss when they are due.

(ii) *Short-term benefits*

Short-term employee benefit obligations are measured on an undiscounted basis and are expensed as the related service is provided.

A liability is recognised for the amount expected to be paid under short-term cash bonus or profit-sharing plans if the Bank has a present legal or constructive obligation to pay this amount as a result of past service provided by the employee and the obligation can be estimated reliably.

Notes to the financial statements

3. Significant accounting policies (continued)

(s) Employee benefits (continued)

(iii) *Other long-term employee benefits*

In accordance with local regulations the Bank pays two average salaries to its employees at the moment of retirement. The employee benefits are discounted to determine their present value. There is no additional liability in respect of post retirement.

(t) Share capital and reserves

(i) *Ordinary shares*

Ordinary shares are classified as equity.

(ii) *Share issue costs*

Incremental costs directly attributable to the issue of equity instruments are recognised as a deduction from equity.

(iii) *Repurchase of share capital*

When share capital recognised as equity is repurchased, the amount of the consideration paid, which includes directly attributable costs, is recognised as a deduction from equity. Repurchased shares are classified as treasury shares and are presented as a deduction from total equity. When treasury shares are sold subsequently the amount received is recognised as an increase on equity, and the resulting surplus or deficit of the transaction is transferred to/from share premium.

(iv) *Dividends*

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

(u) Earnings per share

The Bank presents basic and diluted earnings per share data for its ordinary shares. Basic earnings per share 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. Diluted earnings per share is determined by adjusting the profit or loss attributable to ordinary shareholders and the weighted average number of ordinary shares outstanding for the effects of all dilutive potential ordinary shares, which comprise share options granted to employees.

Notes to the financial statements

3. Significant accounting policies (continued)

(v) Segment reporting

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

(w) New standards and interpretations not yet adopted

The following new Standards and Interpretations are not yet effective for the year ended 31 December 2011, and have not been applied in preparing these financial statements:

- Amendments to IFRS 7 Disclosures - Transfers of Financial Assets (Effective for annual periods beginning on or after 1 July 2011; to be applied prospectively. Earlier application is permitted.)

The Amendments require disclosure of information that enables users of financial statements:

- to understand the relationship between transferred financial assets that are not derecognised in their entirety and the associated liabilities; and
- to evaluate the nature of, and risks associated with, the entity's continuing involvement in derecognised financial assets.

The Amendments define "continuing involvement" for the purposes of applying the disclosure requirements.

The Bank does not expect the amendment to IFRS 7 to have material impact on the financial statements, because of the nature of the Bank's operations and the types of financial assets that it holds.

- Amendments to IFRS 7 Disclosures - Offsetting Financial Assets and Financial Liabilities (Effective for annual periods beginning on or after 1 January 2013 and interim periods within those annual periods; to be applied retrospectively.)

The Amendments contain new disclosure requirements for financial assets and liabilities that are:

- offset in the statement of financial position; or
- subject to master netting arrangements or similar agreements.

The Bank is currently in the process of evaluating the potential effect of this Standard.

Notes to the financial statements

3. Significant accounting policies (continued)

(w) New standards and interpretations not yet adopted (continued)

- IFRS 9 Financial Instruments issued in 2009 (effective for annual periods beginning on or after 1 January 2015, to be applied prospectively, early adoption is permitted).

This Standard replaces the guidance in IAS 39, *Financial Instruments: Recognition and Measurement*, about classification and measurement of financial assets. The Standard eliminates the existing IAS 39 categories of held to maturity, available for sale and loans and receivable.

Financial assets will be classified into one of two categories on initial recognition:

- financial assets measured at amortized cost; or
- financial assets measured at fair value.

A financial asset is measured at amortized cost if the following two conditions are met:

- the asset is held within a business model whose objective is to hold assets in order to collect contractual cash flows; and,
- its contractual terms give rise on specified dates to cash flows that are solely payments of principal and interest on the principal outstanding.

Gains and losses on remeasurement of financial assets measured at fair value are recognised in profit or loss, except that for an investment in an equity instrument which is not held for trading, IFRS 9 provides, on initial recognition, an irrevocable election to present all fair value changes from the investment in other comprehensive income (OCI). The election is available on an individual share-by-share basis. No amount recognised in OCI is ever reclassified to profit or loss at a later date.

The Bank is currently in the process of evaluating the potential effect of this Standard.

- Additions to IFRS 9 Financial Instruments issued in 2010 (effective for annual periods beginning on or after 1 January 2015, to be applied prospectively, early adoption is permitted).

The 2010 additions to IFRS 9 replace the guidance in IAS 39 *Financial Instruments: Recognition and Measurement*, about classification and measurement of financial liabilities and derecognition of financial assets and financial liabilities.

The Standard retains almost all of the existing requirements from IAS 39 on the classification and measurement of financial liabilities and for derecognition of financial assets and financial liabilities.

The Standard requires that the amount of change in fair value attributable to changes in the credit risk of a financial liability designated at initial recognition as fair value through profit or loss, be presented in other comprehensive income (OCI), with only the remaining amount of the total gain or loss included in profit or loss.

Notes to the financial statements

3. Significant accounting policies (continued)

(w) New standards and interpretations not yet adopted (continued)

However, if this requirement creates or enlarges an accounting mismatch in profit or loss, then the whole fair value change is presented in profit or loss. Amounts presented in OCI are not subsequently reclassified to profit or loss but may be transferred within equity.

Derivative financial liabilities that are linked to and must be settled by delivery of an unquoted equity instrument whose fair value cannot be reliably measured, are required to be measured at fair value under IFRS 9.

The Bank is currently in the process of evaluating the potential effect of this Standard.

- Amendments to IFRS 9 and IFRS 7: Mandatory effective date and transitional disclosures.

These Amendments change the disclosure and restatement requirements relating to the initial application of IFRS 9 Financial Instruments (2009) and IFRS 9 (2010).

The amended IFRS 7 require to disclose more details about the effect of the initial application of IFRS 9 when an entity does not restate comparative information in accordance with the amended requirements of IFRS 9.

If an entity adopts IFRS 9 on or after 1 January 2013, then it will no longer be required to restate comparative information for periods prior to the date of initial application.

If an entity early adopts IFRS 9 in 2012, then it has a choice either to restate comparative information or to provide the enhanced disclosures as required by the amended IFRS 7.

If an entity early adopts IFRS 9 prior to 2012, then neither restatement of comparative information nor provision of the enhanced disclosures under the amended IFRS 7 are required.

The Bank is currently in the process of evaluating the potential effect of this Standard.

- IFRS 10 Consolidated Financial Statements and IAS 27 (2011) Separate Financial Statements. (effective for annual periods beginning on or after 1 January 2013; to be applied retrospectively when there is a change in the control conclusion. Earlier application is permitted if IFRS 11, IFRS 12, IAS 27 (2011) and IAS 28 (2011) are also applied early.)

IFRS 10 provides a single model to be applied in the control analysis for all investees, including entities that currently are SPEs in the scope of SIC-12. IFRS 10 introduces new requirements to assess control that are different from the existing requirements in IAS 27 (2008). Under the new single control model, an investor controls an investee when (1) it is exposed or has rights to variable returns from its involvements with the investee, (2) has the ability to affect those returns through its power over that investee and (3) there is a link between power and returns.

The new Standard also includes the disclosure requirements and the requirements relating to the preparation of consolidated financial statements. These requirements are carried forward from IAS 27 (2008).

Notes to the financial statements

3. Significant accounting policies (continued)

(w) New standards and interpretations not yet adopted (continued)

IFRS 10 is not relevant to the Bank's financial statements as the Bank has no investees and does not prepare consolidated financial statements.

- IFRS 11 Joint Arrangements (effective for annual periods beginning on or after 1 January 2013; to be applied retrospectively subject to transitional provisions. Earlier application is permitted if IFRS 10, IFRS 12, IAS 27 (2011) and IAS 28 (2011) are also applied early.)

IFRS 11, Joint Arrangements, supersedes and replaces IAS 31, Interest in Joint Ventures. IFRS 11 does not introduce substantive changes to the overall definition of an arrangement subject to joint control, although the definition of control, and therefore indirectly of joint control, has changed due to IFRS 10.

Under the new Standard, joint arrangements are divided into two types, each having its own accounting model defined as follows:

- a joint operation is one whereby the jointly controlling parties, known as the joint operators, have rights to the assets, and obligations for the liabilities, relating to the arrangement.
- A joint venture is one whereby the jointly controlling parties, known as joint venturers, have rights to the net assets of the arrangement.

IFRS 11 effectively carves out, from IAS 31 jointly controlled entities, those cases in which, although there is a separate vehicle for the joint arrangement, that separation is ineffective in certain ways. These arrangements are treated similarly to jointly controlled assets/operations under IAS 31, and are now called joint operations.

The remainder of IAS 31 jointly controlled entities, now called joint ventures, are stripped of the free choice of equity accounting or proportionate consolidation; they must now always use the equity method in its consolidated financial statements.

The Bank does not expect IFRS 11 to have material impact on the financial statements since it is not a party to any joint arrangements.

- IFRS 12 Disclosure of Interests in Other Entities (effective for annual periods beginning on or after 1 January 2013; to be applied retrospectively. Earlier application is permitted. Providing some of the disclosures required by IFRS 12 before the effective date does not compel the entity to comply with all the requirements of IFRS 12 or to apply IFRS 10, IFRS 11, IFRS 12, IAS 27 (2011) and IAS 28 (2011) early.)

IFRS 12 requires additional disclosures relating to significant judgements and assumptions made in determining the nature of interests in an entity or arrangement, interests in subsidiaries, joint arrangements and associates and unconsolidated structured entities.

The Bank does not expect IFRS 12 to have material impact on the financial statements.

Notes to the financial statements

3. Significant accounting policies (continued)

(w) New standards and interpretations not yet adopted (continued)

- IFRS 13 Fair Value Measurement (effective prospectively for annual periods beginning on or after 1 January 2013. Earlier application is permitted.)

IFRS 13 replaces the fair value measurement guidance contained in individual IFRSs with a single source of fair value measurement guidance. It defines fair value, establishes a framework for measuring fair value and sets out disclosure requirements for fair value measurements. IFRS 13 explains 'how' to measure fair value when it is required or permitted by other IFRSs. The standard does not introduce new requirements to measure assets or liabilities at fair value, nor does it eliminate the practicability exceptions to fair value measurements that currently exist in certain standards.

The standard contains an extensive disclosure framework that provides additional disclosures to existing requirements to provide information that enables financial statement users to assess the methods and inputs used to develop fair value measurements and, for recurring fair value measurements that use significant unobservable inputs, the effect of the measurements on profit or loss or other comprehensive income.

The Bank is currently in the process of evaluating the potential effect of this Standard.

- Amendments to IAS 1 Presentation of Financial Statements: Presentation of Items of Other Comprehensive Income (effective for annual periods beginning on or after 1 July 2012; to be applied retrospectively. Earlier application is permitted.)

The amendments:

- require that an entity presents separately the items of other comprehensive income that may be reclassified to profit or loss in the future from those that would never be reclassified to profit or loss. If items of other comprehensive income are presented before related tax effects, then the aggregated tax amount should be allocated between these sections.
- change the title of the Statement of Comprehensive Income to Statement of Profit or Loss and Other Comprehensive Income, however, other titles are also allowed to be used.

The Bank is currently in the process of evaluating the potential effect of these amendments.

- Amendments to IAS 12 Income taxes - Deferred Tax: Recovery of Underlying Assets (effective for annual periods beginning on or after 1 January 2012. Earlier application is permitted.).

Notes to the financial statements

3. Significant accounting policies (continued)

(w) New standards and interpretations not yet adopted (continued)

The 2010 amendment introduces an exception to the current measurement principles based on the manner of recovery in paragraph 52 of IAS 12 for investment property measured using the fair value model in accordance with IAS 40 by introducing a rebuttable presumption that the carrying value of the underlying assets would be recovered entirely by sale. Management's intention would not be relevant unless the investment property is depreciable and held within a business model whose objective is to consume substantially all of the asset's economic benefits over the life of the asset. This is the only instance in which the presumption can be rebutted

The amendments are not relevant to the Bank's financial statements, since under the unique tax regime applied in the Republic of Macedonia deferred tax may not be recognised (see note 3 f) and the Bank does not have any investment properties measured using the fair value model in IAS 40.

- IAS 19 (2011) Employee Benefits (effective for annual periods beginning on or after 1 January 2013; to be applied retrospectively. Transitional provisions apply. Earlier application is permitted.)

The amendment requires actuarial gains and losses to be recognised immediately in other comprehensive income. The amendment removes the corridor method previously applicable to recognising actuarial gains and losses, and eliminates the ability for entities to recognise all changes in the defined benefit obligation and in plan assets in profit or loss, which currently is allowed under the requirements of IAS 19.

The amendment also requires the expected return on plan assets recognised in profit or loss to be calculated based on rate used to discount the defined benefit obligation.

The amendments are not relevant to the Bank's financial statements, since the Bank does not have any defined benefit plans.

- IAS 27 (2011) Separate Financial Statements (effective for annual periods beginning on or after 1 January 2013. Earlier application is permitted if IFRS 10, IFRS 11, IFRS 12 and IAS 28 (2011) are also applied early.)

IAS 27 (2011) carries forward the existing accounting and disclosure requirements of IAS 27 (2008) for separate financial statements, with some minor clarifications. As well, the existing requirements of IAS 28 (2008) and IAS 31 for separate financial statements have been incorporated into IAS 27 (2011). The Standard no longer addresses the principle of control and requirements relating to the preparation of consolidated financial statements, which have been carried over into IFRS 10 Consolidated Financial Statements.

IAS 27 is not relevant to the Bank's financial statements as the Bank has no investees and does not prepare consolidated financial statements.

Notes to the financial statements

3. Significant accounting policies (continued)

(w) New standards and interpretations not yet adopted (continued)

- IAS 28 (2011) Investments in Associates and Joint Ventures (amendments effective for annual periods beginning on or after 1 January 2013; to be applied retrospectively. Earlier application is permitted if IFRS 10, IFRS 11, IFRS 12 and IAS 27 (2011) are also applied early.)

There are limited amendments made to IAS 28 (2008):

- Associates and joint ventures held for sale. IFRS 5 Non-current Assets Held for Sale and Discontinued Operations applies to an investment, or a portion of an investment, in an associate or a joint venture that meets the criteria to be classified as held for sale. For any retained portion of the investment that has not been classified as held for sale, the equity method is applied until disposal of the portion held for sale. After disposal, any retained interest is accounted for using the equity method if the retained interest continues to be an associate or a joint venture.

Changes in interests held in associates and joint ventures. Previously, IAS 28 (2008) and IAS 31 specified that the cessation of significant influence or joint control triggered remeasurement of any retained stake in all cases, even if significant influence was succeeded by joint control. IAS 28 (2011) now requires that in such scenarios the retained interest in the investment is not remeasured.

The Bank does not expect the amendments to Standard to have material impact on the financial statements since it does not have any investments in associates or joint ventures that will be impacted by the amendments.

- *Amendments to IAS 32 Offsetting Financial Assets and Financial Liabilities* (effective for annual periods beginning on or after 1 January 2014; to be applied retrospectively. Earlier application is permitted).

The Amendments do not introduce new rules for offsetting financial assets and liabilities; rather they clarify the offsetting criteria to address inconsistencies in their application.

The Amendments clarify that an entity currently has a legally enforceable right to set-off if that right is:

- not contingent on a future event; and
- enforceable both in the normal course of business and in the event of default, insolvency or bankruptcy of the entity and all counterparties.

The Bank does not expect the Amendments to have any impact on the financial statements since it does not apply offsetting to any of its financial assets and financial liabilities and it has not entered into master netting arrangements.

Notes to the financial statements

3. Significant accounting policies (continued)

(w) New standards and interpretations not yet adopted (continued)

- IFRIC 20 Stripping Costs in the Production Phase of a Surface Mine (effective for annual periods beginning on or after 1 January 2013. It applies prospectively to production stripping costs incurred on or after the beginning of the earliest period presented. Earlier application is permitted.)

The Interpretation sets out requirements relating to the recognition of production stripping costs, initial and subsequent measurement of stripping activity assets.

To the extent that benefits from production stripping are realised in the form of inventory produced, the related production stripping costs are accounted for in accordance with IAS 2 Inventories.

Production stripping costs that improve access to ore to be mined in the future are recognised as a non-current asset if, and only if, all of the following criteria are met:

- it is probable that future economic benefits will flow to the entity;
- the entity can identify the component of the ore body for which access has been improved; and
- the costs relating to the stripping activity associated with that component can be measured reliably.

The stripping activity asset shall be accounted for as an addition to, or as an enhancement of, an existing asset.

The stripping activity asset shall initially be recognised at cost while after initial recognition, it shall be carried at either its cost or its revalued amount, less depreciation or amortisation and impairment losses, in the same way as the existing asset of which it is a part.

The Interpretation also requires that when the costs of the stripping activity asset and of the inventory produced are not separately identifiable, the entity allocates production stripping costs between the two based on a 'relevant' production measure.

The Bank does not expect the Interpretation to have any impact on the financial statements since it does not have any stripping activities.

Notes to the financial statements

4. Financial risk management

(a) Introduction and overview

The Bank has exposure to the following risks from its use of financial instruments:

- credit risk
- liquidity risk
- market risks

This note presents information about the Bank's exposure to each of the above risks, the Bank's objectives, policies and processes for measuring and managing risk, and the Bank's management of capital.

Risk management framework

The Supervisory Board ("the Board") has overall responsibility for the establishment and oversight of the Bank's risk management framework. The Board has established the Credit Committee and Risk Management Committee, which are responsible for developing and monitoring Bank's risk management policies in their specified areas.

The Bank's risk management policies are established to identify and analyse the risks faced by the Bank, to set appropriate risk limits and controls, and to monitor risks and adherence to limits. Risk management policies and systems are reviewed regularly to reflect changes in the regulation, market conditions, products and services offered. The Bank, through its training and procedures and policies for management, aims to develop a constructive control environment, in which all employees understand their roles and obligations.

The Bank's Audit Committee is responsible for monitoring compliance with the Bank's risk management policies and procedures, and for reviewing the adequacy of the risk management framework in relation to the risks faced by the Bank. The Bank's Audit Committee is assisted in these functions by Internal Audit. Internal Audit undertakes both regular and ad-hoc reviews of risk management controls and procedures, the results of which are reported to the Audit Committee.

(b) Credit risk

Credit risk is the risk of financial loss to the Bank if a customer or counterparty to a financial instrument fails to meet its contractual obligations, and arises principally from the Bank's loans and advances to customers and other banks and investment securities. For risk management reporting purposes, the Bank considers and consolidates all elements of credit risk exposure (such as individual obligor default risk, country and sector risk).

Notes to the financial statements

4. Financial risk management (continued)

(b) Credit risk (continued)

For risk management purposes, credit risk arising on trading assets is managed independently; and information thereon is disclosed below. The market risk in respect of changes in value in trading assets arising from changes in market credit spreads applied to investment and included in trading assets is managed as a component of market risk, further details are provided in note 4(d) below.

Management of credit risk

The Supervisory Board has delegated responsibility for the management of credit risk to its Credit Committee that approves all credit exposures less 10% of the Bank's own funds. All credit exposures greater than 10% of the Bank's own funds must be approved by the Risk Management Committee. Separate Bank's Credit departments (Corporate Loans Division and Retail Division) are responsible for oversight of the Bank's credit risk, including:

- *Formulating credit policies*, covering collateral requirements, credit assessment, risk grading and reporting, documentary and legal procedures, and compliance with regulatory and statutory requirements.
- *Reviewing and assessing credit risk*. Credit departments assess all credit exposures in excess of designated limits, prior to facilities being committed to customers.
- *Limiting concentrations of exposure* to geographies and industries (for loans and advances), and by issuer, credit rating band, market liquidity and country (for investment securities).
- *Banks' credit risk gradings* in order to categorise exposures according to the degree of risk of financial loss faced and to focus management on the risks. The risk grading system is used in determining where impairment losses may be required. The current risk grading framework consists of six grades reflecting varying degrees of risk of default and the availability of collateral.
- *Reviewing compliance* with agreed exposure limits, including those for industries, country risk and product types. Regular reports for the credit exposure, risk grading and allowance for impairment are provided to the Risk Management Committee, and appropriate corrective action is taken.

Credit departments are required to implement credit policies and procedures and are responsible for the quality and performance of its credit portfolio and for monitoring and controlling all credit risks in its portfolios.

Regular audits of Credit divisions' processes are undertaken by Internal Audit.

Notes to the financial statements

4. Financial risk management (continued)

(b) Credit risk (continued)

Exposure to credit risk

<i>In thousands of denars</i>	<i>Note</i>	Loans and advances to customers		Loans and advances to banks		Investment securities	
		2011	2010	2011	2010	2011	2010
Carrying amount	18,17,19	5,781,590	4,485,329	396,947	758,037	167,526	768,870
Individually impaired							
Grade A		-	20,698	-	-	-	-
Grade B		40,764	53,319	-	-	-	-
Grade C		18,495	50,895	-	-	-	-
Grade D		11,433	22,003	-	-	-	-
Grade E		221,015	147,302	-	-	-	-
Gross amount		291,707	294,217	-	-	-	-
Allowance for impairment		(181,141)	(170,302)	-	-	-	-
Carrying amount		110,566	123,915	-	-	-	-
Past due but not impaired:							
<i>Past due comprises:</i>							
up to 30 days		28,713	97,491	-	-	-	-
30-60 days		326,457	14,335	-	-	-	-
60-90 days		168,804	7,901	-	-	-	-
90-180 days		42,722	19,629	-	-	-	-
180 days+		28,749	47,717	-	-	-	-
Carrying amount		595,445	187,073	-	-	-	-
Neither past due nor impaired:							
Grade A		5,075,579	4,174,341	396,947	758,037	167,526	768,870
Carrying amount		5,075,579	4,174,341	396,947	758,037	167,526	768,870
Total carrying amount		5,781,590	4,485,329	396,947	758,037	167,526	768,870

Impaired loans and securities

Impaired loans and securities are loans and securities for which the Bank determines that it is probable that it will be unable to collect part or all of the principal and interest due according to the contractual terms of the loan / securities agreement(s). These loans are graded A to E in the Bank's internal credit risk grading system.

Past due but not impaired loans

Loans and securities where contractual interest or principal payments are past due but the Bank believes that impairment is not appropriate on the basis of the level of security / collateral available and / or the stage of collection of amounts owed to the Bank.

Notes to the financial statements

4. Financial risk management (continued)

(b) Credit risk (continued)

Allowances for impairment

The Bank establishes an allowance for impairment losses that represents its estimate of incurred losses in its loan portfolio. The main components of this allowance are a specific loss component that relates to individually significant exposures, and a collective loan loss allowance established for groups of homogeneous assets in respect of losses that have been incurred but have not been identified on loans subject to individual assessment for impairment.

Write-off policy

The Bank writes off a loan / security balance (and any related allowances for impairment) when the Supervisory Board determines that the loans / securities are uncollectible. This determination is reached after considering information such as the occurrence of significant changes in the borrower / issuer's financial position such that the borrower / issuer can no longer pay the obligation, or that proceeds from collateral will not be sufficient to pay back the entire exposure. The Bank can also write off a loan / security balance (and any related allowances for impairment) on the base of a court decision when all other means for collection had expired.

Set out below is an analysis of the gross and net (of allowances for impairment) amounts of individually impaired assets by risk grade.

<i>In thousands of denars</i>	Loans and advances to customers	
	Gross	Net
31 December 2011		
Individually impaired		
Grade A	-	
Grade B	40,764	35,833
Grade C	18,495	12,028
Grade D	11,433	4,439
Grade E	221,015	58,266
Total	<u>291,707</u>	<u>110,566</u>
31 December 2010		
Individually impaired		
Grade A	20,698	19,278
Grade B	53,319	47,612
Grade C	50,895	36,862
Grade D	22,003	10,781
Grade E	147,302	9,382
Total	<u>294,217</u>	<u>123,915</u>

Notes to the financial statements

4. Financial risk management (continued)

(b) Credit risk (continued)

The Bank holds collateral against loans and advances to customers in the form of mortgage interests over property, other registered securities over assets, and guarantees. Estimates of fair value are based on the value of collateral assessed at the time of borrowing. Collateral generally is not held over loans and advances to banks. Collateral usually is not held against investment securities, and no such collateral was held at 31 December 2010 or 2009.

An estimate of the fair value of collateral and other security enhancements held against loans and advances to customers is shown below:

<i>In thousands of denars</i>	Loans and advances to customers	
	2011	2010
Cash collateral	89,661	94,461
Apartments	3,329,561	2,583,907
Business premises	3,949,782	3,329,680
Moveable lien	1,211,530	1,576,507
Other	457,457	519,067
	<u>9,037,991</u>	<u>8,103,622</u>

Details of financial and non-financial assets obtained by the Bank during the year by taking possession of collateral held as security against loans and advances as well as calls made on credit enhancements and held at the year end are shown below:

<i>In thousands of denars</i>	2011	2010
Land	24,922	-
Apartments	3,998	-
Business premises	2,953	5,139
Other	7,143	1,275
	<u>39,016</u>	<u>6,414</u>

The Bank's policy is to pursue timely realisation of the collateral in an orderly manner.

Notes to the financial statements

4. Financial risk management (continued)

(b) Credit risk (continued)

The Bank monitors concentrations of credit risk by sector and by geographic location. An analysis of concentrations of credit risk at the reporting date is shown below:

<i>In thousands of denars</i>	<i>Note</i>	Loans and advances to banks		Loans and advances to customers		Investment securities	
		2011	2010	2011	2010	2011	2010
Carrying amount	18,17,19	396,947	758,037	5,781,590	4,485,329	167,526	768,870
Concentration by sector							
Corporate		-	-	2,773,191	2,464,585	33,730	30,994
Public sector		-	-	-	-	133,796	737,876
Bank		396,947	758,037	-	-	-	-
Retail		-	-	3,008,399	2,020,744	-	-
		<u>396,947</u>	<u>758,037</u>	<u>5,781,590</u>	<u>4,485,329</u>	<u>167,526</u>	<u>768,870</u>
Concentration by location							
EU countries		396,947	746,553	-	-	4,555	-
Other European countries		-	-	-	122,893	-	-
USA		-	11,484	-	-	-	-
Republic of Macedonia		-	-	5,781,590	4,362,436	162,971	768,870
		<u>396,947</u>	<u>758,037</u>	<u>5,781,590</u>	<u>4,485,329</u>	<u>167,526</u>	<u>768,870</u>

Concentration by location for loans and advances is measured based on the location of the borrower. Concentration by location for investment securities is measured based on the location of the issuer of the security.

Trading assets

The Bank's trading assets are comprised of debt securities – government bonds of the Republic of Macedonia of MKD 174,422 thousand at 31 December 2011 (2010: government bonds of MKD 178,895 thousand).

An analysis of the credit quality of the maximum credit exposure, is as follows:

<i>In thousands of denars</i>	2011	2010
Government bonds	174,422	178,895
Treasury bills	-	-
Government bills	-	-
Fair value and carrying amount	<u>174,422</u>	<u>178,895</u>

The Bank considers that the trading portfolio is with high quality as all investments included in trading assets are issued by the government and are low risk securities.

The Bank does not require collateral for investment in securities.

Notes to the financial statements

4. Financial risk management (continued)

(b) Credit risk (continued)

Settlement risk

The Bank's activities may give rise to risk at the time of settlement of transactions and trades. Settlement risk is the risk of loss due to the failure of an entity to honour its obligations to deliver cash, securities or other assets as contractually agreed.

For certain types of transactions the Bank mitigates this risk through broker clearing agent to ensure that a trade is settled only when both parties have fulfilled their contractual settlement obligations.

Cash and cash equivalents

The Bank held cash and cash equivalents of MKD 996,451 thousand at 31 December 2011 (2010: MKD 986,600 thousand) which represents its maximum credit exposure on these assets. The cash and cash equivalents are held with the central bank, domestic banks and foreign financial institution counterparties which are rated BBB - to AA, based on rating agency Standard&Poor's ratings.

(c) Liquidity risk

Liquidity risk is the risk that the Bank will encounter difficulty in meeting obligations associated with its financial liabilities that are settled by delivering cash or another financial asset.

Management of liquidity risk

The Bank's approach to managing liquidity is to ensure, as far as possible, that it will always have sufficient liquidity to meet its liabilities when due, under both normal and stressed conditions, without incurring unacceptable losses or risking damage to the Bank's reputation.

Assets, Liability and Payment Division receive information from other departments regarding the liquidity profile of their financial assets and liabilities and details of other projected cash flows arising from projected future business. Assets, Liability and Payment Division then maintain a portfolio of short-term liquid assets, largely made up of short-term liquid investment securities, loans and advances to banks and other inter-bank facilities, to ensure that sufficient liquidity is maintained within the Bank.

The daily liquidity position and market conditions are regularly monitored. All liquidity policies and procedures are subject to review and approval by ALCO. Daily reports cover the liquidity position of the Bank. Liquidity reports are submitted monthly to the NBRM.

Notes to the financial statements

4. Financial risk management (continued)

(c) Liquidity risk (continued)

Exposure to liquidity risk

The Bank has access to a diverse funding base. Funds are raised using a broad range of instruments including deposits, borrowed funds and share capital. This enhances funding flexibility, limits dependence on any one source of funds and generally lowers the cost of funds. The Bank strives to maintain a balance between continuity of funding and flexibility through the use of liabilities with a range of maturities. The Bank continually assesses liquidity risk by identifying and monitoring changes in funding required meeting business goals and targets set in terms of the overall Bank strategy.

In addition the Bank holds a portfolio of liquid assets as part of its liquidity risk management strategy.

Residual contractual maturities of financial liabilities

<i>In thousands of denars</i>	<i>Note</i>	Carrying amount	Gross nominal inflow / (outflow)	Less than 1 month	1-3 months	3 months to 1 year	1-5 years	More than 5 years
31 December 2011								
<i>Non-derivative liabilities</i>								
Deposits from banks	23	10,238	(10,238)	(9,612)	-	(626)	-	-
Deposits from customers	24	5,478,398	(5,478,398)	(2,993,168)	(825,976)	(1,181,516)	(475,197)	(2,541)
Other borrowed funds	25	1,429,258	(1,429,258)	(286,036)	(28,478)	(147,990)	(601,283)	(365,471)
Other liabilities	27	92,958	(92,958)	(78,053)	(14,905)	-	-	-
Unrecognised loan commitments		240,354	(240,354)	(240,354)	-	-	-	-
		<u>7,251,206</u>	<u>(7,251,206)</u>	<u>(3,607,223)</u>	<u>(869,359)</u>	<u>(1,330,132)</u>	<u>(1,076,480)</u>	<u>(368,012)</u>
31 December 2010								
<i>Non-derivative liabilities</i>								
Deposits from banks	23	630,845	(630,845)	(15,795)	-	(615,050)	-	-
Deposits from customers	24	4,488,934	(4,488,934)	(2,076,375)	(916,375)	(1,143,214)	(352,970)	-
Other borrowed funds	25	1,797,604	(1,797,604)	(56,130)	(160,777)	(267,120)	(833,840)	(479,737)
Other liabilities	27	81,794	(81,794)	(81,794)	-	-	-	-
Unrecognised loan commitments		251,735	(251,735)	(251,735)	-	-	-	-
		<u>7,250,912</u>	<u>(7,250,912)</u>	<u>(2,481,829)</u>	<u>(1,077,152)</u>	<u>(2,025,384)</u>	<u>(1,186,810)</u>	<u>(479,737)</u>

The previous table shows the undiscounted cash flows on the Bank's financial liabilities and unrecognised loan commitments on the basis of their earliest possible contractual maturity. The Bank's expected cash flows on these instruments vary significantly from this analysis. For example, demand deposits from customers are expected to maintain a stable or increasing balance and unrecognised loan commitments are not all expected to be drawn down immediately.

The gross nominal inflow / (outflow) disclosed in the previous table is the contractual, undiscounted cash flow on the financial liability or commitment.

Notes to the financial statements

4. Financial risk management (continued)

(c) Liquidity risk (continued)

To manage the liquidity risk arising from financial liabilities, the Bank holds liquid assets comprising cash and cash equivalents and investment securities for which there is an active and liquid market. These assets can be readily sold to meet liquidity requirements. Hence, the Bank believes that it is not necessary to disclose a maturity analysis in respect of these assets to enable users to evaluate the nature and extent of liquidity risk.

(d) Market risks

Market risk is the risk that changes in market prices, such as interest rate, equity prices, foreign exchange rates and credit spreads (not relating to changes in the obligor's / issuer's credit standing) will affect the Bank's income or the value of its holdings of financial instruments. The objective of market risk management is to manage and control market risk exposures within acceptable parameters, while optimising the return on risk.

Management of market risks

Excess of the liquidity the Bank is placing in high yielding instruments that according to the Central bank regulation are considered as placements with no risk. The Bank separates its exposure to market risk between trading and non-trading portfolios. Trading portfolios are held by the Treasury Front Office. Treasury Front Office daily follows the price movement of the quoted instruments and for adverse market movement, Board of Directors of the Bank, is instantaneously informed. In this process the Parent's support in terms of providing information on international market movements and developments is also utilized.

Assets and liabilities committee (ALCO) which holds a meeting every week is platform where market risks are analyzed and decisions are made at the operational level. ALCO performs analyses and makes decisions with regard to balance sheet structure, liquidity risk, currency risk and also is analyzing the risk of the Bank's treasury unit.

Exposure to market risks – trading portfolios

The Bank focuses on the real and potential sensitiveness of the separate positions in the portfolio as well as the total portfolio. The Bank uses internal calculation methods and stress-testing on the potential market risk exposure. Trading limits are used for daily risk management and every limits are monitored by the Risk Management Department and reported to the Board of directors of the Bank.

The principal tool used to control and measure market risk exposure within the Bank's trading portfolios is performing sensitivity analyses. By performing sensitivity analyses the Bank is making estimation of the loss that might arise on the portfolio from an adverse market movement. Sensitivity analyses that are performed are based mainly on historical simulation. The rules that are applied for performing the sensitivity analyses are:

Notes to the financial statements

4. Financial risk management (continued)

(d) Market risks (continued)

- Price volatility (in absolute terms over previous number of days)
- Previous trading range (price high/low over previous number of days)
- Maximum/minimum price changes (over previous number of days)
- Price volatility correlation to P&L, internal and regulatory ratios and indicators

In order for the Bank to estimate the effect of potential volatility in the price of the securities in the trading portfolio, using the portfolio data as of 31 December 2010, hypothetical stress-test scenario analyses were performed, based on assumptions for shock changes in their price.

Under first scenario there is 10% instantaneous change in the price and results are respectively shown in the following table:

Sensitivity of prices of securities in trading portfolio

	Profit / loss for the period <i>(Effect in thousands of denars)</i>	Capital ratio <i>(effect in %)</i>
2011		
Net trading income (10% increase in the market price)	17,115	0.45
Net trading income (10% decrease in the market price)	(17,115)	(0.45)

Under second, more conservative scenario there is 20% instantaneous change in the price and results are respectively shown in the following table:

Sensitivity of prices of securities in trading portfolio

	Profit / loss for the period <i>(Effect in thousands of denars)</i>	Capital ratio <i>(effect in %)</i>
2011		
Net trading income (20% increase in the market price)	34,231	0.91
Net trading income (20% decrease in the market price)	(34,231)	(0.91)

In both scenarios the Capital ratio is above the prescribed limit of 8%.

Notes to the financial statements

4. Financial risk management (continued)

(d) Market risks (continued)

Exposure to interest rate risk – non-trading portfolios

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 repricing at different times or/and 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, such as the savings rate, LIBOR and different types of interest.

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. In general, the Bank is asset sensitive because of the majority of the interest-earning assets and liabilities, the Bank has the right simultaneously to change the interest rates. However the actual effect will depend on various factors, including stability of the economy, environment and level of the inflation.

Notes to the financial statements

4. Financial risk management (continued)

(d) Market risks (continued)

A summary of the Bank's interest rate gap position on non-trading portfolios is as follows:

<i>In thousands of denars</i>	<i>Note</i>	Carrying amount	Less than 1 month	1- 3 months	3-12 months	1-5 years	More than 5 years
31 December 2011							
Cash and cash equivalents	15	2,174,409	2,174,409	-	-	-	-
Loans and advances to banks	17	396,947	396,947	-	-	-	-
Loans and advances to customers	18	5,781,590	326,488	1,318,607	434,065	2,973,075	729,355
Investment securities	19	167,526	44,516	-	-	123,010	-
		<u>8,520,472</u>	<u>2,942,360</u>	<u>1,318,607</u>	<u>434,065</u>	<u>3,096,085</u>	<u>729,355</u>
Deposits from banks and other financial institutions	23	(10,238)	(9,628)	-	(610)	-	-
Deposits from customers	24	(5,478,398)	(3,035,703)	(824,316)	(1,143,757)	(472,107)	(2,515)
Other borrowed funds	25	(1,429,258)	(135,550)	(338,415)	(588,651)	(359,056)	(7,586)
		<u>(6,917,894)</u>	<u>(3,180,881)</u>	<u>(1,162,731)</u>	<u>(1,733,018)</u>	<u>(831,163)</u>	<u>(10,101)</u>
		<u>1,602,578</u>	<u>(238,521)</u>	<u>155,876</u>	<u>(1,298,953)</u>	<u>2,264,922</u>	<u>719,254</u>
31 December 2010							
Cash and cash equivalents	15	986,600	640,218	-	18,987	327,395	-
Loans and advances to banks	17	758,037	758,037	-	-	-	-
Loans and advances to customers	18	4,485,329	232,962	278,015	1,357,869	2,141,120	475,363
Investment securities	19	768,870	31,037	548,993	49,601	139,239	-
		<u>6,998,836</u>	<u>1,662,254</u>	<u>827,008</u>	<u>1,426,457</u>	<u>2,607,754</u>	<u>475,363</u>
Deposits from banks and other financial institutions	23	(630,845)	(15,795)	-	(615,050)	-	-
Deposits from customers	24	(4,488,934)	(2,076,375)	(916,375)	(1,143,214)	(352,970)	-
Other borrowed funds	25	(1,797,604)	(10,481)	(267,018)	(1,340,756)	(179,349)	-
		<u>(6,917,383)</u>	<u>(2,102,651)</u>	<u>(1,183,393)</u>	<u>(3,099,020)</u>	<u>(532,319)</u>	<u>-</u>
		<u>81,453</u>	<u>(440,397)</u>	<u>(356,385)</u>	<u>(1,672,563)</u>	<u>2,075,435</u>	<u>475,363</u>

The management of interest rate risk against interest rate gap limits is supplemented by monitoring the sensitivity of the Bank's financial assets and liabilities to various standard and non-standard interest rate scenarios. Standard scenarios include a 1% parallel fall or rise in all yield curves.

Notes to the financial statements

4. Financial risk management (continued)

(d) Market risks (continued)

An analysis of the Bank's sensitivity to an increase or decrease in market interest rates (assuming no asymmetrical movement in yield curves and a constant balance sheet position) is as follows:

<i>Effect in thousands of denars</i>	Profit / loss for the period
2011	
Interest income (1% increase)	64,046
Interest income (1% decrease)	64,046
Interest expense (1% increase)	(27,449)
Interest expense (1% decrease)	(27,449)
2010	
Interest income (1% increase)	26,762
Interest income (1% decrease)	(26,762)
Interest expense (1% increase)	(15,132)
Interest expense (1% decrease)	15,132

Exposure to currency risk – non-trading portfolios

The Bank is exposed to currency risk through transactions in foreign currencies. The Bank ensures that the net exposure is kept to an acceptable level by buying or selling foreign currency at spot when necessary to address short-term imbalances. The Denar is pegged to the Euro and the monetary projections envisage stability of the exchange rate of the Denar against Euro.

Notes to the financial statements

4. Financial risk management (continued)

(d) Market risks (continued)

The Bank's exposure to foreign currency risk for non-trading portfolio is as follows:

In thousands of denars

	2011					2010				
	MKD	EUR	USD	Other	Total	MKD	EUR	USD	Other	Total
Monetary assets										
Cash and cash equivalents	1,704,525	324,458	73,429	71,997	2,174,409	553,756	363,932	37,342	31,570	986,600
Loans and advances to banks	-	377,835	119,112	-	396,947	-	689,531	68,506	-	758,037
Loans and advances to customers	2,792,004	2,988,746	840	-	5,781,590	1,939,512	2,545,817	-	-	4,485,329
Investment securities	29,221	133,796	4,509	-	167,526	575,283	189,149	4,438	-	768,870
Other assets	171,937	38,035	3,023	-	212,995	149,995	36,830	2,112	-	188,937
	<u>4,697,687</u>	<u>3,862,870</u>	<u>200,913</u>	<u>71,997</u>	<u>8,733,467</u>	<u>3,218,546</u>	<u>3,825,259</u>	<u>112,398</u>	<u>31,570</u>	<u>7,187,773</u>
Monetary liabilities										
Deposits from banks	657	8,345	1,211	25	10,238	612	629,251	982	-	630,845
Deposits from customers	3,401,762	1,914,935	90,797	70,904	5,478,398	2,836,364	1,521,559	101,304	29,707	4,488,934
Other borrowed funds	23,571	1,405,688	-	-	1,429,259	25,457	1,772,147	-	-	1,797,604
Other liabilities	76,238	16,326	48	347	92,959	73,909	6,790	851	244	81,794
	<u>3,502,228</u>	<u>3,345,294</u>	<u>92,056</u>	<u>71,276</u>	<u>7,010,854</u>	<u>2,936,342</u>	<u>3,929,747</u>	<u>103,137</u>	<u>29,951</u>	<u>6,999,177</u>
Net position	<u>1,195,459</u>	<u>517,576</u>	<u>108,857</u>	<u>721</u>	<u>1,722,613</u>	<u>282,204</u>	<u>(104,488)</u>	<u>9,261</u>	<u>1,619</u>	<u>188,596</u>
Commitments and contingencies	(383,136)	(9,774)	(66,334)	-	(459,244)	(376,238)	(67,885)	-	-	(444,123)
Net FX position	<u>812,323</u>	<u>507,802</u>	<u>42,523</u>	<u>721</u>	<u>1,263,369</u>	<u>(94,034)</u>	<u>(172,373)</u>	<u>9,261</u>	<u>1,619</u>	<u>(255,527)</u>

Notes to the financial statements

4. Financial risk management (continued)

(e) Operational risk

Operational risk is risk of loss due to inappropriate or weak internal processes, inappropriate persons and inappropriate or weak systems in the Bank as well as external events.

The Bank defined its framework for managing with the operational risk by adopting the Policy and Procedure on operational risk management. Policy and Procedure for Operational Risk Management was adopted by the Supervisory Board of the Bank. In the Policy the basic aims are defined such as operational risk management (system and processes for managing operational risk, organisational structure, reporting system, internal control and etc), as well as measuring and monitoring the operational risk. Implementation of the operational risk management framework is meant to be delivered by performing RCSA (Risk and control self assessment) which is continuous process, and by using the operational loss event database.

Within the strategy for Risk Management, the Bank has defined the acceptable level of exposure to operational risk. The Bank plans to use the basic indicator for operational risk in calculating the capital necessary for covering operational risk.

(e) Capital management

Regulatory capital

The Bank's lead regulator NBRM sets and monitors capital requirements for the Bank as a whole. The Bank is directly supervised by the local regulators.

In implementing capital adequacy requirements NBRM requires the Bank to maintain a prescribed ratio of 8% of own funds to sum of total risk-weighted assets. Total risk-weighted assets are sum of credit risk-weighted assets and sum of capital requirements for currency risk.

Notes to the financial statements

4. Financial risk management (continued)

(e) Capital management (continued)

Bank's own funds are a sum of core capital, supplementary capital, less deductions, as follows:

- Core capital, which includes ordinary and non cumulative preference shares, share premium, bank reserves allocated from net profit that serve for covering losses arising from risks the Bank faces in its operations, retained earnings not encumbered by any future obligations, stated in the balance sheet and confirmed by a Decision of the Bank's Shareholders' Assembly or accumulated loss from previous year, profit for the year if confirmed by the certified auditor, after deductions for loss for the year, licenses, patents, goodwill and other trademarks, treasury shares and the difference between the amount of the required allowance for impairment in accordance with the risk classification and allocated allowance for impairment and allowance for impairment calculated according the Decision for credit risk management.
- Supplementary capital, which includes cumulative preference shares, share premium less the amount of purchased treasury cumulative preference shares, hybrid capital instruments and subordinated liabilities issued by the Bank.
- The total of core capital and supplementary capital is reduced by the Bank's capital investments in banks and financial institutions exceeding 10% of the capital of such institutions, subordinated instruments and other investments in other banks or other financial institutions where the Bank holds more than 10% of the capital and other deductions.

When determining the amount of own funds, the bank shall observe the following restrictions:

- The amount of the supplementary capital cannot exceed the amount of the core capital.
- The sum of the nominal value of subscribed and paid-in ordinary shares, the share premium of such shares and the amount of reserves and the retained earnings, less the deductions from the core capital and supplementary capital previously described, should exceed the sum of other positions which are part of the Bank's core capital.

The amount of subordinated instruments which are part of the supplementary capital is not to exceed 50% of the amount of core capital.

The Bank's policy is to maintain a strong capital base so as to maintain investor, creditor and market confidence and to sustain future development of the business. The impact of the level of capital on shareholders' return is also recognised and the Bank recognises the need to maintain a balance between the higher returns that might be possible with greater gearing and the advantages and security afforded by a sound capital position.

The Bank and its individually regulated operations have complied with all externally imposed capital requirements throughout the period.

There were no significant changes in the Bank's approach to capital management during the year.

As at 31 December 2011 the capital adequacy ratio of the Bank is 29.85% (31 December 2010: 14,05%) and is above the prescribed minimum of 8%.

Notes to the financial statements

5. Key sources of estimation uncertainty

Capital allocation

The allocation of capital between specific operations and activities is, to a large extent, driven by optimisation of the return achieved on the capital allocated. The amount of capital allocated to each operation or activity is based primarily upon the regulatory capital. The process of allocating capital to specific operations and activities is monitored independently of those responsible for the operation and is subject to review by the Supervisory Board.

Allowances for impairment losses on loans and advances

Assets accounted for at amortised cost are assessed for impairment on a basis described in accounting policy 3(h)(vii).

The Bank reviews its loan portfolio to assess impairment at least on a quarterly basis. In determining whether an impairment loss should be recorded in the profit and loss the Bank makes judgments as to whether there is any observable data indicating that there is a measurable decrease in the estimated future cash flows from a portfolio of loans before the decrease can be identified with an individual loan in that portfolio. This evidence may include observable data indicating that there has been adverse change in the payment status of borrowers in a group, or national or local economic conditions that correlate with defaults on assets in a group.

The Bank's Management uses estimates based on historical loss experience for assets with credit risk characteristics and objective evidence of impairment similar to those in the portfolio when scheduling its future cash flows. The methodology and assumptions used for estimating both the amount and timing of future cash flows are reviewed regularly to reduce any differences between loss estimates and actual loss experience.

Collectively assessed impairment allowances cover credit losses inherent in portfolios of loans and advances and held-to-maturity investment securities with similar credit risk characteristics when there is objective evidence to suggest that they contain impaired loans and advances and held-to-maturity investment securities, but the individual impaired items cannot yet be identified. In assessing the need for collective loan loss allowances, management considers factors such as credit quality, portfolio size, concentrations, and economic factors. In order to estimate the required allowance, assumptions are made to define the way inherent losses are modeled and to determine the required input parameters, based on historical experience and current economic conditions. The accuracy of the allowances depends on how well these estimate future cash flows for specific counterparty allowances and the model assumptions and parameters used in determining collective allowances.

Notes to the financial statements

5. Key sources of estimation uncertainty (continued)

Allowance for impairment of available for sale equity investments

The Bank determines that available-for-sale equity investments are impaired when there has been a significant or prolonged decline in the fair value below its cost. This determination of what is significant or prolonged requires judgment. In making this judgment, the Bank evaluates among other factors, the normal volatility in share price. In addition, impairment may be appropriate when there is evidence of deterioration in the financial health of the investee, industry and sector performance, changes in technology, and operational and financing cash flows.

Determining fair values

The determination of fair value for financial assets and liabilities for which there is no observable market price requires the use of valuation techniques as described in accounting policy 3(h)(vi). For financial instruments that trade infrequently and have little price transparency, fair value is less objective, and requires varying degrees of judgement depending on liquidity, concentration, uncertainty of market factors, pricing assumptions and other risks affecting the specific instrument.

Critical accounting judgments in applying the Bank's accounting policies

Critical accounting judgments made in applying the Bank's accounting policies include:

Valuation of financial instruments

The fair value measurements is disclosed in the accounting policy 3(h)(vi).

The Bank measures fair values using the following fair value hierarchy that reflects the significance of the inputs used in making the measurements:

Level 1: Quoted market price (unadjusted) in an active market for an identical instrument;

Level 2: Valuation techniques based on observable inputs, either directly (i.e., as prices) or indirectly (i.e., derived from prices). This category includes instruments valued using: quoted market prices in active markets for similar instruments; quoted prices for identical or similar instruments in markets that are considered less than active; or other valuation techniques where all significant inputs are directly or indirectly observable from market data;

Notes to the financial statements

5. Key sources of estimation uncertainty (continued)

Critical accounting judgments in applying the Bank's accounting policies (continued)

Valuation of financial instruments (continued)

Level 3: Valuation techniques using significant unobservable inputs. This category includes all instruments where the valuation technique includes inputs not based on observable data and the unobservable inputs have a significant effect on the instrument's valuation.

This category includes instruments that are valued based on quoted prices for similar instruments where significant unobservable adjustments or assumptions are required to reflect differences between the instruments.

The table below analyses financial instruments measured at fair value at the end of the reporting period, by the level in the fair value hierarchy into which the fair value measurement is categorised:

<i>In thousands of denars</i>	Note	Level 1	Level 2	Level 3	Total
31 December 2011					
Trading assets	16	174,422	-	-	174,422
Investment securities	19	133,796	-	-	133,796
<hr/>					
31 December 2010					
Trading assets	16	178,895	-	-	178,895
Investment securities	19	139,282	-	-	139,282
<hr/>					
318,177					
<hr/>					

Financial asset and liability classification

The Bank may designate financial assets and liabilities on inception into different accounting categories in certain circumstances:

- In classifying financial assets as “trading”, the Bank has determined that it meets the definition of financial assets held for trading.
- In designating financial assets or liabilities at fair value through profit or loss, the Bank has determined that it has met one of the criteria for this designation.
- In classifying financial assets as held-to-maturity, the Bank has determined that it has both the positive intention and ability to hold the assets until their maturity date.

Details of the Bank's classification of financial assets and liabilities are given in note 7.

Notes to the financial statements

6. Operating segments

The Bank has 4 reportable segments, as described below, which are the Bank's strategic business units. The strategic business units offer different products and services, and are managed separately based on the Bank's management and internal reporting structure. For each of the strategic business units, the Managing Board reviews internal management reports. The following summary describes the operations in each of the Bank's reportable 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
- Investment Banking - Includes the Bank's trading and investment finance activities
- Treasury - Undertakes the Bank's funding and centralized risk management activities through investing in liquid assets such as short-term placements and government debt securities.

Information regarding the results of each reportable segment is included below. Performance is measured based on segment profit before income tax. Segment profit is used to measure performance as management believes that such information is the most relevant in evaluating the results of certain segments relative to other entities that operate within these industries.

Notes to the financial statements

6. Operating segments (continued)

Information about operating segments

2011

<i>In thousands of denars</i>	Investment Banking	Corporate Banking	Retail Banking	Central Treasury	Unallocated	Total
External revenue						
Net interest income	40,120	127,230	155,641	(9,150)	-	313,841
Net fee and commission income/(expense)	-	27,439	52,517	(9,882)	-	70,074
Net trading income	7,012	-	-	-	-	7,012
Other operating income	2,916	35,408	3,769	-	17,018	59,111
Total segment revenue	<u>50,048</u>	<u>190,077</u>	<u>211,927</u>	<u>(19,032)</u>	<u>17,018</u>	<u>450,038</u>
Other material non- cash items:						
Impairment losses on financial assets	-	11,278	12,455	-	-	23,733
Reportable segment profit before income tax	<u>50,048</u>	<u>178,799</u>	<u>199,472</u>	<u>(19,032)</u>	<u>17,018</u>	<u>426,305</u>
Reportable segment assets	1,486,643	3,658,765	2,981,460	1,323,783	-	9,450,650
Reportable segment liabilities	-	2,760,792	3,031,300	1,221,031	-	7,013,123

Notes to the financial statements

6. Operating segments (continued)

Information about operating segments (continued)

2010

<i>In thousands of denars</i>	Investment Banking	Corporate Banking	Retail Banking	Central Treasury	Total
External revenue					
Net interest income	48,757	88,757	43,579	5,729	186,822
Net fee and commission income	(37)	52,026	14,406	-	66,395
Net trading income	27,132	-	-	-	27,132
Other operating income	-	2,830	-	-	2,830
Total segment revenue	<u>75,852</u>	<u>143,613</u>	<u>57,985</u>	<u>5,729</u>	<u>283,179</u>
Other material non-cash items:					
Impairment losses on financial assets	-	21,012	4,785	-	25,797
Reportable segment profit before income tax	<u>75,852</u>	<u>138,784</u>	<u>55,191</u>	<u>5,729</u>	<u>275,556</u>
Reportable segment assets	1,719,692	2,318,920	2,163,159	947,724	7,149,495
Reportable segment liabilities	-	3,412,759	2,893,825	-	6,306,584

Notes to the financial statements

6. Operating segments (continued)

Information about operating segments (continued)

Reconciliations of reportable segment revenues, profit or loss and assets and liabilities

<i>In thousands of denars</i>	2011	2010
Revenues		
Total revenue for reportable segments	433,020	283,179
Unallocated amounts	17,018	33,685
Revenue	<u>450,038</u>	<u>316,864</u>
Profit or loss		
Total profit or loss for reportable segments	437,205	275,556
Unallocated amounts:		
Depreciation and amortisation	(71,069)	(76,922)
Other	(346,402)	(290,350)
Profit before income tax	<u>19,734</u>	<u>(91,716)</u>
Assets		
Total assets for reportable segments	9,450,650	7,149,495
Other unallocated amounts	-	823,134
Total assets	<u>9,450,650</u>	<u>7,972,629</u>
Liabilities		
Total liabilities for reportable segments	7,013,123	6,306,584
Other unallocated amounts	-	712,620
Total liabilities	<u>7,013,123</u>	<u>7,019,204</u>

Notes to the financial statements

6. Operating segments (continued)

Information about operating segments (continued)

Geographical areas

In presenting information on the basis of geographical areas, revenue is based on the geographical location of customers and assets are based on geographical location of the assets.

Geographical information

<i>In thousands of denars</i>	Republic of Macedonia	Europe	Other	Total
2011				
External revenues	450,714	6,256	(6,932)	450,038
Non-current assets*	542,761	-	-	542,761
2010				
External revenues	318,629	(5,586)	3,821	316,864
Non-current assets*	605,961	-	-	605,961

* Includes property and equipment and intangibles assets

Notes to the financial statements

7. Financial assets and liabilities

Accounting classifications and fair values

The table below sets out the carrying amount and fair values of the Bank's financial assets and financial liabilities:

<i>In thousands of denars</i>	<i>Note</i>	Trading	Held-to-maturity	Loans and receivables	Available-for-sale	Other amortised cost	Total carrying amount	Fair value
31 December 2011								
Cash and cash equivalents	15		1,177,958	996,451	-	-	2,174,409	2,174,409
Trading assets	16	174,422	-	-	-	-	174,422	174,422
Loans and advances to banks	17	-	-	396,947	-	-	396,947	396,947
Loans and advances to customers	18	-	-	5,781,590	-	-	5,781,590	5,781,590
Investment securities								
Measured at fair value	19	-	-	-	167,526	-	167,526	167,526
Other assets	22	-	-	212,995	-	-	212,995	212,995
		174,422	1,177,958	7,387,983	167,526	-	8,907,889	8,907,889
Deposits from banks	23	-	-	-	-	10,238	10,238	10,238
Deposits from customers	24	-	-	-	-	5,478,398	5,478,398	5,478,398
Other borrowed funds	25	-	-	-	-	1,429,259	1,429,259	1,429,259
Other liabilities	27	-	-	-	-	92,958	92,958	92,958
		-	-	-	-	7,010,853	7,010,853	7,010,853
31 December 2010								
Cash and cash equivalents	15	-	-	986,600	-	-	986,600	986,600
Trading assets	16	178,895	-	-	-	-	178,895	178,895
Loans and advances to banks	17	-	-	758,037	-	-	758,037	758,037
Loans and advances to customers:	18	-	-	4,485,329	-	-	4,485,329	4,485,329
Investment securities:								
Measured at fair value	19	-	-	-	219,877	-	219,877	219,877
Measured at amortised cost	19	-	548,993	-	-	-	548,993	548,993
Other assets	22	-	-	86,700	-	-	86,700	86,700
		178,895	548,993	6,316,666	219,877	-	7,264,431	7,264,431
Deposits from banks	23	-	-	-	-	630,845	630,845	630,845
Deposits from customers	24	-	-	-	-	4,488,934	4,488,934	4,488,934
Other borrowed funds	25	-	-	-	-	1,797,604	1,797,604	1,797,604
Other liabilities	27	-	-	-	-	81,794	81,794	81,794
		-	-	-	-	6,999,177	6,999,177	6,999,177

Notes to the financial statements

7. Financial assets and liabilities (continued)

Investment securities – unquoted equity securities at cost

The above table includes MKD 33,730 thousand (2010: MKD 30,994 thousand) of equity investment securities in both the carrying amount and fair value columns that are measured at cost and for which disclosure of fair value is not provided because their fair value cannot be reliably measured. According to the Bank's management fair value do not differ significantly from the carrying amount and it is not cost effective to carry out independent valuation.

8. Net interest income

<i>In thousands of denars</i>	2011	2010
Interest income		
Cash and cash equivalents	9,818	7,904
Loans and advances to banks	5,330	7,140
Loans and advances to customers	501,585	355,157
Investment securities	40,634	48,785
Total interest income	<u>557,367</u>	<u>418,986</u>
Interest expense		
Deposits from banks	17,124	16,129
Deposits from customers	159,201	164,679
Other borrowed funds	67,201	51,356
Other	-	-
Total interest expense	<u>243,526</u>	<u>232,164</u>
Net interest income	<u>313,841</u>	<u>186,822</u>

Notes to the financial statements

9. Net fee and commission income

<i>In thousands of denars</i>	2011	2010
Fee and commission income		
Credit related fees	9,162	5,481
Payment operations in the country	33,262	28,977
Payment operations abroad	37,778	30,826
Letters of credit and guarantees	3,102	1,682
Other	36,010	28,947
Total fee and commission income	<u>119,314</u>	<u>95,913</u>
Fee and commission expense		
Credit related fees	166	415
Payment operations within the country	11,144	9,452
Payment operations abroad	7,305	6,547
Letters of credit and guarantees	188	32
Credit cards operations	-	10,148
Other	30,437	8,755
Total fee and commission expense	<u>49,240</u>	<u>35,349</u>
Net fee and commission income	<u>70,074</u>	<u>60,564</u>

10. Net trading income

<i>In thousands of denars</i>	2011	2010
Interest income	11,484	15,825
Net change in fair value of held-for-trading assets	(4,472)	11,307
	<u>7,012</u>	<u>27,132</u>

11. Other operating income

<i>In thousands of denars</i>	2011	2010
Capital gain on sale of property and equipment	12,774	-
Capital gain on sale of assets acquired through foreclosure procedure	1,270	859
Dividends on available-for-sale equity securities	2,957	2,144
Collection of previously written off receivables	5,239	10,384
Release of impairment provision for court cases	15,329	-
Release of impairment provisions related to off balance sheet items	-	2,952
Other	4,524	12,509
	<u>42,093</u>	<u>28,848</u>

Notes to the financial statements

12. Personnel expenses

In thousands of denars

	2011	2010
Wages and salaries	(119,243)	106,467
Compulsory contributions	(40,934)	37,046
Other staff costs	(14,224)	7,839
	<u>(174,401)</u>	<u>151,352</u>

13. Other expenses

In thousands of denars

	2011	2010
Materials and services	93,953	93,219
Marketing and advertisement costs	32,344	18,502
Insurance premiums of deposits	20,465	16,985
Telecommunications	16,720	16,665
Rents	17,140	15,686
Security expenses	13,295	10,899
Impairment provision for off balance sheet items	459	-
Impairment provision for court cases	-	12,771
Insurance of property and employees	5,641	5,419
Impairment losses on assets acquired through foreclosure procedure	1,668	4,362
Tax on non-deductable expenses	1,988	1,157
Penalties, court and administrative expenses	124	362
Capital losses on sale of assets acquired through foreclosure procedure	-	202
Losses on sale of available for sale securities	-	-
Other	4,770	9,874
	<u>208,567</u>	<u>206,103</u>

Notes to the financial statements

14. Earnings per share

Basic and diluted earnings per share

The calculation of basic and diluted earnings per share at 31 December 2011 was based on the profit attributable to ordinary shareholders of MKD19,734 thousand (2010: MKD 91,716 thousand) and a weighted average number of ordinary shares outstanding of 100,087 (2010: 41,870), calculated as follows:

Profit attributable to ordinary shareholders

<i>In thousands of denars</i>	2011	2010
Net profit /(loss) for the period	19,734	(91,716)
Net profit /(loss) attributable to ordinary shareholders	<u>19,734</u>	<u>(91,716)</u>

Weighted average number of ordinary shares

<i>Number of shares</i>	2011	2010
Issued ordinary shares at 1 January	41,870	41,870
Effect of own shares issued in August	<u>58,217</u>	<u>-</u>
Weighted average number of ordinary shares at 31 December	<u>100,087</u>	<u>41,870</u>

Notes to the financial statements

15. Cash and cash equivalents

<i>In thousands of denars</i>	2011	2010
Cash on hand	129,025	116,581
Balances with the National Bank of Republic of Macedonia	719,454	801,445
Current accounts with foreign banks	147,953	49,528
Current accounts with local banks	19	59
Treasury bills	1,177,958	-
Restricted deposits	-	18,987
	<u>2,174,409</u>	<u>986,600</u>

At 31 December 2011 cash and cash equivalents included MKD 421,126 thousand (2010: MKD 330,940 thousand) as obligatory reserve requirement in MKD and MKD 284,240 thousand (2010: MKD 327,395 thousand) as obligatory reserve in foreign currency requirement. Funds from obligatory reserve in foreign currency are not available for the Bank's daily business.

The restricted deposits in 2010 include deposit placed in Detsche Bank AG in the amount of MKD 7,972 thousand as collateral for transactions performed with MASTER payment cards and deposit placed in Raiffeisen Zentralbank Oesterreich AG in the amount of MKD 10,834 thousand as collateral for transactions performed with VISA payment cards. These funds are not available for the Bank's daily business.

16. Trading assets

<i>In thousands of denars</i>	2011	2010
Government bonds	<u>174,422</u>	<u>178,895</u>
	<u>174,422</u>	<u>178,895</u>

Notes to the financial statements

17. Loans and advances to banks

<i>In thousands of denars</i>	2011	2010
Loans and advances to foreign banks	394,487	751,850
Restricted loans and advances to foreign banks	2,460	6,187
	<u>396,497</u>	<u>758,037</u>

18. Loans and advances to customers

<i>In thousands of denars</i>	2011	2010
Loans and advances to customers at amortised cost	5,781,590	4,485,329
	<u>5,781,590</u>	<u>4,485,329</u>

At 31 December 2011 MKD 3,702,430 thousand (2010: MKD 2,616,482 thousand) of loans and advances to customers are expected to be recovered more than 12 months after the reporting date.

Loans and advances to customers at amortised cost

<i>In thousands of denars</i>	2011	2010
Retail customers:		
Mortgage lending	315,536	280,915
Consumer loans	2,238,765	1,536,218
Credit cards	269,673	260,267
Other	305,136	115,226
Corporate customers	<u>2,833,621</u>	<u>2,463,009</u>
		4,655,635
Less allowances for impairment	<u>(181,141)</u>	<u>(170,306)</u>
Total loans and advances to customers	<u>5,781,590</u>	<u>4,485,329</u>

Notes to the financial statements

18. Loans and advances to customers (continued)

<i>In thousands of denars</i>	2011	2010
Specific allowances for impairment		
Balance at 1 January	170,306	171,463
Impairment loss for the year recognised in the income statement		
Charge for the year	5,422	-
Recoveries	-	(28,486)
Calculated penalty interest	5,402	27,329
Write-offs	-	-
Balance at 31 December	<u>181,130</u>	<u>170,306</u>

19. Investment securities

<i>In thousands of denars</i>	2011	2010
Available-for-sale investment securities	167,526	219,877
Held-to-maturity investment securities	-	548,993
	<u>167,526</u>	<u>768,870</u>

Held-to-maturity investment securities

<i>In thousands of denars</i>	2011	2010
Treasury Bills	-	548,993
	<u>-</u>	<u>548,993</u>

Available-for-sale investment securities

<i>In thousands of denars</i>	2011	2010
Government Bonds	133,796	139,282
Government Bills	-	49,601
Unquoted equity securities at cost	33,730	30,994
	<u>167,526</u>	<u>219,877</u>

Notes to the financial statements

20. Property and equipment

<i>In thousands of denars</i>	Buildings	Furniture and equipment	Assets under construction	Leasohold improvements	Total
Cost					
Balance at 1 January 2010	500,566	268,362	-	-	768,928
Acquisitions	599	14,445	-	-	15,044
Disposals	-	(9,110)	-	-	(9,110)
Balance at 31 December 2010	<u>501,165</u>	<u>273,697</u>	<u>-</u>	<u>-</u>	<u>774,862</u>
Balance at 1 January 2011	501,165	273,697	-	-	774,862
Acquisitions	612	5,809	19,095	5,765	31,284
Disposals	(30,588)	(7,912)	-	-	(38,500)
Balance at 31 December 2011	<u>471,189</u>	<u>271,594</u>	<u>19,095</u>	<u>5,765</u>	<u>767,643</u>
Depreciation					
Balance at 1 January 2010	35,834	144,223	-	-	180,057
Depreciation for the period	12,522	41,692	-	-	54,214
Disposals	-	(8,420)	-	-	(8,420)
Balance at 31 December 2010	<u>48,356</u>	<u>177,495</u>	<u>-</u>	<u>-</u>	<u>225,851</u>
Balance at 1 January 2011	48,356	177,495	-	-	225,851
Depreciation for the period	12,081	36,761	-	-	48,842
Disposals	(6,346)	(6,981)	-	-	(13,327)
Other transfers	-	227	-	1,180	1,407
Balance at 31 December 2011	<u>54,091</u>	<u>207,500</u>	<u>-</u>	<u>1,180</u>	<u>262,771</u>
Carrying amounts					
Balance at 1 January 2010	<u>464,732</u>	<u>124,139</u>	<u>-</u>	<u>-</u>	<u>588,871</u>
Balance at 31 December 2010	<u>452,809</u>	<u>96,202</u>	<u>-</u>	<u>-</u>	<u>549,011</u>
Balance at 31 December 2011	<u>417,097</u>	<u>64,095</u>	<u>19,095</u>	<u>4,585</u>	<u>504,872</u>

There were no capitalised borrowing costs related to the acquisition of property and equipment during the year (2010: nil).

As at 31 December 2011 the Bank does not hold property deeds for part of the buildings with carrying amount MKD 1,171 thousand (2010: MKD 25,153 thousand). The Bank is in process of obtaining the necessary documents.

As at 31 December 2011 the Bank does not have any property pledged as collateral (2010: none).

Notes to the financial statements

20. Property and equipment (continued)

Operating leases

The Bank leases business premises under operating leases. The leases are cancellable and typically run for a period of up to 5 years.

21. Intangible assets

<i>In thousands of denars</i>	Software	Rights and licences	Assets under development	Total
Cost				
Balance at 1 January 2010	62,623	41,941	-	104,564
Acquisitions	14,268	488	-	14,756
Balance at 31 December 2010	<u>76,891</u>	<u>42,429</u>	<u>-</u>	<u>119,320</u>
Balance at 1 January 2011	76,891	42,429	-	119,320
Acquisitions	1,955	1,211	-	3,166
Balance at 31 December 2011	<u>78,846</u>	<u>43,640</u>	<u>-</u>	<u>122,486</u>
Amortisation				
Balance at 1 January 2010	16,924	22,738	-	39,662
Amortisation for the period	13,904	8,804	-	22,708
Balance at 31 December 2010	<u>30,828</u>	<u>31,542</u>	<u>-</u>	<u>62,370</u>
Balance at 1 January 2011	30,828	31,542	-	62,370
Amortisation for the period	15,959	6,268	-	22,227
Balance at 31 December 2011	<u>46,787</u>	<u>37,810</u>	<u>-</u>	<u>84,597</u>
Carrying amounts				
Balance at 1 January 2010	45,699	19,203	-	64,901
Balance at 31 December 2010	<u>46,063</u>	<u>10,887</u>	<u>-</u>	<u>56,950</u>
Balance at 31 December 2011	<u>32,059</u>	<u>5,830</u>	<u>-</u>	<u>37,889</u>

Notes to the financial statements

22. Other assets

<i>In thousands of denars</i>	2011	2010
Asset acquired through foreclosure procedure	128,774	102,237
Prepayments	12,075	12,484
Trade receivables	1,376	1,578
Inventories	3,166	3,894
Numismatic collections	3,201	3,201
Fee and commission receivables	3,316	3,089
Receivables upon performed transactions - Western Union	3,048	2,133
Receivables upon performed transactions – Master Card	37,905	45,835
Receivables upon performed transactions – Visa	12,965	9,303
Other	13,355	11,096
Less: allowances for impairment	<u>(6,186)</u>	<u>(5,913)</u>
	<u>212,995</u>	<u>188,937</u>

In thousands of denars **2011** **2010**

Specific allowances for impairment

Balance at 1 January	5,913	3,224
Impairment loss for the year:		
Charge for the year	273	2,689
Recoveries	-	-
Write-offs	-	-
Balance at 31 December	<u>6,186</u>	<u>5,913</u>

23. Deposits from banks

<i>In thousands of denars</i>	2011	2010
Domestic banks		
Current deposits	6,796	6,355
Foreign banks		
Term deposits	<u>3,442</u>	<u>624,490</u>
	<u>10,238</u>	<u>630,845</u>

Notes to the financial statements

24. Deposits from customers

<i>In thousands of denars</i>	2011	2010
Retail customers:		
Term deposits	2,181,908	2,105,993
Current deposits	747,804	680,073
Restricted deposits	93,189	103,750
Corporate customers:		
Term deposits	727,795	647,590
Current deposits	1,635,925	818,887
Restricted deposits	74,403	55,887
Public sector		
Current deposits	17,374	76,754
	<u>5,478,398</u>	<u>4,488,934</u>

At 31 December 2011 MKD 477,738 thousand (2010: MKD 352,970 thousand) of deposits from customers are expected to be settled more than 12 months after the reporting date.

25. Other borrowed funds

<i>In thousands of denars</i>	2011	2010
Un-secured bank loans from other financial institutions	<u>1,429,259</u>	<u>1,797,604</u>
	<u>1,429,259</u>	<u>1,797,604</u>

At 31 December 2011 MKD 886,366 thousand (2010: MKD 1,313,577 thousand) of other borrowed funds are expected to be settled more than 12 months after the reporting date.

Notes to the financial statements

25. Other borrowed funds (continued)

Terms and conditions of outstanding loans were as follows:

<i>In thousands of denars</i>	Currency	Nominal interest rate	Year of maturity	2011		2010	
				Face value	Carrying amount	Face value	Carrying amount
		1% plus 3 months					
Unsecured loans	EUR	EURIBOR	2010 - 2012	363,416	363,416	259,090	259,090
Unsecured loans	EUR	1%	Revolving fund	396	396	2,712	2,712
		2,9% plus semiannual					
Unsecured loans	EUR	EURIBOR	2006 - 2010	-	-	-	-
Unsecured loans	EUR	2,5%	2008 - 2011	1,733	1,733	2,350	2,350
			According to contracts signed with end users				
Unsecured loans	EUR	No interest		2,093	2,093	2,093	2,093
		6 monthly EURIBOR plus 3.1%	2011 - 2016	-	-	307,525	307,525
		6 monthly EURIBOR plus 2.9%	30 September 2011	280,622	280,622	315,515	315,515
		6 monthly EURIBOR plus 2.6%	2009 - 2012	28,828	28,828	86,489	86,489
		6 monthly EURIBOR plus 2.5%	2008 - 2012	19,219	19,219	57,659	57,659
		6 monthly EURIBOR plus 2.6%	2009 - 2017	189,963	189,963	189,098	189,098
			According to contracts signed with end users				
Unsecured loans	EUR	5%		32,277	32,277	67,045	67,045
		6 monthly EURIBOR plus 3.42%	2013 - 2018	305,565	305,565	305,679	305,679
		6 monthly EURIBOR plus 2.25%	2012 - 2015	183,421	183,421	181,054	181,054
			According to contracts signed with end users				
Unsecured loans	MKD	no interest		-	-	-	-
			According to contracts signed with end users				
Unsecured loans	MKD	2%		1,480	1,480	1,079	1,079
Unsecured loans	MKD	5.85%	Revolving fund	20,246	20,246	20,216	20,216
Total				1,429,259	1,429,259	1,797,604	1,797,604

Notes to the financial statements

26. Provisions

<i>In thousands of denars</i>	Off balance sheet items	Litigation and claims	Total
Balance at 1 January 2011	603	16,930	17,533
Provisions made during the year	458	-	458
Release	-	(15,329)	(15,329)
Used provisions during the year	-	(392)	(392)
Balance at 31 December 2011	<u>1,061</u>	<u>1,209</u>	<u>2,270</u>

27. Other liabilities

<i>In thousands of denars</i>	2011	2010
Suppliers payable	25,415	11,778
Accrued expenses	16,331	24,865
Other taxes and contributions	519	92
Liabilities for not realised money transfers	-	123
Liabilities upon performed transactions – Master Card	28,431	20,385
Liabilities upon performed transactions – Visa	3,491	11,591
Other	18,722	12,960
	<u>92,909</u>	<u>81,794</u>

28. Capital and reserves

Share capital

<i>In number of shares</i>	Ordinary shares	
	2011	2010
On issue at 1 January	41,870	41,870
Issued during the year	146,545	-
On issue at 31 December	<u>188,415</u>	<u>41,870</u>

At 31 December 2011 the authorised share capital comprised 188,415 (2010: 41,870) ordinary shares. Ordinary shares have a par value of MKD 10,000 (2010: MKD 10,000). All issued shares are fully paid.

The holders of ordinary shares are entitled to receive dividends as declared from time to time and are entitled to one vote per share (2010: one vote per share) at shareholders' meetings of the Bank. All shares rank equally with regard to the Bank's residual assets.

Notes to the financial statements

28. Capital and reserves (continued)

Share capital (continued)

The following shareholders have an interest exceeding 5% of the Bank's issued voting share capital:

	% of voting share capital	
	2011	2010
Halk Bankasi A.S. Ankara	98,12%	-
Demir Halk Bank Nederland – N.V	-	66.6%
European Bank for Reconstruction and Development	-	25.0%
Agency for managing repossessed property	1,66%	7.4%

Statutory reserve

Under local statutory legislation, the Bank is required to set aside 15 percent of its net profit for the year in a statutory reserve until the level of the reserve reaches 1/5 of the court registered capital. Until achieving the minimum required level the statutory reserve could only be used for loss recovery. When the minimum level is reached the statutory reserve can also be used for distribution of dividends, based on a decision of the shareholders' meeting, but only if the amount of the dividends for the current business year has not reached the minimum for distribution as prescribed in the Trade Company Law or by the Bank's Statute.

Fair value reserve

The fair value reserve includes the cumulative net change in the fair value of available-for-sale investments, excluding impairment losses, until the investment is derecognised.

Dividends

After 31 December 2011 no dividends were proposed by the Supervisory Board of the Bank.

Notes to the financial statements

29. Contingencies

The Bank provides financial guarantees and letters of credit to guarantee the performance of customers to third parties. These agreements have fixed limits and generally extend for a period of up to one year. Expirations are not concentrated in any period.

The contractual amounts of commitments and contingent liabilities are set out in the following table by category.

<i>In thousands of denars</i>	<i>Note</i>	2011	2010
Guarantees			
in MKD		143,843	125,106
in foreign currency		38,447	36,759
Letters of credit in foreign currency		37,661	31,126
Loan commitments		240,354	251,735
Provisions	26	<u>(1,061)</u>	<u>(603)</u>
		<u>459,244</u>	<u>444,123</u>

These commitments and contingent liabilities have off balance-sheet credit risk because only organisation fees and accruals for probable losses are recognised in the balance sheet until the commitments are fulfilled or expire. Many of the contingent liabilities and commitments will expire without being advanced in whole or in part. Therefore, the amounts do not represent expected future cash flows.

30. Related parties transactions

On 7 April 2011 Halk Bank Turkey purchased majority of the shares of Export and Credit Bank AD, Skopje (Halkbank AD, Skopje) of 91.56% and became the parent company of the Bank. Shares were acquired from Demir Halk Bank, Netherlands (DHB Bank) which owned 66.56% of shares of Export and Credit Bank AD, Skopje (Halkbank AD, Skopje) and 25% of shares from the European Bank for Research and Development (EBRD).

According to the Banking Law persons related to the Bank are the following: persons with special rights and responsibilities and persons related thereto, shareholders with qualified holding in the Bank (direct or indirect ownership of at least 5% of the total number of shares or the issued voting shares in a Bank or which makes it possible to exercise a significant influence in the Bank) and entities related thereto and responsible persons of those shareholders – legal entities.

The Bank approves loans, extends guarantees attracts and takes deposits and loans from enterprises and banks to which it is related.

Notes to the financial statements

30. Related parties transactions (continued)

The volumes of related party transactions at the year end are as follows:

(i) Cash and cash equivalents

<i>In thousands of denars</i>	Transactions with the Parent	
	2011	Bank 2010
Placements as at 1 January	7,934	5,545
Placements during the year	7,538,681	18,020,271
Withdrawals during the year	(7,545,666)	(18,017,882)
Cash and cash equivalents outstanding at 31 December	949	7,934
Specific allowance for impairment	-	-
Interest income earned	-	-

(ii) Loans and advances to related parties

<i>In thousands of denars</i>	Transactions with the Parent	
	2011	Bank 2010
Placements as at 1 January	-	244,845
Placements during the year	-	26,503,456
Withdrawals during the year	-	(26,748,301)
Loans and advances to banks outstanding at 31 December	-	-
Specific allowance for impairment	-	-
Interest income earned	-	6,215

(ii) Loans and advances to related parties

<i>In thousands of denars</i>	Key management personnel of the Bank and other related parties	
	2011	2010
Loans outstanding at 1 January	7,426	4,511
Loans issued during the year	3,741	16,119
Loan repayments during the year	(5,057)	(13,204)
Loans outstanding at 31 December	6,110	7,426
Specific allowance for impairment	1	75
Interest income earned	2	69

Notes to the financial statements

(iv) Deposits from related parties

<i>In thousands of denars</i>	Parent and with it related parties		Other related parties		Key management personnel of the Bank and with them related parties	
	2011	2010	2011	2010	2011	2010
Deposits at 1 January	615,050	311,159	12,744	-	5,979	17,148
Deposits received during the year	8,309,080	1,955,351	24,481	12,744	110,404	49,178
Deposits repaid during the year	-8,920,689	(1,651,460)	29,755	-	(109,969)	(60,347)
Deposits at 31 December	3,441	615,050	7,470	12,744	6,414	5,979
Interest expense on deposits	17,112	15,800	50	461	290	160

(v) Borrowings from related parties

<i>In thousands of denars</i>	Parent and with it related parties		Other related parties	
	2011	2010	2011	2010
Borrowings at 1 January	180,825	-	-	15,293
Borrowings received during the year	-	180,825	-	-
Borrowings repaid during the year	180,825	-	-	(15,293)
Borrowings at 31 December	-	180,825	-	-
Interest expense - borrowings	-	25	-	-

Notes to the financial statements

30. Related parties transactions (continued)

(v) Other transactions with related parties

<i>In thousands of denars</i>	Other related parties		Parent		Key management personnel of the Bank and with them related parties	
	2011	2010	2011	2010	2011	2010
Commitments and contingences	272	1,125	-	-	918	652
Provision for off balance	2	11	-	-	9	7
Interest income	-	-	1,594	-	397	-
Interest expense	19	-	6,609	-	215	-
Fee and commission expense	-	-	68	49	12	3
Fee and commission income	-	40	881	-	-	74

(vi) Key management personnel compensation

<i>In thousands of denars</i>	2011	2010
Short-term employee benefits	27,379	23,838
Termination benefits	3,485	-
	<u>30,864</u>	<u>23,838</u>

31. Subsequent events

On 18 January 2012 the Supervisory Board reached a decision to establish a representative office of Halkbank AD Skopje in Belgrade, the Republic of Serbia.

On 24 February 2012 the Shareholder's Assembly on an extraordinary meeting reached a decision for initiation of a procedure for merging the Bank with Ziraat Banka AD Skopje.