ProCredit Bank

Serbia

Annual Report 2006

Key Figures

EUR '000	2006	2005*	Change
Balance Sheet Data			
Total Assets	495,290	273,778	81%
Gross Loan Portfolio	306,196	185,910	65%
Business Loan Portfolio	195,188	132,058	48%
EUR < 10,000	67,341	40,938	65%
EUR > 10,000 < 50,000	64,642	42,356	53%
EUR > 50,000 < 150,000	31,781	19,694	61%
EUR > 150,000	31,424	29,070	8%
Agricultural Loan Portfolio	64,517	37,991	70%
Housing Loan Portfolio	16,540	3,336	396%
Other	29,951	12,525	139%
Allowance for Impairment on Loans	5,881	4,241	39%
Net Loan Portfolio	300,315	181,669	65%
Liabilities to Customers	256,222	159,834	60%
Liabilities to Banks and Financial Institutions	177,197	86,431	105%
Shareholders' Equity	43,009	24,583	75%
Income Statement			
Operating Income	32,560	24,276	34%
Operating Expenses	31,460	19,463	62%
Operating Profit Before Tax	1,101	4,813	-77%
Net Profit	2,306	5,003	-54%
Key Ratios			
Cost/Income Ratio	88.9%	72.2%	
ROE	6.9%	27.4%	
Capital Ratio	14.4%	12.0%	
Operational Statistics			
Number of Loans Outstanding	87,558	48,622	80%
Number of Loans Disbursed within the Year	85,689	48,194	78%
Number of Business and Agricultural Loans Outstanding	52,735	35,629	48%
Number of Deposit Accounts	310,143	240,375	29%
Number of Staff	1,421	1,005	41%
Number of Branches and Outlets	52	33	58%

* Some figures differ slightly from those in the 2005 annual report as they have been adjusted to reflect new calculation methods.

Mission Statement

ProCredit Bank Serbia is a development-oriented full-service bank. We offer excellent customer service and a wide range of banking products. In our credit operations, we focus on lending to very small, small and medium-sized enterprises, as we are convinced that these businesses create the largest number of jobs and make a vital contribution to the economies in which they operate.

Unlike other banks, our bank does not promote consumer loans. Instead we focus on responsible banking, by building a savings culture and long-term partnerships with our customers.

Our shareholders expect a sustainable return on investment, but are not primarily interested in short-term profit maximisation. We invest extensively in the training of our staff in order to create an enjoyable and efficient working atmosphere, and to provide the friendliest and most competent service possible for our customers.

Letter from the Board of Directors

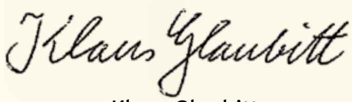
ProCredit Bank Serbia celebrated its fifth anniversary in 2006. The bank has achieved outstanding results during its five years of operation and has had a significant impact on the country's financial sector. ProCredit was the first bank in Serbia to focus on very small, small and medium-sized enterprises and agricultural producers.

Since its inception, the bank has consistently outperformed the sector's growth in terms of its total assets, loan portfolio, deposits and, more importantly, number of clients. Large volume was never ProCredit Bank's primary goal; the bank strives to provide high quality products and services to a substantial number of small businesses and low-income clients.

ProCredit Bank Serbia is firmly anchored in its development orientation and commitment to social responsibility. Despite strong competition, the bank continues to be the national leader in serving small businesses. In 2006 we attracted approximately 80,000 new clients, including 15,500 agricultural producers, 14,800 very small business owners and 9,000 salary earners. The bank had close to 52,900 loans outstanding to very small businesses and SMEs, representing a total volume of EUR 260 million. To support ProCredit Bank's strong growth, the shareholders increased its capital base to EUR 55 million in October 2006.

In 2006 the bank invested heavily in 19 new branches, 416 additional employees, and increased staff training. Despite higher expenses and an unfavourable regulatory environment, the bank reported an ROE of 7%. This result demonstrates that a bank can produce a sufficient return on investment without adopting irresponsible lending strategies.

It is also a tribute to ProCredit Bank's 1,421 staff members, who are highly committed to setting new standards for responsible banking in Serbia.



Klaus Glaubitt,
Chairman of the Board of Directors

Members of the Board of Directors as at December 31, 2006:
Claus-Peter Zeitinger
Gabriele Heber
Helen Alexander
Maria Teresa Zappia
Per Fischer
Kori Udovicki
(until December 31, 2006)

Members of Executive Management as at December 31, 2006:
Doerte Weidig
Svetlana Tolmacheva
Mirjana Zakanji

The Bank and its Shareholders

ProCredit Bank's shareholders – ProCredit Holding, Commerzbank AG, the European Bank for Reconstruction and Development, and KFW Development Bank – continue to provide indispensable support. ProCredit Holding is the bank's majority shareholder. In December 2006 ProCredit Holding purchased a portion of KfW's shares, increasing its ownership to 57.29%.

Shareholder (as of Dec. 31, 2006)	Sector	Headquarters	Share	Paid-in Capital (in EUR)
ProCredit Holding	Investment	Germany	57.29%	20.2
Commerzbank	Banking	Germany	16.67%	5.9
EBRD	Banking	UK	16.67%	5.9
KfW	Banking	Germany	9.37%	3.3
Total Capital			**100%**	**35.3**

ProCredit Holding AG is the parent company of the global group of ProCredit banks located in transition and developing countries across three continents. It was founded as Internationale Micro Investitionen AG (IMI) in 1998. The ProCredit group of banks aim to make a difference by providing banking services to people whom other banks either do not serve at all (usually on the grounds of cost or risk) or only serve inadequately. The holding company, working closely with Internationale Projekt Consult GmbH (IPC), guides the development of the ProCredit institutions, providing support in all key areas of banking operations and human resources management. The company currently has an equity base of more than EUR 200 million. Its shareholders consist of a sound mix of private and public investors.

Commerzbank AG was established in 1870 and following the takeover of Eurohypo AG, announced in November 2005, is now Germany's second-largest bank and one of the leading commercial banks in Europe. With a strong international network comprising offices and shareholdings in more than 40 countries, Commerzbank is a universal bank providing retail, corporate, public-sector and investment banking services. It also offers financial products and services via a number of subsidiaries, such as online banking, leasing, asset management and real-estate investment.

The **European Bank for Reconstruction and Development (EBRD)** was established in 1991. It aims to foster the transition towards open, market-oriented economies and to promote private and entrepreneurial initiative in the countries of Central and Eastern Europe and the Commonwealth of Independent States (CIS) committed to democracy, pluralism and market economics. The EBRD seeks to help its 29 countries of operations to implement structural and sectoral economic reforms, promoting competition, privatisation and entrepreneurship. In fulfilling its role as a catalyst of change, the Bank encourages cofinancing and foreign direct investment from the private and public sectors, helps to mobilise domestic capital, and provides technical cooperation in relevant areas.

KfW Entwicklungsbank (KfW Development Bank): On behalf of the German federal government, KfW Entwicklungsbank finances investments and accompanying advisory services in developing and transition countries. Its aim is to build up and expand the social and economic infrastructure of the countries in which it is active, and to advance sound financial sectors while protecting resources and ensuring a healthy environment. KfW Entwicklungsbank is a leader in the field of microfinance and is involved in target group-oriented financial institutions around the world. It is part of KfW Bankengruppe (KfW Banking Group), which has a balance sheet total of EUR 362 billion (as of September 2006). KfW Bankengruppe is one of the ten biggest banks in Germany and is AAA rated.

The ProCredit Group – Neighbourhood Banks for Ordinary People

The ProCredit group currently comprises 19 target group-oriented banks operating in as many countries. We focus on developing countries and transition economies in three regions: Eastern Europe, Latin America and Africa. The group has 470 branches staffed by 12,600 employees. Currently, ProCredit banks disburse more than 60,000 loans totalling more than EUR 185 million every month. By the end of 2006, the number of loans outstanding had grown to more than 740,000 (amounting to EUR 2.1 billion). The average loan amount outstanding is EUR 2,850 and the loan portfolio quality remains excellent with a ratio of loans in arrears (>30 days) to total loan portfolio of only 1.2%. Over 2006, the group's deposit base increased from EUR 1.3 billion to EUR 1.8 billion, with nearly one million new accounts having been opened.

The ProCredit group is led by the Frankfurt-based ProCredit Holding AG, founded by the consulting firm IPC in 1998. The staff of ProCredit Holding and IPC provide centralised support, supervision and management of all the ProCredit banks. ProCredit Holding is a private-public company, with international shareholders that include KfW, IFC, FMO, and the DOEN Foundation. In 2006, the shareholder group was joined by two new US-based private shareholders, TIAA-CREF and the Omidyar-Tufts Microfinance Fund.

But what do these facts and figures mean and what are these shareholders trying to achieve? ProCredit is building a global group of neighbourhood banks. But what is a neighbourhood bank? Wherever we are, we aim to be the accessible, trusted, socially responsible bank for the local small businesses and the ordinary people who live and work in the area. In our lending business, we focus on very small, small and medium-sized enterprises. At the same time ProCredit provides retail banking services to "ordinary" people, with a focus on low-income families. In this way we aim to be the long-term banking partner for target groups which most conventional commercial banks neglect. By providing socially responsible products we aim to contribute to the economic development of the countries in which we work.

In the developing countries and transition economies in which the ProCredit group operates, conventional commercial banks tend to neglect small and very small businesses because they are thought to keep inadequate records, have insufficient collateral and generate high administrative costs. However, these businesses are the main engine of economic growth and of job creation. Over the years, the ProCredit group and IPC, which developed the lending methodology used by the ProCredit group, have gained a profound understanding of both the problems faced by small businesses and the opportunities available to them, and have tailored the credit technology to reflect the realities of their operating environment. Thanks to this credit technology, which combines careful analysis of all credit risks with a high degree of standardisation and efficiency, the ProCredit institutions are able to reach a large number of small borrowers.

In contrast to ProCredit, other commercial banks give priority in their lending operations to corporate finance and consumer lending, especially the latter. Consumer finance is attractive because it usually does not require skilled staff or much financial analysis of the client, allowing banks focused on market share to grow quickly. However, this quest for market share can lead to irresponsible lending and overindebtedness on the part of the client. ProCredit never forgets that a loan is also a debt. We place great emphasis on the careful evaluation of a borrower's debt capacity and on building lasting relationships. In this way, ProCredit is characterised by a responsible, long-term attitude towards business development and client relationships.

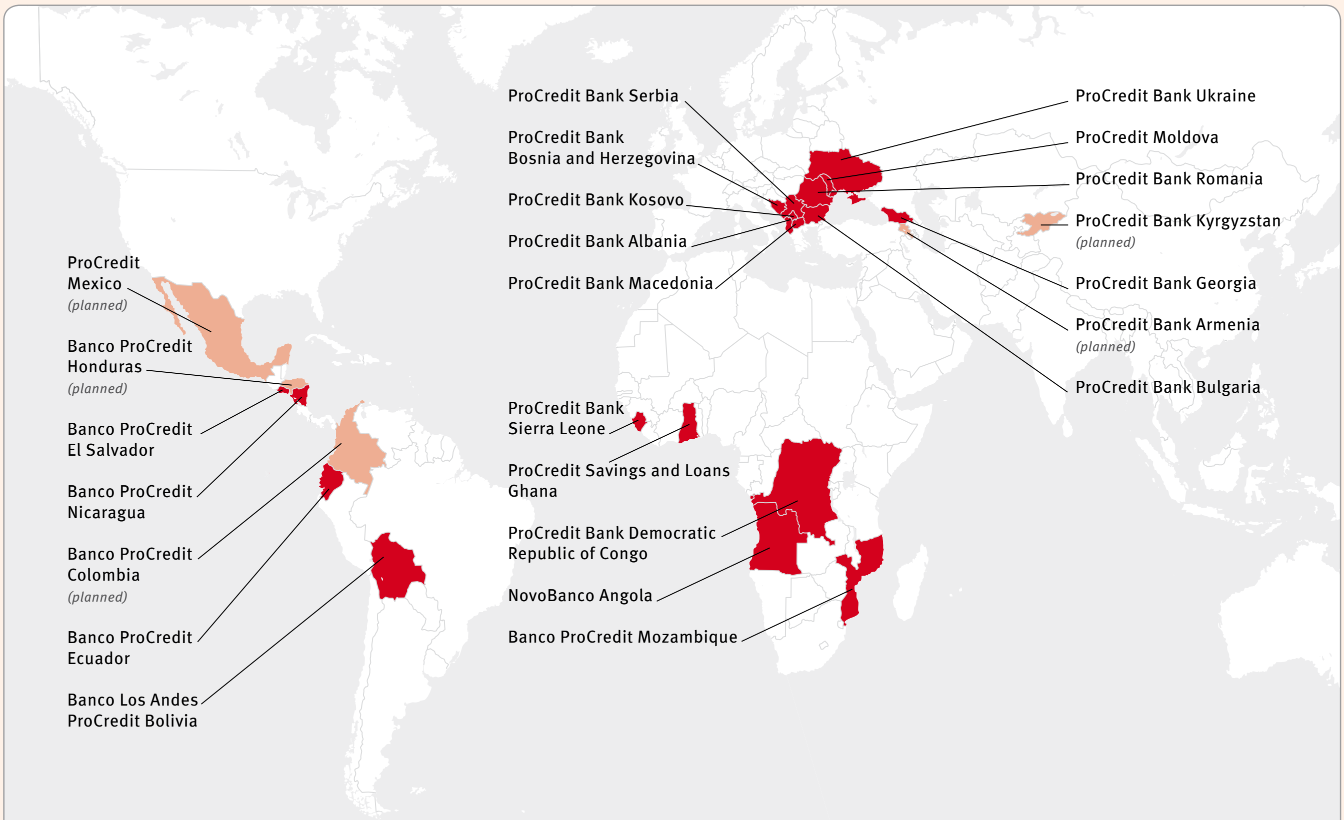
Furthermore, ProCredit institutions strive to foster a savings culture. We aim to build public confidence in banks by setting new standards in customer service, transparency and business ethics. ProCredit deposit facilities are appropriate for a broad range of customers, especially low-income groups. We offer simple savings products with no minimum deposit requirement. Eighty percent of all deposit accounts have a balance of less than EUR 100. This illustrates our target group orientation and highlights the challenge of serving this target group of small savers, who account for only 1% of our total deposit volume. In the spirit of a neighbourhood bank, ProCredit banks place great emphasis on children's savings products and education campaigns as well as on sponsoring local community events. In addition to deposit facilities, clients are offered a full range of standard non-credit banking services.

The shareholders of the group aim to strike the right balance between their prime developmental goals: reaching as many small enterprises and small savers as possible, and achieving commercial success. For 2006, the return on equity for the group as a whole, expressed in hard currency after deduction of profit taxes, is expected to reach 13%. This level of profitability is required to support our rapid growth, to ensure our long-term sustainability and to generate a reasonable return for our shareholders.

The neighbourhood bank concept is not limited to our target customers and how we reach them. It is also about our staff: how we work with one another and how we work with our customers. The neighbourhood bank approach requires a high degree of decentralised decision-making and therefore judgement and creativity from all staff, especially our branch managers. Our corporate values embed principles such as honest communication, transparency and professionalism into our day-to-day business. Key to our success is therefore the selection and training of the right staff. We maintain a corporate culture that harnesses the creativity and entrepreneurial spirit of our staff, while fostering their deep sense of personal and social responsibility. This entails not only intensive training in technical and management skills, but also a continuous exchange of personnel between our member institutions in order to take full advantage of the opportunities for staff development which are created by their membership of a truly international group.

A central plank in our approach to training is the group's ProCredit Academy in Germany, which provides a three-year, part-time "ProCredit Banker" training programme for its high-potential local personnel. The programme includes intensive technical training and also exposes participants to a very multicultural learning environment and to subjects such as anthropology and the humanities. The programme provides an opportunity for our future leaders to develop their views of the world, as well as their communication and staff management skills. The continued success of ProCredit relies on a self-confident team of people who share a personal commitment to the target group and to the neighbourhood way of doing things.

The international group of ProCredit institutions; see also ***www.procredit-holding.com***




Štednja u ProCredit banci:
Platne kartice ProCredit banke:
Dobro je da ih imam!
VISA


ProCredit Bank

ProCredit in Eastern Europe

ProCredit operates in 10 countries across Eastern Europe. With more than 430,000 loans outstanding, it is the region's leading provider of banking services to very small, small and medium-sized businesses. Financial sectors and private sector lending are rapidly expanding in Eastern Europe, often through heavy investment in the form of foreign capital and the activities of strong western banks. In this context we are sometimes asked: can ProCredit really claim to be different and to be making a difference in the region? Our answer is a resounding "yes". We stand out as banks deeply committed to small business lending over the long term, to building a responsible savings culture rather than blindly fuelling consumer spending, and to setting new standards of transparency and service for our customers.

Across the region, the focus of most banks, including the western banks, continues to be corporate finance and consumer lending. They neglect lending to small entrepreneurs and family businesses. Yet these businesses are the driving force behind economic growth and job creation across Eastern Europe, and have been since the collapse of Soviet influence and the large state-owned enterprises of the Soviet era. For most banks, it is simply easier to make money with consumer lending and loans to larger corporate clients, since small business lending requires decentralised decision-making and highly qualified staff who are able to assess risk quickly and reliably and maintain durable client relationships. The importance of ProCredit in transition economies should be no surprise: even in well-developed western markets, only a few banks are dedicated to the long-term support of small business customers.

It is also no surprise that consumer lending, which is being so aggressively pursued by other banks in Eastern Europe, is not a business in which ProCredit actively engages. We believe that it tends to drive imports rather than domestic production. If pushed irresponsibly in the context of a market share gain game – with very little analysis of a customer's repayment capacity – it quickly leads to overindebtedness. This creates suffering for the individuals and families affected, and can threaten financial sector stability. The growing incidence of steeply rising default rates underpins this view. Our approach is to provide loans primarily to businesses and to do so based on a careful, efficient analysis of a client's ability to repay. We aim to build lasting relationships and we never forget that a loan is also a debt. In this way, ProCredit is characterised by a responsible, long-term attitude towards business development.

Across the region we provide agricultural loans, supporting a sector that has been particularly neglected by other banks and that is vital for employment and social cohesion outside the main urban areas. We also provide housing improvement loans to help low-income families renovate their homes and improve energy efficiency. ProCredit banks offer their business clients loans and other services, including plastic cards and fast, low-cost money transfers ("ProPay"), providing a truly integrated service for entrepreneurs who are active across the region.

In the face of rapid expansion in consumer lending, we make it a priority to create a "savings" culture, not just a "spending" culture – because savings are an important buffer against the vagaries of life. Through promotional events and direct, personal communication we encourage people – particularly those who do not yet have a banking relationship – to use banking services and to regularly set aside a certain portion of their earnings. This outreach is combined with the offer of simple and reliable banking products, especially savings and deposit accounts.

In keeping with our mission to be accessible to clients wherever they are, the ProCredit group provides comprehensive coverage across the region with its 341 branches and more than 8,600 staff. Our clients can now drive from Tirana in Albania to Kiev in Ukraine and enjoy the same friendly service and open, welcoming branches all along the way. We place a strong emphasis on transparency in all ProCredit banks. We run information campaigns to ensure that all customers understand the pricing of our products as well as those of our competitors, since we find that aggressively growing markets create a lot of scope for misleading customers about the true price of banking services.

Our staff are the key element in our approach to being a stable, down-to-earth banking partner to clients across the region. The group has a strong commitment to staff training, professional development and cultivating an open, honest communication culture. Staff exchanges, cross-border training programmes and regional workshops are an important part of our approach. In the highly competitive Eastern European banking sectors, the well-trained, highly motivated ProCredit staff, who have built strong, long-term relationships with clients, are in high demand from competitor banks. However, the ProCredit work environment, the investment we make in our staff and the international opportunities that they enjoy, demonstrate that we have been very successful in retaining our best people, providing a firm base for our ongoing growth in the region.

Name	Highlights	Contact
ProCredit Bank Albania	Founded in March 1999 22 branches 28,581 loans / EUR 94.2 million in loans 143,679 deposit accounts / EUR 191.9 million 577 employees	Rruga Sami Frasheri Tirana Tel./Fax: +355 4 271 272 / 276 info@procreditbank.com.al www.procreditbank.com.al
ProCredit Bank Bosnia and Herzegovina	Founded in October 1997 26 branches 42,459 loans / EUR 117.4 million in loans 60,620 deposit accounts / EUR 90.4 million 595 employees	Emerika Bluma 8 71000 Sarajevo Tel./Fax: +387 33 250 950 / 250 971 info@procreditbank.ba www.procreditbank.ba
ProCredit Bank Bulgaria	Founded in October 2001 60 branches 49,728 loans / EUR 309.8 million in loans 136,223 deposit accounts / EUR 218.5 million 1,074 employees	131, Hristo Botev Blvd. Sofia Tel./Fax: +359 2 921 71 00 / 71 10 contact@procreditbank.bg www.procreditbank.bg
ProCredit Bank Georgia	Founded in May 1999 32 branches 58,967 loans / EUR 141.1 million in loans 335,064 deposit accounts / EUR 97.8 million 1,198 employees	D. Agmashenebeli Ave 154 Tbilisi Tel./Fax: +995 32-20 2222 / 0580 info@procreditbank.ge www.procreditbank.ge
ProCredit Bank Kosovo	Founded in January 2000 30 branches 52,016 loans / EUR 237.7 million in loans 229,995 deposit accounts / EUR 389.9 million 722 employees	Str. Skenderbeu 10 000 Prishtina/ Kosovo UNMIK Tel./Fax: +381 38-240 248 / 248777 info@procreditbank-kos.com www.procreditbank-kos.com
ProCredit Bank Macedonia	Founded in July 2003 24 branches 21,277 loans / EUR 73.4 million in loans 87,125 deposit accounts / EUR 74.2 million 537 employees	Jane Sandanski 109a 1000 Skopje Tel./Fax: +389 2 321 99 00 / 01 info@procreditbank.com.mk www.procreditbank.com.mk
ProCredit Moldova	Founded in December 1999 21 branches 14,096 loans / EUR 25.2 million in loans 259 employees	Stefan cel Mare si Sfant, 65 Off. 900, 902, 904; Chisinau Tel./Fax: +373 22 270707/ 3488 office@procredit.md www.procredit.md
ProCredit Bank Romania	Founded in June 2002 29 branches 29,621 loans / EUR 157.3 million in loans 87,986 deposit accounts / EUR 116.9 million 795 employees	Calea Buzesti, no. 62-64, Sector 1 011017 Bucharest Tel./Fax: +40 21 2016000 / 2016002 headoffice@procreditbank.ro www.procreditbank.ro
ProCredit Bank Serbia	Founded in April 2001 52 branches 87,558 loans / EUR 306.2 million in loans 310,143 deposit accounts / EUR 256.2 million 1,421 employees	Bulevar despota Stefana 68c Belgrade Tel./Fax: +381 11 20 77 906/ 905 info@procreditbank.co.yu www.procreditbank.co.yu
ProCredit Bank Ukraine	Founded in January 2001 52 branches 49,270 loans / EUR 226.9 million in loans 81,985 deposit accounts / EUR 118.2 million 1,495 employees	107-A Pobedy Ave. Kyiv 03115 Tel./Fax: +380 44 590 10 41 / 01 info@procreditbank.com.ua www.procreditbank.com.ua

The Year in Review

January

- In cooperation with the Corporate Journalists' Club of Serbia, ProCredit Bank establishes the ProBusiness Leader award for SME entrepreneurship.
- ProCredit Bank issues credit and debit cards free of charge in response to the abolition of cheques as a means of payment in 2005.

February

- ProCredit Bank reduces interest rates, lowers collateral requirements and extends the repayment period for housing and home improvement loans.

March

- The bank opens a branch in Pozarevac, a town in eastern Serbia with very few banks. It also opens a branch in a district of Belgrade that has a growing number of small and very small enterprises. At the branch openings, children participate in a contest in which winners are awarded a savings book with a small deposit.

April

- The bank opens two new branches, one in Zajecar and one in Smederevo.
- ProCredit Bank introduces "ProAgro Imanje", a long-term loan for agricultural producers. This innovative product is for the purchase of land and is unique in the Serbian market.

May

- To celebrate its fifth anniversary, ProCredit Bank Serbia hosts a Family Day for employees and clients in a Belgrade theatre. The event includes a play for children and an exhibition of products made by ProCredit Bank clients.
- Total volume of outstanding loans in the agricultural sector reaches EUR 40 million.

June

- ProCredit Bank opens two branches in Belgrade.
- The bank launches a national advertising campaign based on well-known Serbian proverbs and how they relate to the bank's values and products.

July

- ProCredit Bank Serbia opens three new branches: in Subotica in the northern part of Serbia, Stara Pazova in western Serbia, and Jagodina in southern Serbia.
- After more than three years in Serbia, Deputy General Manager Gian Marco Felice is promoted to General Manager of ProCredit Bank Bulgaria.

August

- The bank opens one branch in Niš, one of the most populous cities in Serbia, and one in Leskovac in the south.

September

- The bank launches a loan for purchase, construction and renovation of business premises.
- A branch is opened in Kragujevac in central Serbia.

October

- The bank introduces Visa cards for its business clients.
- A savings campaign highlights increased interest rates on term deposits and an educational brochure entitled “Truth and Misconceptions about Savings”.
- The bank celebrates International Savings Day by organising events for children in all branches.
- The bank opens two branches, one in Belgrade and one in Novi Sad in northern Serbia.

November

- The bank signs a loan agreement with the International Finance Corporation (IFC). The funds will be used to provide loans to improve energy efficiency in homes and businesses.
- ProCredit Bank opens two branches, one in Obrenovac near Belgrade, and another in Sremska Mitrovica in central Serbia.

December

- The bank establishes a presence in two cities – Backa Palanka and Indjija – and opens an additional branch in Novi Sad. At year-end, ProCredit Bank Serbia has 52 branches.
- The bank signs a loan agreement with the Netherlands Development Finance Company (FMO) for EUR 46 million. The funds will provide medium-term financing to very small businesses and SMEs.

Management Business Review

Members of the Management Board
from left to right:

Svetlana Tolmacheva
Member of the Executive Board

Doerte Weidig
Chairperson of the Executive Board

Mirjana Zakanji
Member of the Executive Board

Political and Economic Environment

In 2006 the Serbian government sought to boost economic growth and to continue reforms required for European integration. Montenegro declared independence from Serbia in June and peacefully seceded. The future status of Kosovo was not resolved; the international community and the Serbian government are actively seeking a solution that will satisfy all parties and sustain regional stability.

The government adopted a new constitution and defined a national strategy for EU accession. Serbia joined NATO's Partnership for Peace Programme, a significant step towards Euro-Atlantic integration. Negotiations on EU accession came to a standstill, however, after Serbia failed to meet conditions imposed by the International Criminal Tribunal for the Former Yugoslavia.

Serbia's macroeconomic situation improved significantly in 2006. Real GDP growth was 6.5%, the current account deficit was 11.7% of GDP, and public debt decreased to 67% of GDP. With a budget surplus of EUR 2.2 billion, Serbia is likely to repay its outstanding debt to the IMF in 2007.

The National Bank announced a transition to exchange rate flexibility in early 2006. Meanwhile, the supply of foreign exchange increased. Banks decreased their open currency positions after the National Bank of Serbia adjusted its method for calculating foreign currency risk. In addition, several foreign-owned banks strengthened their capital base, and two large companies were privatised, leading to substantial capital inflows. Consequently, the dinar appreciated by 12.1% in real terms against the euro.

Foreign direct investment reached an all-time high in 2006. A further increase is expected in 2007 due to the privatisation of large state-owned companies in the energy sector. GDP per capita was EUR 3,338. The official unemployment rate remained high at 18%, and inflation was 6.6%.

Despite Serbia's remaining political and economic challenges, the EBRD declared the country a regional leader in development. Economic growth and competition are expected to improve further in 2007.

Financial Sector Development

Banks remained Serbia's dominant financial institutions. Foreign-owned banks accounted for 75% of total banking assets. ProCredit Bank Serbia was ranked 9th with a 3.3% share of total assets.

In September the National Bank of Serbia announced a new monetary policy framework to stabilise inflation caused by growing lending activity, among other factors. It lowered the interest rate on repo operations from 18% to 15%. In addition, the National Bank raised its reserve requirements for foreign liabilities and foreign currency deposits. Consequently, inflation decreased from 17.5% in 2005 to 7% in 2006, and the growth of lending slowed.

Serbia has taken important steps to promote a competitive and robust banking system. Privatisation has been rapid and supported by regulatory and legal reforms. A new banking law was adopted in October to bring domestic regulation into compliance with Basle II standards. Vojvodjanska Banka, one of the largest banks in Serbia, was privatised. The National Bank of Greece purchased 99.4%, increasing Greek banks' market share to 16.7%. Many financial institutions merged over the past five years, halving the number of banks since 2001. As of year-end 2006, the banking sector consisted of 37 institutions. According to the National Bank of Serbia, privatisation and mergers and acquisitions will continue in 2007. This consolidation will further intensify competition in the financial sector.

Total lending and deposit-taking increased in 2006. Loan placements rose by 25.5%: 36% of the increase was to private individuals and 59% was to legal entities. A significant increase of 60% in domestic savings led to total deposits growing by 37.5%.

Lending Performance

ProCredit Bank achieved remarkable growth in its lending operations in 2006. Its year-end outstanding loan portfolio was EUR 307 million, of which EUR 260 million was accounted for by loans to very small, small and medium-sized enterprises. The total loan portfolio grew by 67%, or EUR 123 million. The number of loans grew by 66% to more than 87,500, of which approximately 52,900 were to businesses.

In line with the bank's mission, 37% or EUR 112 million of its total outstanding loan portfolio consisted of loans in amounts less than EUR 10,000. The bank disbursed EUR 111 million of these loans to very small enterprises in 2006. ProCredit Bank Serbia aims to achieve maximum efficiency in serving this target group. Throughout the year, lending procedures were revised, enabling employees to serve clients faster at lower cost. On average, the processing time from application to disbursement for very small loans was less than 3 days.

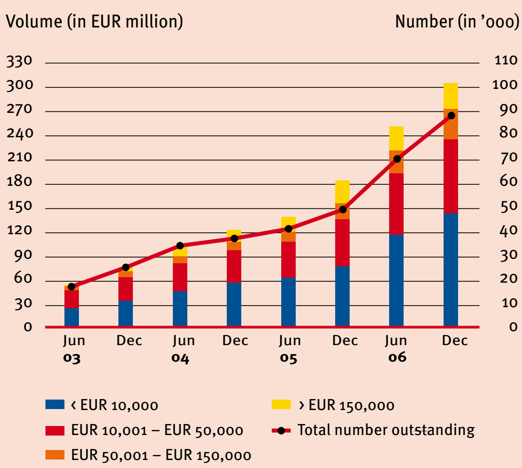
The bank had EUR 81 million in loans outstanding to small businesses for amounts between EUR 10,000 and EUR 50,000, an increase of 47% over 2005. Loans outstanding to medium-sized businesses for amounts greater than EUR 50,000 grew by 38% to EUR 67 million at the end of 2006. The bank offers a full range of products and services to these clients, including account administration, domestic and international payments, and trade finance instruments. It also provides high-quality and proactive customer care through 21 customer relationship managers who are responsible for this target group.

The bank increased the volume of its trade finance business by 86% in 2006. It had 815 outstanding documentary exposures totalling EUR 35 million in its off-balance sheet portfolio at year-end. Eighty percent were guarantees, and the remainder were letters of credit and other forms of documentary business. Guarantees were issued primarily in conjunction with payment transactions, participation in tenders and the fulfilment of customs requirements.

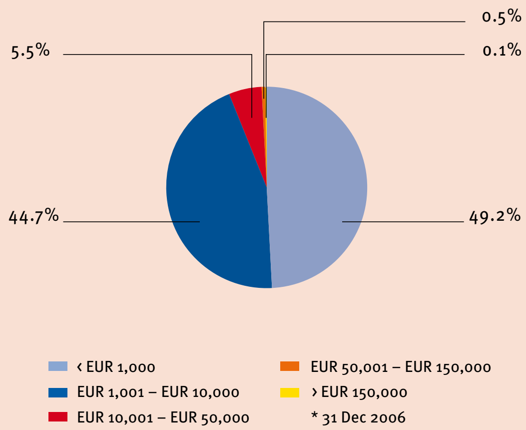
Agricultural loans comprised 21% of the total loan portfolio. ProCredit Bank had nearly 23,000 agricultural loans outstanding with a total volume of EUR 65 million at year-end. These loans, which averaged EUR 2,870, financed working capital and investments in livestock and machinery.

As from 2006, agricultural producers were required by law to have commercial bank accounts in order to register their households or businesses. The government began transferring subsidies and other payments directly into these accounts. Since we are well known for our active role in serving agricultural customers, many farmers chose to open an account with ProCredit. As a result, the number of current accounts held by this target group increased by 51%.

Loan Portfolio Development



Number of Loans Outstanding – Breakdown by Loan Size*



In 2006 the bank broadened its range of loan products. Companies can now obtain overdrafts on their current accounts, enabling them to manage their liquidity more efficiently. Thanks to our highly competitive prices, demand for this attractive product among both existing and new clients was strong. Overdrafts, which ranged from 30% to 50% of clients' monthly account turnover, were approved in a total volume of EUR 31 million in 2006. The availability of overdraft facilities prompted many clients to execute payments through our bank, contributing to a significant increase in the volume of domestic transfers.

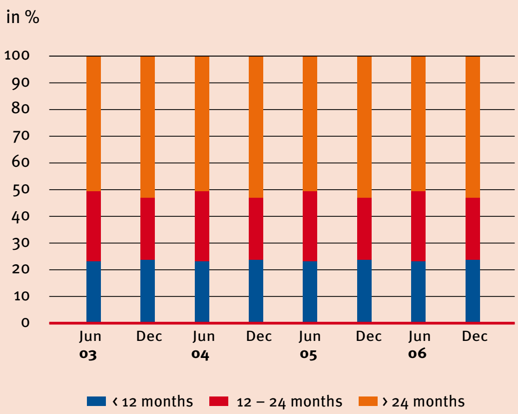
The total consumer loan portfolio, comprising consumer instalment loans, overdrafts on accounts held by private individuals and credit card exposures, grew by EUR 8.5 million to EUR 16 million during 2006. In this area, our credit card business experienced the greatest growth; the outstanding volume rose by EUR 0.6 million to EUR 5.7 million. The bank approved overdrafts in amounts equal to a single month's income for private individuals with a stable salary. In line with its business policy, ProCredit Bank Serbia issued traditional consumer instalment loans only to clients who were not over-indebted; monthly instalments did not exceed one-third of clients' monthly income, and the maximum repayment period was five years. These loans were approved in local currency and were not pegged to the euro; the bank does not transfer foreign currency risk to customers who may not be able to manage this type of risk. ProCredit Bank ensures that consumer loans are offered in a socially responsible manner. Unlike its competitors, the bank refuses to flood the market with consumer loans that have seemingly easy terms and conditions. It is therefore not surprising that consumer loans issued by ProCredit Bank increased by only EUR 1.5 million, reaching EUR 9 million at year-end.

As a development-oriented bank, we are committed to broadening private individuals' access to loans for financing home improvements and housing purchases. Our portfolio of this type of loan grew from EUR 3.3 million in 2005 to EUR 16.8 million in 2006. A total of 3,845 clients had a housing or home improvement loan outstanding at year-end.

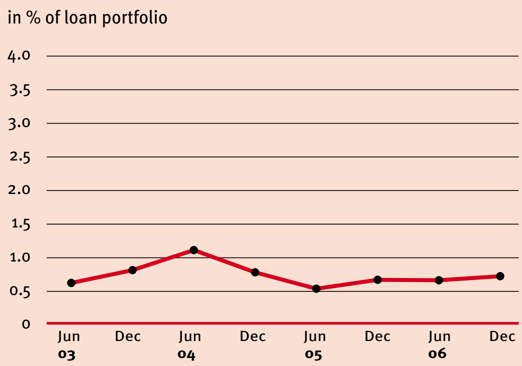
Loan portfolio quality remains excellent. Outstanding loans with payments more than 30 days overdue constitute only 0.7% of the total loan portfolio. Accumulated loan losses are low, amounting to 0.9% of the portfolio. We are confident that our strong focus on efficiency and our strict adherence to the principles of sound loan monitoring will allow us to maintain this high portfolio quality in the future.

ProCredit Bank has the 9th largest loan portfolio in the Serbian banking sector. Since we first opened our doors in Serbia, we have disbursed a cumulative total of more than EUR 890 million.

Business Loan Portfolio – Breakdown by Maturity



Loan Portfolio Quality (arrears >30 days)



Net write-offs: in 2003: EUR 41,015; in 2004: EUR 294,201; in 2005: EUR 612,741; in 2006: EUR 848,073

Other Banking Services

ProCredit Bank Serbia's predominant retail services were deposits and payment cards. As of December 31, more than 207,000 clients were using the bank's retail services. They held 252,000 current accounts, 25,000 term deposits and 33,000 savings accounts. Savings with maturities exceeding six months accounted for roughly 70% of the total volume of deposits held with ProCredit Bank. Deposits held by private individuals grew by 48% to EUR 156 million. The volume of "ProFit" term deposits, which are more flexible than any other term deposit product in Serbia, grew by 47% to EUR 117 million. The funds held in our "ProFit Fleks" savings accounts, with interest rates that vary with the balance, grew by 55% to EUR 26.5 million. This growth coincided with a market-wide increase in term deposits, indicating that the public is regaining confidence in the banking system. ProCredit Bank has played an active role in this ongoing process.

In 2006 ProCredit Bank Serbia increased its share of the payment card and ATM market. The total number of debit and credit payment cards held by our customers increased by over 95%. By the end of 2006, ProCredit Bank had issued more than 90,000 cards and had captured a market share of 1.8%. Turnover on all ProCredit Bank payment cards tripled and exceeded EUR 29.5 million. The number of transactions also tripled, rising to more than 654,000.

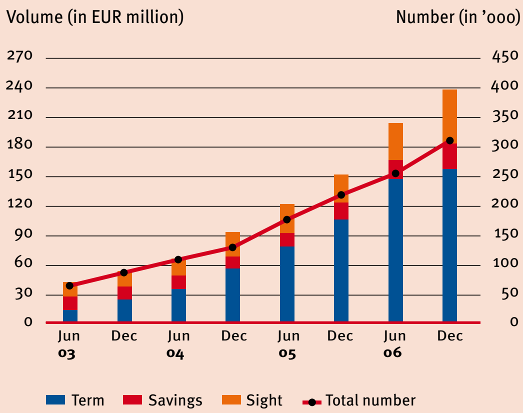
The abolition of the cheque guarantee function contributed substantially to increased demand for credit cards. ProCredit Bank staff made a concerted effort to inform cardholders about the product's features and advantages. By the end of 2006, the bank had issued more than 15,000 credit cards. In August, we launched the Visa Business Electron debit card for legal entities and entrepreneurs. Clients submitted more than 1,500 applications for this product.

The bank invested heavily in the extension of its ATM network, which grew by 100% to 70 units, representing 5% of the total number of ATMs in Serbia. To increase access to our banking services, we installed 18 ATMs at various locations in small cities and towns in remote areas.

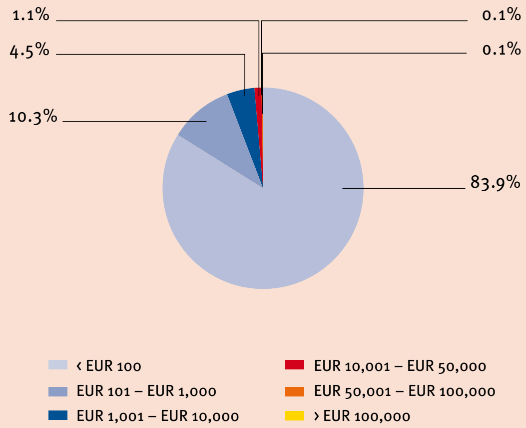
ProCredit was the first bank in Serbia to introduce automatic statement printers, enabling clients to obtain a copy of their account statements free of charge. At year-end, the bank had 35 of these printers, which were issuing more than 35,000 statements each month.

In the year under review, more than 3,400 customers used electronic banking for money transfers and payment orders. Over 820,000 payment orders, or 26% of the total, were placed through the Internet, reflecting a clear trend towards e-banking. We expect this rapid increase to continue in 2007.

Customer Deposits



Number of Customer Deposits – Breakdown by Size



Financial Results

ProCredit Bank's performance in 2006 was influenced by four main factors:

- strong growth in the loan portfolio and customer deposits
- major investments in expanding the branch network
- a substantial rise in the cost of funds due to higher mandatory reserve requirements
- appreciation of the local currency against the euro.

ProCredit Bank Serbia opened 19 new branches and renovated 6 existing branches in 2006. The corresponding increase in capital, operating and staff expenditures was not offset by an immediate contribution to the bank's income.

While branch expansion had a short-term negative impact on ProCredit Bank's financial results, it will enable the bank to strengthen its market position over the long term. We considered the bank's high cost-income ratio of 89% to be an acceptable trade-off in the framework of our long-term expansion strategy.

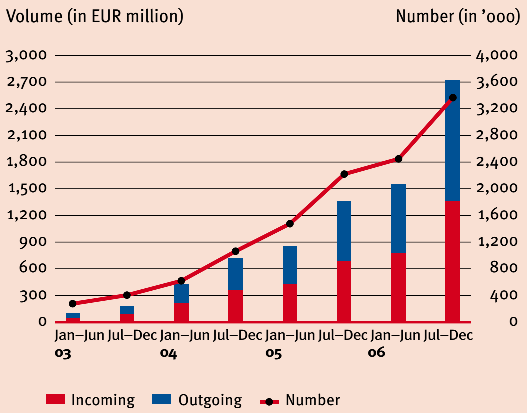
Expenses were kept under control through continued efforts to increase efficiency and reduce costs without compromising our customer service quality. For instance, the bank centralised all back-office functions, which means that our branches can now be smaller and more streamlined.

The loan portfolio increased by 65% in 2006. Interest income grew by 68% and fee income by 56%. More than 53% of the bank's lending business was funded with customer deposits. The bank obtained 5% of its funds from deposits held by other banks and 37% from long-term loans issued by international financial institutions. Shareholders' equity and subordinated debt provided 11% of the bank's funding.

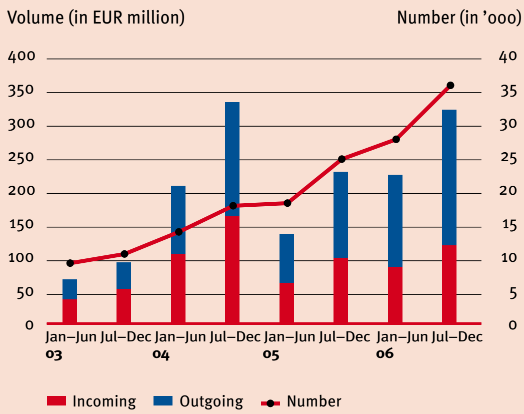
The National Bank of Serbia adjusted mandatory reserve requirements and the repo rate to reduce inflationary pressure and narrow the trade gap. ProCredit Bank adapted to changing monetary conditions to ensure that it could adequately fund its portfolio growth. The bank's mandatory reserves grew by 68% in 2006. As a result, interest expenses rose by 154%. The bank's significant loan portfolio and deposit growth thus produced only a moderate profit. In its financial statements prepared in accordance with IFRS, the bank recorded a profit of EUR 2.3 million, with an ROA of 0.6% and an ROE of 7%.

Total shareholders' equity and subordinated debt rose by 108% to EUR 55 million, following several capital increases in 2006 and the capitalisation of retained earnings. The bank's capital ratio improved significantly, rising to more than 14%.

Domestic Money Transfers



International Money Transfers



Outlook

Since its founding in 2001, ProCredit Bank's assets, loan portfolio and deposit volume have grown rapidly. The bank has also achieved significant brand awareness. At year-end the bank held 3% of the Serbian banking sector's total assets, positioning ProCredit among the top 10 banks in the country. During 2006 we opened 19 branches, many of which are in small cities and remote areas where ProCredit did not previously have a presence.

ProCredit Bank Serbia has remained committed to promoting economic development while strengthening its market position. The institution's biggest challenge in 2007 will be to expand services to its current portfolio of 180,000 clients. By informing clients about the bank's new services and product features, we will increase customer satisfaction and generate fresh demand for our products.

The acquisition of new clients remains a significant challenge. We plan to open 17 more branches distributed evenly among the country's four regions: Northern Serbia, Belgrade, Central Serbia and Southern Serbia. These new branches in Vrbas, Senta, Ruma, Lazarevac, Mladenovac, Arandjelovac, Svilajnac, Paracin and Aleksinac will undoubtedly be an important source of growth because these cities have strong potential for MSME development. Since the market is growing, we also expect to continue generating new business through our existing 52 branches.

The bank places strong emphasis on increasing the efficiency of all its operations. This crucial effort will reduce costs and increase profitability; it will also boost customer satisfaction by reducing the bank's processing time for its products and services. By achieving these goals, ProCredit Bank will enhance its competitive advantage.

In 2007 we will invest significant time and resources in integrating our new employees. The bank considers it very important to ensure that all staff members understand the mission and history of ProCredit Bank. Employees are expected to adopt the corporate values that characterise the ProCredit group: transparency, communication and a high level of professionalism. Managers at all levels will stimulate discussion of our philosophy and values among employees. Integrating and motivating the 1,700 employees projected for 2007 will be a key task for the bank's management. The positive spirit fostered by sharing and living ProCredit's values will enable the bank to achieve even better performance in the future.

Special Feature

Retail Services

ProCredit Bank continued to grow its customer base in 2006. We improved our existing services and expanded our product range for private individuals and businesses. Over 70,000 new accounts were opened, bringing the total number to 310,143. The number of retail clients exceeded 170,000 at year-end.

In 2006 ProCredit Bank began offering retail products to farmers. The agricultural sector contributes substantially to GDP and provides employment to 17% of the Serbian labour force. Most agricultural producers do not have a bank account, but their demand for banking services is growing. Having served this sector for four years, ProCredit Bank recognises that farmers can benefit from basic banking products and that they are valuable customers. In 2006 we were the first bank to offer Visa cards and MasterCards to agricultural producers. By year-end, 2,030 of ProCredit Bank's agricultural clients had credit and/or debit cards.

ProCredit Bank also began offering Visa Business Cards to very small, small and medium-sized enterprises. This product makes it possible for clients to separate their business expenses from their personal expenses, and key staff can make purchases on behalf of the business.

The bank considers its ability to promote a savings culture to be an important measure of its success. We therefore encouraged all citizens to open a savings account, especially those who could not afford to deposit large amounts. As a sign of our long-term commitment to our clients, we introduced the ProCredit Savings Plan in 2006. The Savings Plan is flexible but involves clear obligations for clients. It pays high interest rates on regular savings deposits, even if the amounts are very small: the minimum monthly instalment is as low as EUR 5.

Based on client feedback, we have learned that our customers prefer a simple product line to a vast array of products and services. We therefore introduced two basic "account packages" that link the most popular services, such as debit cards and overdrafts, to a current account. The packages offer lower costs and greater simplicity.

By introducing innovative services in 2006, ProCredit Bank emphasised its customer orientation and reinforced its reputation as a reliable long-term partner for all Serbians.

Risk Management

In an environment characterised by rapidly expanding banking operations and a constantly changing macroeconomic situation, professional risk management is crucial. Risk management is an integral part of ProCredit Bank's business procedures and processes. The bank has established a culture of risk awareness that ensures effective control and mitigation of all relevant risk exposures.

ProCredit Bank is dedicated to providing sound and reliable banking services to very small, small and medium-sized enterprises. Simply by virtue of the bank's target group, its assets and liabilities are highly diversified. Experience has shown very small and SME clients to be highly reliable; the risks associated with serving these customers are thus minimal. The bank adheres strictly to a policy of not engaging in any speculative activities. Trading in derivatives and other financial instruments is undertaken only to the extent necessary to close or limit open currency positions and interest rate gaps.

The bank has implemented clear procedures to deal with the various risks it faces: credit risk, country risk, exposure risk, liquidity risk, foreign exchange risk, interest rate risk and operational risk. All are managed within the framework of three risk committees: the Credit Risk Committee, the Operational Risk Committee and the Assets and Liabilities Committee (ALCO). These are convened periodically and require participation by a member of the Management Board. They enable the bank to identify, assess, monitor and manage risks effectively and in a timely manner.

The Internal Audit Department continually enhances its risk assessment tools, and management is increasingly able to use the auditors' reports as a basis for improved risk management.

Credit Risk

Since lending is the bank's primary source of income, effective credit risk management is essential to its operations. The bank implements and regularly upgrades rigorous and formalised credit procedures that enable thorough assessment of clients' creditworthiness. Credit committees make all lending decisions based on an extensive analysis of each individual case. The composition of credit committees varies according to loan size and the complexity of the case. Lending staff receive frequent training to enhance their credit analysis skills.

The Credit Risk Committee analyses risks associated with the bank's loan portfolio. It reviews portfolio quality, monitors portfolio diversification, determines loan classifications and evaluates the potential impact of major macroeconomic changes. The committee's decisions are made with the full involvement of the Risk Department, the Credit Risk Department, the Internal Audit Department, and the management of ProCredit Bank and ProCredit Leasing.

Thanks to its effective credit risk management, the bank has achieved a low level of portfolio at risk (PAR – loans in arrears for more than 30 days). At the end of 2006, PAR stood at 0.73% (0.70% in 2005). The bank maintained high loan portfolio quality throughout the year.

Market and Liquidity Risk

In 2006 ProCredit Bank expanded its range of tools for minimising foreign currency and interest rate risks. The open currency position was monitored daily to achieve a closed position in each currency. In addition, the ALCO committee reported on the bank's open currency position on a weekly and monthly basis, ensuring compliance with all established standards.

The bank is exposed to interest rate risk because it issues most of its loans with fixed interest rates but receives credit lines with floating rates. In 2006 the bank successfully hedged its interest rate gap. It increasingly concluded loan agreements with variable interest rates for loans of relatively large amounts and with long tenors.

Liquidity risk is managed on a daily, weekly and monthly basis. We maintained a strong liquidity position throughout the year thanks to our solid customer deposit base, our predictable and stable cash flows, and our shareholders' strong support.

Operational Risk

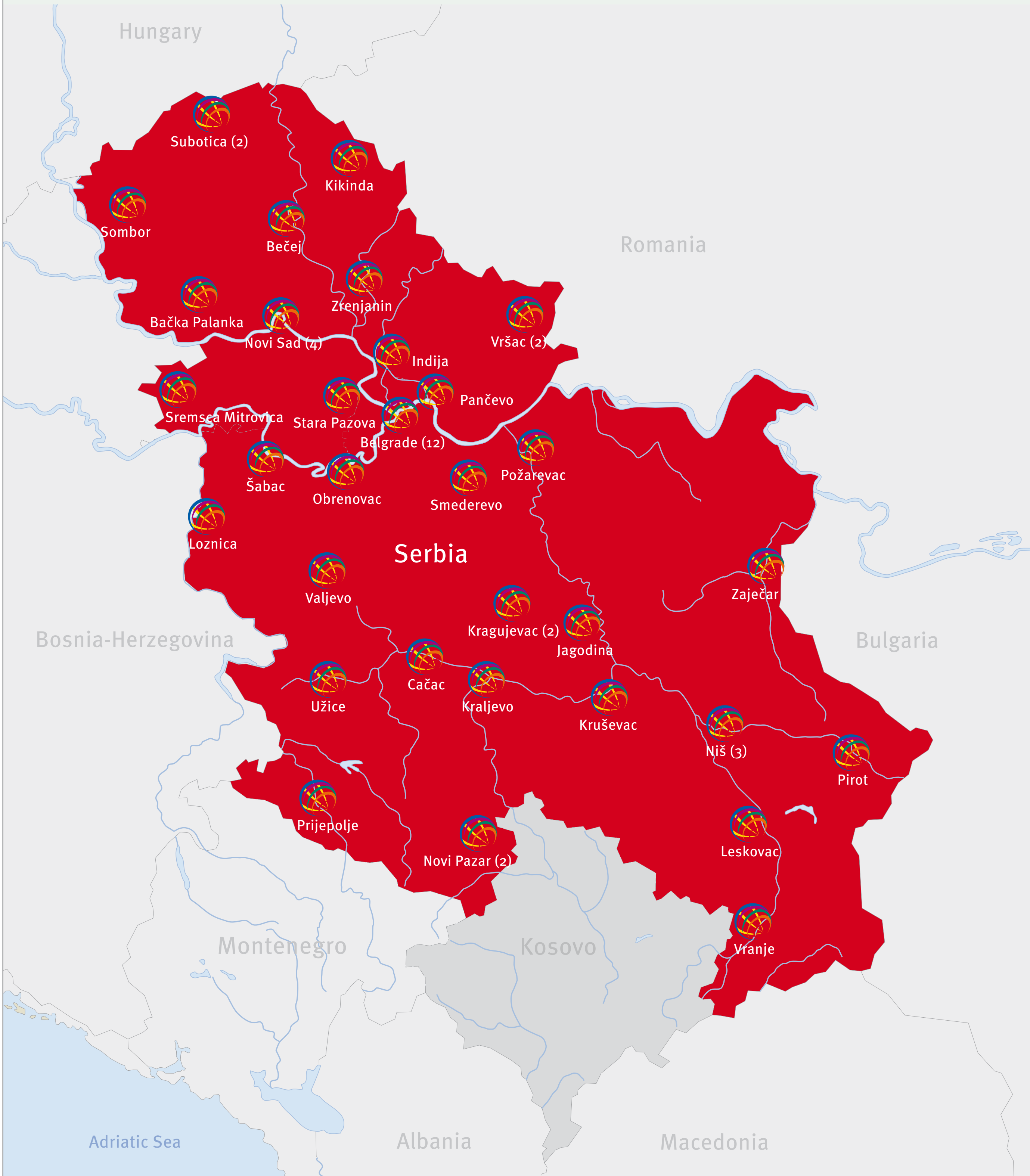
ProCredit Bank has established reliable structures for managing its operational risks. Each banking operation is based on a set of procedures and manuals. The bank applies the “four-eyes” principle in all areas of its activities. We have worked consistently to safeguard operations against fraud and misconduct, both internal and external. In 2006 we raised awareness of operational risks among staff and created a Risk Department, a Compliance Department and a Credit Control Department. The bank experienced no material losses from operational risk in 2006.

Serbian law requires all banks to report to a newly established database on operational risks. As an active participant in this process, ProCredit Bank created an internal database for recording its operational risk events. Using this tool, Risk Officers determine the sources of and potential losses from a given risk. Risk Officers also regularly analyse the bank’s processes to identify actual and potential losses, ensuring that all operations are closely monitored and controlled.

The bank’s overall risk profile is low. It has consistently maintained high loan portfolio quality and an open currency position within the required limit of 30% of equity. The bank complies with all requirements set by the National Bank of Serbia, such as the capital adequacy ratio, liquidity ratio, and exposure to a single party. The bank also observes internally defined ratios that are more stringent than those stipulated by the National Bank. ProCredit Bank’s employees are strongly committed to upholding our corporate values and adhering to prudent banking practices at all times.

Branch Network

2006 was one of the most dynamic years in terms of branch network expansion in the history of ProCredit Bank Serbia. By accelerating the pace of expansion, we achieved our ambitious goal of opening a record number of branches, which will help us to attract a larger client base. By year-end the total number of branches had risen to 52, an increase of 58% over the previous year. ProCredit Bank was among the industry leaders in terms of branch network expansion, strengthening its position as a financial institution with one of the most extensive networks in the country.



The bank opened premises in 10 new cities (Požarevac, Smederevo, Zaječar, Stara Pazova, Jagodina, Leskovac, Sremska Mitrovica, Bačka Palanka, Obrenovac and Indjija), entering several new regional markets. We also strengthened our presence in the country's regional centres (Belgrade, Novi Sad, Kragujevac and Niš) by setting up additional branches and establishing central offices that coordinate the work of branches in their respective regions. These measures enabled more Serbian citizens and businesses to gain access to high quality banking services. In addition to opening 19 new branches, the bank refurbished eight branches and enlarged seven others. This impressive growth was prompted by increased demand for our services in the respective locations.

Particular attention was given to compliance with the ProCredit corporate design standards. We made a special effort to standardise the appearance of our branches and our use of the ProCredit Bank logo. Now every branch in the country is instantly recognisable as a branch of ProCredit Bank.

Maintaining our strong market position is an ongoing challenge. We will continue to expand our branch network and improve our customer service in 2007.

Organisation, Staff and Staff Development

ProCredit Bank's success is dependent on the commitment of its employees. The bank's human resources strategy has enabled it to maintain the high service quality for which it is renowned. All four units of the HR Department – HR Administration, Recruitment/Performance Appraisal, Benefits/Banking Services and Training – actively support our expansion. In 2006, 500 new employees were recruited and trained, bringing the total number of staff members to 1,421. As a values-driven bank, we hire candidates who are not only highly qualified, but who can also identify with our corporate values and target group orientation. We make every effort to integrate new staff into the team so that they can fully share in the "ProCredit spirit".

Our rapid expansion provides employees with opportunities for career advancement, but it also poses significant challenges for HR development. Large numbers of young managers have to be selected and trained in a short period, and great care must be taken to ensure that they are adequately prepared for their new roles. Our selection process has been designed to identify the most suitable candidates for managerial positions, based on our core values.

ProCredit Bank's corporate values guide every aspect of its business. To help employees apply these values in their day-to-day work, the bank developed a set of communication guidelines. The guidelines emphasise the importance of open communication and outline how to facilitate staff meetings. They also accentuate the importance of feedback and include comprehensive evaluation guidelines for managers and other employees.

Our annual corporate events provide an opportunity for all staff to meet in a relaxed atmosphere outside of work. In 2006, 950 employees attended a weekend of sports activities in Zlatibor. We celebrated the bank's fifth anniversary on five separate occasions, with each region holding its own party. Colleagues from Romania, Bulgaria and Ukraine joined us for the festivities.

ProCredit Bank is proud to offer its employees health benefit packages. We have upgraded our health insurance programme regularly since it was introduced in 2004. Employees can also take advantage of a new loan agreement signed with the Ministry of Finance that provides loans to young employees at favourable conditions.

We regard the professional development of our employees as a long-term investment, and our level of staff training reflects this view. The bank's 2006 training and development plan was based on a detailed training needs analysis and information gathered from performance appraisals. We delivered basic, advanced, and specialist training courses designed to meet employees' development needs.

In 2006 seven groups of new Client Advisors and Loan Officers and three groups of Retail Sales Officers successfully their courses at our internal training centre. The centre also offered communication and basic sales courses to all employees who work directly with clients. In addition to classroom instruction, all new staff received extensive on-the-job training.

In 2006 the bank held more than 150 training events, amounting to a cumulative total of 600 days of training. A significant percentage of these training sessions were for our middle management development programme, which focuses on a broad range of managerial skills that are rooted in our core values.

Employees also participated in seminars organised by ProCredit Holding and our sister banks in the ProCredit group. Six of our best managers successfully completed their first year at the ProCredit Academy in Germany, and five more will begin the programme in 2007. The Academy provides young managers with a unique opportunity for professional and personal growth, and the impact is highly visible.

We aim to provide each of our employees with the opportunity for professional development. We are proud to have been named one of the 20 most attractive employers in Serbia by a public opinion poll conducted in 2006.

Business Ethics and Environmental Standards

Part of the overall mission of the ProCredit group is to set standards in the financial sectors in which we operate. We want to make a difference not only in terms of the target groups we serve and the quality of the financial services we provide, but also with regard to business ethics. Our strong **corporate values** play a key role in this respect. We have established six essential principles which guide the operations of ProCredit institutions:

- **Transparency:** We adhere to the principle of providing transparent information both to our customers and the general public and to our employees, and our conduct is straightforward and open;
- **A culture of open communication:** We are open, fair and constructive in our communication with each other, and deal with conflicts at work in a professional manner, working together to find solutions;
- **Social responsibility and tolerance:** We give our clients sound advice; their economic and financial situation, their potential and their capacities are assessed and are translated into appropriate "products"; promoting a culture of savings is important to us; we are committed to treating all customers and employees respectfully and fairly, irrespective of their origin, colour, language, gender or religious or political beliefs;
- **Service orientation:** Every client is served in a friendly, competent and courteous manner. Our employees are committed to providing excellent service to all customers, regardless of their background or the size of their business;
- **High professional standards:** Every employee takes responsibility for the quality of his/her work and strives to do his/her job even better;
- **A high degree of personal commitment:** This goes hand-in-hand with personal integrity and honesty – traits which are required of all employees in all ProCredit institutions.

These ProCredit values represent the backbone of our corporate culture and are discussed and actively applied in our day-to-day operations. Moreover, they are reflected in the Code of Conduct, which translates the ProCredit group's ethical principles into practical guidelines for all ProCredit staff. In order to ensure that staff fully understand all of the principles that have been defined, several training sessions were conducted during the year under review at which case studies were presented and grey areas discussed. We will continue to conduct such training sessions and increase their frequency in the future.

Another aspect of ensuring that our institution adheres to the highest ethical standards is our consistent application of international best-practice methods and procedures to protect ourselves from being used as a vehicle for money laundering or other illegal activities such as the financing of terrorist activities. The important focus here is to "know your customer", and, in line with this principle, to carry out sound reporting and comply with the applicable regulations.

We also set standards regarding the impact of our lending operations on the environment. ProCredit Bank Serbia has implemented an environmental management system based on continuous assessment of the loan portfolio according to environmental criteria, an in-depth analysis of all economic activities which potentially involve environmental risks, and the rejection of loan applications from enterprises engaged in activities which are deemed environmentally hazardous and appear on our institution's exclusion list. By incorporating environmental issues into the loan approval process, ProCredit Bank Serbia is also able to raise its clients' overall level of environmental awareness. We ensure that when loan applications are evaluated, compliance with ethical business practices is a key consideration. No loans are issued to enterprises or individuals if it is suspected that they are making use of unsafe or morally objectionable forms of labour, in particular child labour.

Our Clients

Mirjana Stanojkovic, Day Care Centre Owner

Pre-school education – investing in Serbia's future

Mirjana Stanojkovic founded the Meda ("Bear") day care centre in 1998. Two full-time teachers care for 18 children from 9 am to 6 pm and give the children English lessons each day. The centre is located in the village of Rakovica, near one of the most famous parks in the Belgrade area. It is a dream come true for Ms. Stanojkovic, whose greatest desire was to run a kindergarten that would give children a head start on their education.

When the centre first opened, Ms. Stanojkovic struggled to cover its expenses. She desperately wanted to create a better environment than most other day care centres offered. There was a severe shortage of proper childcare facilities in Serbia, and the waiting lists for state-run nursery schools were long. This shortage delayed the start of some children's education. Private initiatives sought to fill the gap, but many focused more on maximising profits than on investing in high quality care and facilities.

Ms. Stanojkovic did not have sufficient funds to make the investments she felt were necessary. Then she contacted ProCredit Bank. From 2002 to 2006, she obtained three loans from ProCredit to repaint the day care facility and equip it with furniture, books and toys. Ms. Stanojkovic makes all her payments through a ProCredit bank account and has repaid all her loans on time. Meda is now well-known in Rakovica for its high-quality programme, and its future – and that of the children it cares for – looks bright.

Zoran Marinkovic, Bathroom Fixture Manufacturer

A long-term vision for long-term success

Zoran Marinkovic is one of very few bathtub producers in Serbia. He makes various types of high-quality and luxury bathtubs from acrylic and polyester. Having done business with ProCredit Bank for several years, Mr. Marinkovic has taken out nine loans. He used several for working capital to settle outstanding accounts with his suppliers. Two loans were invested in equipment purchased from another ProCredit client. Thanks to these prudent investments, the company has grown rapidly. Mr. Marinkovic now employs 26 people who work in two rented production workshops and one sales showroom in Belgrade.

As the volume of his orders grew, Mr. Marinkovic considered enlarging his production facilities. He began building a new plant on the outskirts of Belgrade, but the construction project stalled. Mr. Marinkovic asked ProCredit Bank for a loan to complete the new building. He will soon consolidate his two production operations in the new facility, which will help to reduce the company's fixed costs.

Mr. Marinkovic already has ideas for his next major project. He will start importing raw materials from Holland, which will enable him to make new types of bathtubs. This material, polyurethane, will speed up the production process without jeopardising quality. Mr. Marinkovic will stay competitive, since his prices are significantly lower than those of imported products, most of which come from Western Europe and China.

Goran Stojanov, Vegetable Grower

Always one step ahead

Agriculture is a mainstay of the Serbian economy. Yet in recent years the economic crisis has brought investment in this sector to a standstill, and large state-owned agricultural enterprises have closed. Agriculture accounts for 16.8% of Serbia's total GDP and 18.4% of its total principal exports. However, very few banks are willing to lend to farmers. ProCredit Bank is the only financial institution that reaches small-scale agricultural producers – the hard-working farmers who sell their crops to bigger producers or to retail chains across the country.

Our client, Goran Stojanov, lives in the village of Baranda near the town of Pancevo with his wife, three children and his mother. His main business activity is growing vegetables, a skill passed on by his father. Mr. Stojanov is often the first farmer to deliver his products to the local market, and his distribution networks are very well structured. He supplies large-scale retail chains in Pancevo and Belgrade, sells wholesale in Pancevo, supplies vegetables to a factory producing animal feed, and takes whatever is left over to a wholesale market in Belgrade.

Over the last two years, Mr. Stojanov has improved his production process and increased his competitiveness. With a loan from ProCredit Bank, he purchased 2.5 hectares of arable land and an irrigation system. With a subsequent ProCredit loan, Mr. Stojanov built a large cooling facility, enabling him to sell vegetables all year round at a lower price. By enlarging the scale of his production, Mr. Stojanov has become more competitive and has been able to expand beyond the local market. He has boosted his income, much of which he intends to invest in next season's production.

Jasmina and Radomir Radovanovic, Savings Clients

Putting money aside for their children's education

Jasmina and Radomir Radovanovic have been married since 1992. They live together with their two children in an apartment in Kotez, an urban settlement on the outskirts of Belgrade. Several years ago they opened a small shop, Srafko, which sells construction materials. Business has been fairly good: turnover and profit have been modest but sustainable, and their client base has grown steadily. Jasmina handles accounting and banking for Srafko, while Radomir deals with suppliers and manages the shop.

The couple became ProCredit customers three years ago, first as borrowers. To date they have repaid one EUR 2,000 loan, and they currently have a EUR 4,000 working capital loan outstanding. They now also keep a business account, hold payment cards issued by the bank, and maintain a savings account.

Their two children, 11-year-old Dusan and 9-year-old Bojana, attend the same elementary school near their home. Both children excel in their schoolwork and are involved in various activities: Dusan plays football for a junior team run by a well-known Belgrade football club, and Bojana enjoys folk dancing. To provide for their future, Jasmina and Radomir decided to put aside as much as they could for Dusan and Bojana's education. Most of the proceeds from the family business go into the children's savings account, which will one day enable them to go to university.

Consolidated Financial Statements

For the year ended 31 December 2006

PRICEWATERHOUSECOOPERS

PricewaterhouseCoopers d.o.o.
Makedonska 30
11000 Belgrade
Republic of Serbia
Telephone +381 (11) 3302 100
Facsimile +381 (11) 3302 101

INDEPENDENT AUDITOR'S REPORT

To the Shareholders and Board of Directors and of ProCredit Bank a.d. Belgrade

We have audited the accompanying consolidated financial statements of ProCredit Bank a.d. Belgrade and its subsidiary (the "Group") which comprise the consolidated balance sheet as of 31 December 2006 and the consolidated income statement, consolidated statement of changes in equity and consolidated cash flow statement for the year then ended and a summary of significant accounting policies and other explanatory notes.

Management's Responsibility for the Financial Statements
Management is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with International Financial Reporting Standards. This responsibility includes: designing, implementing and maintaining internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error; selecting and applying appropriate accounting policies; and making accounting estimates that are reasonable in the circumstances.

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

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

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

PRICEWATERHOUSECOOPERS

Opinion

In our opinion, the accompanying consolidated financial statements present fairly, in all material respects, the financial position of the Group as of 31 December 2006, and of its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards.

PricewaterhouseCoopers d.o.o.

PricewaterhouseCoopers d.o.o. Belgrade

Belgrade, 20 April 2007

Consolidated Income Statement

For the year ended 31 December 2006

		Year ended 31 December	
in RSD	**Notes**	**2006**	**2005**
Interest and similar income		4,024,359	2,401,705
Interest expense and similar charges		(1,516,624)	(596,982)
Net interest income	5	**2,507,735**	**1,804,723**
Fee and commission income		361,797	231,888
Fee and commission expense		(57,254)	(33,680)
Net fee and commission income	6	**304,543**	**198,208**
Net trading income	7	(26,447)	243,227
Other operating income	8	24,065	60,261
Impairment charge for credit losses	9	(222,660)	(230,802)
Other operating expenses	10	(2,500,291)	(1,664,083)
Profit before income tax		**86,945**	**411,534**
Income tax credit	11	95,261	16,181
Profit for the year		**182,206**	**427,715**

The accompanying notes on pages 40 to 57 form an integral part of these consolidated financial statements.

Balance Sheet

For the year ended 31 December 2006

ProCredit Bank a.d. Belgrade
Consolidated Financial Statements for the year ended 31 December 2006
(All amounts expressed in thousands of Dinars unless otherwise stated)

Consolidated balance sheet

	Note	As of 31 December 2006	As of 31 December 2005
ASSETS			
Cash and balances with the Central Bank	12	13,104,952	6,934,913
Loans and advances to banks	13	977,169	388,638
Loans and advances to customers	14	23,724,909	15,532,733
Derivative financial assets	15	6,611	189
Intangible assets	16	9,697	7,806
Property and equipment	17	935,698	329,862
Deferred income tax assets	18	154,598	59,336
Other assets	19	214,244	154,582
Total assets		**39,127,878**	**23,408,059**
LIABILITIES			
Deposits from banks	20	1,954,097	1,568,696
Due to customers	21	19,005,458	12,979,945
Other borrowed funds	22	14,185,001	6,507,071
Other liabilities	23	559,492	250,472
Retirement benefit obligations	24	26,081	-
Total liabilities		**35,730,129**	**21,306,184**
EQUITY			
Share capital	25	1,920,120	1,320,120
Share premium		901,308	266,845
Retained earnings	26	576,321	514,910
Total equity		**3,397,749**	**2,101,875**
Total equity and liabilities		**39,127,878**	**23,408,059**

The accompanying notes on pages 5 to 38 form an integral part of these consolidated financial statements.

These consolidated financial statements have been approved by Executive Board on 20 April 2007 and signed on their behalf by:

Dörte Weidig
Chairperson of the Executive Board

Svetlana Tolmachova
Member of the Executive Board

2

The accompanying notes on pages 40 to 57 form an integral part of these consolidated financial statements.

Consolidated Statement of Changes in Equity

For the year ended 31 December 2006

in RSD	Notes	Share capital	Share premium	Retained earnings	Total
At 1 January 2005		**1,080,000**	**167,995**	**87,195**	**1,335,190**
Profit for the year		–	–	427,715	427,715
New shares issued	25	240,120	98,850		338,970
At 1 January 2006		**1,320,120**	**266,845**	**514,910**	**2,101,875**
Profit for the year				182,206	182,206
Dividends related to 2005		–	–	(120,795)	(120,795)
New shares issued	25	600,000	634,463		1,234,463
At 31 December 2006		**1,920,120**	**901,308**	**576,321**	**3,397,749**

The accompanying notes on pages 40 to 57 form an integral part of these consolidated financial statements.

Consolidated Cash Flow Statement

For the year ended 31 December 2006

in RSD	Year ended 31 December 2006	2005
Cash flows from operating activities:		
Profit before tax	86,945	411,534
Adjustments for non-cash items:		
Impairment loss	222,660	230,802
Depreciation and amortization	165,422	118,502
Unrealized losses/(gains) on foreign currency revaluation	19,843	(122,940)
Retirement benefits provisions	26,081	–
Net cash flow from operating activities before changes in operating assets and liabilities	**520,951**	**637,898**
Changes in operating assets:		
(Increase)/decrease in loans and advances to banks	(86,656)	49,016
(Increase)/decrease in derivative financial assets	(6,422)	2,300
Increase in loans and advances to customers	(8,434,680)	(6,235,287)
Increase in other assets	(59,662)	(281,308)
	(8,587,420)	**(6,465,279)**
Changes in operating liabilities:		
Increase/(decrease) in deposits from banks	385,401	(60,018)
Increase in due to customers	6,025,513	6,519,248
Increase in other liabilities	230,021	246,313
	6,640,935	6,705,543
Net cash (used in)/from operating activities	**(1,425,534)**	**878,162**
Cash flow from investing activities:		
Proceeds from disposal of property and equipment	2,830	31,459
Purchase of property and equipment and intangible assets	(775,980)	(182,114)
Net cash used in investment activity	**(773,150)**	**(150,655)**
Cash flow from financing activities:		
Increase of other borrowed funds	7,677,930	2,732,986
Paid dividends	(41,795)	–
Issued share capital	1,234,463	338,970
Net cash from financing activities	**8,870,598**	**3,071,956**
Net increase in cash and cash equivalents	6,671,914	3,799,463
Cash and cash equivalents as at 1 January	**7,323,551**	**3,524,088**
Cash and cash equivalents as at 31 December (Note 27)	**13,995,465**	**7,323,551**

Cash flows for the year ended 31 December 2006 include interest received in the amount of RSD 4,024,359 thousand (2005: RSD 2,401,705 thousand) and interest paid in the amount of RSD 1,516,624 thousand (2005: RSD 596,982 thousand).

The accompanying notes on pages 40 to 57 form an integral part of these consolidated financial statements.

Notes to the Consolidated Financial Statements

For the year ended 31 December 2006

All amounts expressed in thousands of in RSD unless otherwise stated

1. General information

ProCredit Bank a.d. Beograd (the “Bank”) was established in 2001 as a Joint Stock Company. The National Bank of Yugoslavia (the Central Bank) issued the Bank with a banking licence on 5 April 2001.
In 2003, the Bank changed its name from Micro Finance Bank a.d. Beograd to ProCredit Bank a.d., Beograd
The Bank’s shares are owned by four shareholders: European Bank for Reconstruction and Development (“EBRD”), London, Commerzbank AG, Frankfurt am Main, Kreditanstalt fuer Wiederaufbau, Frankfurt am Main (“KfW”) and ProCredit Holding AG, Frankfurt am Main, with holdings of 16.67 percent, 16.67 percent, 9.37 percent and 57.29 percent of the Bank’s shares, respectively.
The Bank is licensed in the Republic of Serbia to perform payment transfers, credit and deposit activities in the country and abroad, and in accordance with the laws of the Republic of Serbia, is to operate on the principles of liquidity, security of placements and profitability.
The Bank has established ProCredit Leasing d.o.o. as a Limited Liability Company. ProCredit Leasing d.o.o. is registered with the Agency for Legal Entities Belgrade under registration number 1973/2005, dated 17 February 2005. The Bank owns a 100% share of ProCredit Leasing.
The Group consists of the Bank and its subsidiary ProCredit Leasing d.o.o.
As of 31 December 2006, the Group had a head office located in Belgrade, Bul. despota Stefana 68c, and 52 branches throughout Serbia.
As at 31 December 2006 the Group had 1,418 employees (31 December 2005: 1,015 employees).

2. Summary of significant accounting policies

The principal accounting policies applied in the preparation of these consolidated financial statements are set out below. These policies have been consistently applied to all the years presented, unless otherwise stated.

A) Basis of preparation

The Group’s consolidated financial statements have been prepared in accordance with International Financial Reporting Standards (IFRS). The consolidated financial statements have been prepared under the historical cost convention, as modified by the revaluation of derivative financial instruments.
The preparation of financial statements in conformity with IFRS requires the use of certain critical accounting estimates. It also requires management to exercise its judgment in the process of applying the Group’s accounting policies. The areas involving a higher degree of judgment or complexity, or areas where assumptions are significant to the consolidated financial statements are disclosed in Note 3.

(a) Amendments to published standards and interpretations effective 1 January 2006

The application of the amendments and interpretations listed below did not result in substantial changes to the Group’s accounting policies:

IAS 19 Amendment – Actuarial Gains and Losses, Group Plans and Disclosures;
IAS 21 Amendments – Net Investment in a Foreign Operation;
IAS 39 Amendments – Cash Flow Hedge Accounting of Forecast Intragroup Transactions;
IAS 39 Amendments – The Fair Value Option;
IAS 39 and IFRS 4 Amendment – Financial Guarantee Contracts;
IFRS 1 (Amendment), First-time Adoption of International Financial Reporting Standards, and IFRS 6 (Amendment), Exploration for and Evaluation of Mineral Resources;
IFRS 6, Exploration for and Evaluation of Mineral Resources;
IFRIC 4, Determining whether an Arrangement contains a Lease;
IFRIC 5, Rights to Interests arising from Decommissioning, Restoration and Environmental Rehabilitation Funds; and
IFRIC 6, Liabilities arising from Participating in a Specific Market – Waste Electrical and Electronic Equipment.

- IAS 19 Amendment introduces the option of an alternative recognition approach for actuarial gains and losses. It also adds new disclosure requirements. As the Group does not intend to change the accounting policy adopted for recognition of actuarial gains and losses and does not participate in any multi-employer plans, adoption of this amendment only impacts the format and extent of disclosures presented in the accounts.
- IAS 21 Amendment, IAS 39 Amendment – Cash flow hedge accounting of forecasted intragroup transactions, IFRS 1, IFRS 6, IFRIC 4, IFRIC 5 and IFRIC 6 are not relevant to the Group’s operating activities and therefore have no material effect on the Group’s policies.
- IAS 39 Amendment – The Fair Value Option. The Group did not have financial assets and financial liabilities at fair value through profit and loss during reporting period.
- IAS 39 and IFRS 4 Amendment – Financial Guarantee Contracts. These types of contract are now accounted for under IAS 39 and no longer accounted for under IFRS 4, as previously required under IFRS. The measurement and disclosure requirements under IAS 39 have not resulted in a material change to the Group’s policies, due to the fact that the Group did not have financial guarantees during reporting period.

(b) Standards, interpretations and amendments issued but not yet effective

The Group has chosen not to early adopt the following standards and interpretations that were issued but not yet effective for accounting periods beginning on 1 January 2006:

- Amendment to IAS 1 – Capital disclosures
- IAS 21, Borrowing costs;
- IFRS 8, Operating Segments (effective 1 January 2008);
- IFRS 7, Financial instruments: Disclosures
- IFRIC 7, Applying the Restatement Approach under IAS 29 (effective 1 March 2006);
- IFRIC 8, Scope of IFRS 2 (effective 1 May 2006);
- IFRIC 9, Reassessment of embedded derivatives (effective 1 June 2006);
- IFRIC 10, Interim Financial Reporting and Impairment (effective 1 November 2006);
- IFRIC 11, IFRS 2 – Group Treasury Share Transactions (effective 1 March 2007); and
- IFRIC 12, Service Concession Arrangements (effective 1 January 2009).

IFRS 7, Financial Instruments: Disclosures, and a complementary amendment to IAS 1, Presentation of Financial Statements – Capital Disclosures (effective from 1 January 2007). IFRS introduces new disclosures to improve the information about financial instruments. It requires the disclosure of qualitative and quantitative information about exposure to risks arising from financial instruments, including specified minimum disclosures about credit risk, liquidity risk and market risk, including sensitivity analysis to market risk. The amendment to IAS 1 introduces disclosures about the level of an entity's capital and how it manages capital.

The Group assessed the impact of IFRS 7 and the amendment to IAS 1 and concluded that the main additional disclosures will be:

(i) Credit risk

- maximum exposure to credit risk ('current exposure') without taking account of any collateral held or other credit enhancements (e.g. guarantees received, netting agreements);
- description of collaterals / other credit enhancements in respect of the amounts disclosed;
- analysis of repossessed collateral;
- credit quality of financial assets neither past due nor impaired;
- analysis of the age of financial assets past due but not impaired;
- analysis of financial assets individually determined to be impaired;
- the sensitivity analysis to market risk and the capital disclosures required by the amendment of IAS 1.

(ii) Market risk measurement techniques and sensitivity analysis to market risk.

(iii) Capital management disclosures required by the amendment to IAS 1.
The Group will apply IFRS 7 and the amendment to IAS 1 to annual periods starting from 1 January 2007.
The application of all other new standards, interpretations and amendments will not have a material impact on the Group's financial statements in the period of initial application.

B) Consolidation

(a) Subsidiaries
Subsidiaries are all entities over which the Group has the power to govern the financial and operating policies generally accompanying a shareholding of more than one half of the voting rights.
The Bank has only one 100% owned subsidiary – ProCredit Leasing d.o.o.
Inter-company transactions, balances and unrealized gains on transactions between group companies are eliminated. Unrealized losses are also eliminated unless the transaction provides evidence of impairment of the asset transferred. The accounting policies of subsidiaries have been changed where necessary to ensure consistency with the policies adopted by the Group.

C) Foreign currency translation

(a) Functional and presentation currency
Items included in the financial statements of each of the Group's entities are measured using the currency of the primary economic environment in which the entity operates ('the functional currency'). The consolidated financial statements are presented in RSD, which is the functional and presentation currency of the Group entities.

(b) Transactions and balances
Foreign currency transactions are translated into the functional currency using the exchange rates prevailing at the dates of the transactions. Foreign exchange gains and losses resulting from the settlement of such transactions and from the translation at year-end exchange rates of monetary assets and liabilities denominated in foreign currencies are recognized in the income statement.

D) Financial assets

The Group classifies its financial assets in the following categories: financial assets at fair value through profit or loss; loans and receivables; held-to-maturity investments; and available-for-sale financial assets. Management determines the classification of its investments at initial recognition.

(a) Financial assets at fair value through profit or loss
This category has two sub-categories: financial assets held for trading, and those designated at fair value through profit or loss at inception.
A financial asset is classified as held for trading if it is acquired or incurred principally for the purpose of selling or repurchasing in the near term or if it is part of a portfolio of identified financial instruments that are managed together and for which there is evidence of a recent actual pattern of short-term profit-taking. Derivatives are also categorized as held for trading unless they are designated as hedging instruments.
Financial assets and financial liabilities are designated at fair value through profit or loss when:

- doing so significantly reduces measurement inconsistencies that would arise if the related derivatives were treated as held for trading and the underlying financial instruments were carried at amortized cost for loans and advances to customers or banks and debt securities in issue;
- certain investments, such as equity investments, are managed and evaluated on a fair value basis in accordance with a documented risk management or investment strategy and reported to key management personnel on that basis; and
- financial instruments, such as debt securities held, containing one or more embedded derivatives significantly modify the cash flows.

Gains and losses arising from changes in the fair value of derivatives that are managed in conjunction with designated financial assets or financial liabilities are included in "Other operating income".
The Group did not designate any financial asset as at fair value through profit or loss during the reporting period.

(b) Loans and receivables
Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. All loans and advances are initially recognized at fair value. All loans and advances are recognized when cash is advanced to borrowers. After initial recognition, these are subsequently measured at amortized costs using the effective interest rate method. Amortized cost is calculated by taking into account any issue costs and any discount or premium on settlement.

(c) Held-to-maturity financial assets
Held-to-maturity investments are non-derivative financial assets with fixed or determinable payments and fixed maturities that the Group's management has the positive intention and ability to hold to maturity. If the Group were to sell other than an insignificant amount of held-to-maturity assets, the entire category would be reclassified as available for sale.
The Group did not classify any financial assets as held-to-maturity during the reporting period.

(d) Available-for-sale financial assets

Available-for-sale investments are those intended to be held for an indefinite period of time, which may be sold in response to needs for liquidity or changes in interest rates, exchange rates or equity prices.

The Group did not classify any financial assets as available-for-sale during the reporting period.

Regular-way purchases and sales of financial assets at fair value through profit or loss, held to maturity and available for sale are recognized on trade-date – the date on which the Group commits to purchase or sell the asset.

Financial assets are initially recognized at fair value plus transaction costs for all financial assets not carried at fair value through profit or loss. Financial assets carried at fair value through profit or loss are initially recognized at fair value and transaction costs are expensed in the income statement. Available-for-sale financial assets and financial assets at fair value through profit or loss are subsequently carried at fair value. Loans and receivables and held-to-maturity investments are carried at amortized cost using the effective interest method.

Gains and losses arising from changes in the fair value of the 'financial assets at fair value through profit or loss' category are included in the income statement in the period in which they arise. Gains and losses arising from changes in the fair value of available-for-sale financial assets are recognized directly in equity, until the financial asset is derecognized or impaired. At this time, the cumulative gain or loss previously recognized in equity is recognized in profit or loss. However, interest calculated using the effective interest method and foreign currency gains and losses on monetary assets classified as available for sale is recognized in the income statement.

The fair values of quoted investments in active markets are based on current bid prices. If there is no active market for a financial asset, the Group establishes fair value using valuation techniques. These include the use of recent arm's length transactions, discounted cash flow analysis, and other valuation techniques commonly used by market participants.

E) Offsetting financial instruments

Financial assets and liabilities are offset and the net amount reported in the balance sheet when there is a legally enforceable right to offset the recognized amounts and there is an intention to settle on a net basis, or realize the asset and settle the liability simultaneously.

F) Derivative financial instruments and hedge accounting

Derivatives are initially recognized at fair value on the date on which a derivative contract is entered into and are subsequently remeasured at their fair value. Fair values are obtained from quoted market prices in active markets, including recent market transactions, and valuation techniques, including discounted cash flow models as appropriate. All derivatives are carried as assets when fair value is positive and as liabilities when fair value is negative. Gains and losses arising from changes in fair value of derivatives are included in "Net trading income".

The Group undertook only economic hedging transactions during the reporting period.

G) Interest income and expense

Interest income and expense for all interest-bearing financial instruments are recognized within 'interest income' and 'interest expense' in the income statement using the effective interest method.

The effective interest method is a method of calculating the amortized cost of a financial asset or a financial liability and of allocating the interest income or interest expense over the relevant period. The effective interest rate is the rate that exactly discounts estimated future cash payments or receipts through the expected life of the financial instrument or, when appropriate, a shorter period to the net carrying amount of the financial asset or financial liability. When calculating the effective interest rate, the Group estimates cash flows considering all contractual terms of the financial instrument but does not consider future credit losses. The calculation includes all fees and points paid or received between parties to the contract that are an integral part of the effective interest rate, transaction costs and all other premiums or discounts.

Once a financial asset or a group of similar financial assets has been written down as a result of an impairment loss, interest income is recognized using the rate of interest used to discount the future cash flows for the purpose of measuring the impairment loss.

H) Fee and commission income

Fees and commissions are generally recognized on an accrual basis when the service has been provided. Loan commitment fees for loans that are likely to be drawn down are deferred (together with related direct costs) and recognized as an adjustment to the effective interest rate on the loan.

I) Sale and repurchase agreements

Securities purchased under agreements to resell ('reverse repos') are recorded as cash and balances with the Central Bank, as appropriate. Reverse repos are included in cash and cash equivalents if they have a maturity less than three months from the date of acquisition. The difference between sale and repurchase price is treated as interest and accrued over the life of the agreements using the effective interest method. Securities lent to counterparties are also retained in the financial statements.

J) Impairment of financial assets carried at amortized cost

The Group assesses at each balance sheet date whether there is objective evidence that a financial asset or group of financial assets is impaired. A financial asset or a group of financial assets is impaired and impairment losses are incurred only if there is objective evidence of impairment as a result of one or more events that occurred after the initial recognition of the asset (a 'loss event') and that loss event (or events) has an impact on the estimated future cash flows of the financial asset or group of financial assets that can be reliably estimated.

The criteria that the Group uses to determine that there is objective evidence of an impairment loss include:

- Delinquency in contractual payments of principal or interest;
- Cash flow difficulties experienced by the borrower (for example, equity ratio, net income percentage of sales);
- Breach of loan covenants or conditions;
- Initiation of bankruptcy proceedings;
- Deterioration of the borrower's competitive position;
- Deterioration in the value of collateral; and
- Downgrading below investment grade level.

The estimated period between a loss occurring and its identification is determined by local management for each identified portfolio. In general, the periods used vary between three months and 12 months; in exceptional cases, longer periods are warranted.

The Group first assesses whether objective evidence of impairment exists individually for financial assets that are individually significant, and individually or collectively for financial assets that are not individually significant. If the Group determines that no objective evidence of impairment exists for an individually assessed financial asset, whether significant or not, it includes the asset in a group of financial assets with similar credit risk characteristics and collectively assesses them for impairment. Assets that are individually assessed for impairment and for which an impairment loss is or continues to be recognized are not included in a collective assessment of impairment.

The amount of the loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows (excluding future credit losses that have not been incurred) discounted at the financial asset's original effective interest rate. The carrying amount of the asset is reduced through the use of an allowance account and the amount of the loss is recognized in the income statement.

The calculation of the present value of the estimated future cash flows of a collateralized financial asset reflects the cash flows that may result from foreclosure less costs for obtaining and selling the collateral, whether or not foreclosure is probable.

For the purposes of a collective evaluation of impairment, financial assets are grouped on the basis of similar credit risk characteristics (i.e., on the basis of the Group's grading process that considers asset type, industry, geographical location, collateral type, past-due status and other relevant factors). Those characteristics are relevant to the estimation of future cash flows for groups of such assets by being indicative of the debtors' ability to pay all amounts due according to the contractual terms of the assets being evaluated.

Future cash flows in a group of financial assets that are collectively evaluated for impairment are estimated on the basis of the contractual cash flows of the assets in the group and historical loss experience for assets with credit risk characteristics similar to those in the group. Historical loss experience is adjusted on the basis of current observable data to reflect the effects of current conditions that did not affect the period on which the historical loss experience is based and to remove the effects of conditions in the historical period that do not currently exist.

Estimates of changes in future cash flows for groups of assets should reflect and be directionally consistent with changes in related observable data from period to period (for example, changes in unemployment rates, property prices, payment status, or other factors indicative of changes in the probability of losses in the group and their magnitude). The methodology and assumptions used for estimating future cash flows are reviewed regularly by the Group to reduce any differences between loss estimates and actual loss experience.

When a loan is uncollectible, it is written off against the related provision for loan impairment. Such loans are written off after all the necessary procedures have been completed and the amount of the loss has been determined.

If, in a subsequent period, the amount of the impairment loss decreases and the decrease can be related objectively to an event occurring after the impairment was recognized (such as an improvement in the debtor's credit rating), the previously recognized impairment loss is reversed by adjusting the allowance account. The amount of the reversal is recognized in the income statement in impairment charge for credit losses.

K) Intangible assets

Acquired computer software licences are capitalized on the basis of the costs incurred to acquire and bring to use the specific software. These costs are amortized on the basis of the expected useful lives of the software and the periods for which licences are issued. Costs associated with developing or maintaining computer software programs are recognized as an expense as incurred.

L) Property and equipment

All property and equipment is stated at historical cost less depreciation. Historical cost includes expenditure that is directly attributable to the acquisition of the items.

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

Depreciation of fixed assets is calculated using the straight-line method to allocate their cost to their residual values over their estimated useful lives, as follows:

- Leasehold improvements – at least 10 years, or leasehold contract duration if longer,
- Motor vehicles – 4 years,
- Furniture – 6-8 years,
- Computers – 3 years;

The assets' residual values and useful lives are reviewed, and adjusted if appropriate, at each balance sheet date.

Gains and losses on disposals are determined by comparing proceeds with carrying amount. These are included in other operating expenses in the income statement.

M) Impairment of non-financial assets

Assets that are subject to amortization are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. An impairment loss is recognized for the amount by which the asset's carrying amount exceeds its recoverable amount. The recoverable amount is the higher of an asset's fair value less costs to sell and value in use. For the purposes of assessing impairment, assets are grouped at the lowest levels for which there are separately identifiable cash flows (cash-generating units).

N) Leases

(a) A Group company is the lessee

Leases in which a significant portion of the risks and rewards of ownership are retained by the lessor are classified as operating leases.

The leases entered into by the Group are primarily operating leases. The total payments made under operating leases are charged to other operating expenses in the income statement on a straight-line basis over the period of the lease.

When an operating lease is terminated before the lease period has expired, any payment required to be made to the lessor by way of penalty is recognized as an expense in the period in which termination takes place.

(b) A Group company is the lessor

When assets are held subject to a finance lease, the present value of the lease payments is recognized as a receivable. The difference between the gross receivable and the present value of the receivable is recognized as unearned finance income. Lease income is recognized over the term of the lease using the net investment method (before tax), which reflects a constant periodic rate of return.

O) Cash and cash equivalents

For the purposes of the cash flow statement, cash and cash equivalents comprise balances with less than a three-month maturity from the date of acquisition, including cash and non-restricted balances with the Central Bank, treasury bills and other eligible bills, loans and advances to banks, amounts due from other banks and short-term government securities.

P) Provisions

Provisions for legal claims are recognized when: the Group has a present legal or constructive obligation as a result of past events; it is more likely than not that an outflow of resources will be required to settle the obligation; and the amount has been reliably estimated.

Where there are a number of similar obligations, the likelihood that an outflow will be required in settlement is determined by considering the class of obligations as a whole. A provision is recognized even if the likelihood of an outflow with respect to any item included in the same class of obligations may be small.

Provisions are measured at the present value of the expenditures expected to be required to settle the obligation using a pre-tax rate that reflects current market assessments of the time value of money and the risks specific to the obligation. The increase in the provision due to passage of time is recognized as interest expense.

Q) Financial guarantee contracts

Financial guarantee contracts are contracts that require the issuer to make specified payments to reimburse the holder for a loss it incurs because a specified debtor fails to make payments when due, in accordance with the terms of a debt instrument. Such financial guarantees are given to banks, financial institutions and other bodies on behalf of customers to secure loans, overdrafts and other banking facilities.

Financial guarantees are initially recognized in the financial statements at fair value on the date the guarantee was given. Subsequent to initial recognition, the bank's liabilities under such guarantees are measured at the higher of the initial measurement, less amortization calculated to recognize in the income statement the fee income earned on a straight line basis over the life of the guarantee and the best estimate of the expenditure required to settle any financial obligation arising at the balance sheet date. These estimates are determined based on the experience of similar transactions and the history of past losses, supplemented by the management's judgment.

Any increase in the liability relating to guarantees is recognised in the income statement under other operating expenses.

The Group did not have any financial guarantees during the reporting period.

R) Employee benefits

(a) Pension obligations

The Group operates a defined contribution pension plan. The Group companies pay contributions to publicly administered pension insurance plans on a mandatory basis. The Group has no further payment obligations once the contributions have been paid. The contributions are recognized as employee benefit expense when they are due. Prepaid contributions are recognized as an asset to the extent that a cash refund or a reduction in the future payments is available.

(b) Retirement benefit scheme

The Group companies provide a retirement benefit scheme for employees, as required by the Labour code in Serbia. Entitlement to these benefits is usually conditional on the employee remaining in service up to retirement age and/or the completion of a minimum service period and is calculated as three average monthly salaries in Serbia, as of the month preceding the employee's retirement. The expected costs of these benefits are accrued over the period of employment. The defined benefit obligation is valued annually by independent qualified actuaries using the projected unit credit method. The present value of the defined benefit obligation is determined by discounting the estimated future cash outflows using interest rates of high-quality corporate bonds that are denominated in the currency in which the benefits will be paid and that have terms to maturity approximating to the terms of the related pension liability. Actuarial gains and losses arising from experience adjustments, and changes in actuarial assumptions in excess of the greater of 10% of the value of plan assets or 10% of the defined benefit obligation, are charged or credited to income over the expected average remaining working lives of the related employees.

The assumptions used by the actuary in calculating the retirement benefits are as follows:

- Three average salaries in December 2006, based on the Ser bian economy as a whole;
- Estimated annual increase in salaries of 3.5%; and
- Discounting rate of 10%.

S) Deferred income tax

Deferred income tax is provided in full, using the liability method, on temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the consolidated financial statements.

Deferred income tax is determined using tax rates (and laws) that have been enacted or substantially enacted by the balance sheet date and are expected to apply when the related deferred income tax asset is realized or the deferred income tax liability is settled.

The principal temporary differences arise from depreciation of property and equipment, revaluation of certain financial assets and liabilities including derivative contracts, provisions for pensions and other post-retirement benefits and tax losses carried forward. The rates enacted or substantively enacted at the balance sheet date are used to determine deferred income tax.

Deferred tax assets are recognized where it is probable that future taxable profit will be available against which the temporary differences can be utilized.

The tax effects of income tax losses available for carry-forward are recognized as an asset when it is probable that future taxable profits will be available against which these losses can be utilized.

Deferred tax related to fair value re-measurement of available-for-sale investments, which are charged or credited directly to equity, is also credited or charged directly to equity and subsequently recognized in the income statement together with the deferred gain or loss.

T) Borrowings

Borrowings are recognized initially at fair value net of transaction costs incurred. Borrowings are subsequently stated at amortized cost; any difference between proceeds net of transaction costs and the redemption value is recognized in the income statement over the period of the borrowings using the effective interest method.

U) Share capital

(a) Share issue costs

Incremental costs directly attributable to the issue of new shares or options or to the acquisition of a business are shown in equity as a deduction, net of tax, from the proceeds.

(b) Dividends on ordinary shares

Dividends on ordinary shares are recognized in equity in the period in which they are approved by the Bank's shareholders.

Dividends for the year that are declared after the balance sheet date are dealt with in the subsequent events note.

V) Comparatives

Where necessary, comparative figures have been reclassified to conform with changes in presentation in the current year. The amounts of reclassifications in the balance sheet and the income statement are not material.

Reclassifications in the cash flow statement were made as follows:

- Cash and cash equivalents as at 31 December 2005 and 2004 were increased by RSD 509,764 thousand and RSD 388,637 thousand, respectively, due to reclassification of Nostro accounts in foreign banks and short-term money market placements to cash and cash equivalents. As a result the 'decrease in loans and advances to banks' for 2005 was reduced by RSD 127,417 thousand;
- The positions 'Income tax' and 'Increase in deferred income tax assets' were netted in the amount of RSD 16,181 thousand;
- 'Other non-cash items' in the amount of RSD 2,872 thousand were transferred to 'Purchase of property and equipment';
- 'Losses on disposal of property and equipment' in amount of RSD 49,539 thousand, were transferred to 'Purchase of property and equipment';
- The position 'Increase / (decrease) in financial liabilities at fair value through profit and loss' in the amount of RSD 3,477 was reclassified to the position 'Increase in other liabilities'.

3. Critical accounting estimates and judgments

The Group makes estimates and assumptions that affect the reported amounts of assets and liabilities within the next financial year. Estimates and judgments are continually evaluated and based on historical experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances.

(a) Impairment losses on loans and advances

The Group reviews its loan portfolio to assess impairment at least on a monthly basis. In determining whether an impairment loss should be recorded in the income statement, the Group 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 an adverse change in the payment status of borrowers in a group, or national or local economic conditions that correlate with defaults on assets in the group. 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.

(b) Provisions

Provisions, in general, are highly judgmental, especially in the cases of legal disputes. The Group assesses the probability of the occurrence of an adverse event as a result of a past event, and if the probability is evaluated to be more than fifty percent, the Group fully provides for the total amount of the liability. The Group is rather prudent in these assessments, but due to the high level of uncertainty, in some cases the evaluation may prove not to be in line with the eventual outcome of the case.

4. Financial risk management

The Group's activities expose it to a variety of financial risks and those activities involve the analysis, evaluation, acceptance and management of some degree of risk or combination of risks. Taking risk is core to the financial business, and the operational risks are an inevitable consequence of being in business. The Group's aim is therefore to achieve an appropriate balance between risk and return and minimize potential adverse effects on the Group's financial performance.
The Group's risk management procedures are designed to identify and analyze these risks, to set appropriate risk limits and controls, and to monitor the risks and adherence to limits by means of reliable and up-to-date information systems. The Group regularly reviews its risk management procedures and systems to reflect changes in markets, products and emerging best practice.
Risk management is carried out by a central Risk Department and the Group's Risk Committees under procedures approved by the Board of Directors. The Risk Department identifies, evaluates and hedges financial risks in close co-operation with the Group's operating units. The Board provides principles for overall risk management, as well as written policies covering specific areas, such as foreign exchange risk, interest rate risk, credit risk, use of derivative financial instruments and non-derivative financial instruments. In addition, internal audit is responsible for the independent review of risk management and the control environment.
The most important types of risk are credit risk, liquidity risk, market risk and other operational risk. Market risk includes currency risk, interest rate and other price risk.

A. Credit risk

The Group takes on exposure to credit risk which is the risk that a counterparty will be unable to pay amounts in full when due. The Group's primary exposure to credit risk arises through its loans.

To manage the level of credit risk, the Group:

- reviews the creditworthiness of customers applying for loans, guarantees and other credit products,
- establishes credit limits on the basis of the risk assessment,
- deals with counterparties of good credit standing and takes appropriate collateral.

Customers are monitored continually and risk limits are adjusted if necessary. The risk limits also take into account different collateral types.
Although no limits are prescribed for sector concentration, this factor is constantly monitored. The exposure to any borrower including banks is further restricted by sub-limits covering on and off-balance sheet exposures. Total exposures are monitored against the limits prior to entering into transactions.

Credit-related commitments

The primary purpose of these instruments is to ensure that funds are available to a customer as required. Guarantees and standby letters of credit, which represent irrevocable assurances that the Group will make payments in the event that a customer cannot meet its obligations to third parties, carry the same credit risk as loans

B. Market risk

It is the policy of the Group not to engage in any speculative transactions and to keep all types of risk at an acceptable level. Market risks arise from open positions in interest rate, currency and equity products, all of which are exposed to general and specific market movements and changes in the level of volatility of market rates or prices such as interest rates, credit spreads, foreign exchange rates and equity prices. The Group complies with the limits on acceptable levels of risk that are prescribed by the Central Bank as well as with limits set by the Risk Committees.

B.1. Foreign currency risk

Foreign currency risk exposure is monitored regularly through compliance with the regulatory limits prescribed by the Central Bank. The Group maintains the foreign currency position by granting loans with foreign currency clauses. On the other hand, the Group takes an active approach to currency risk management, and it prudently assesses and manages open foreign currency positions, engaging in foreign currency swaps and keeping foreign currency risk exposure within the limits set by the Central Bank, as well as being in compliance with internal rules and limits prescribed by the Management and Risk Committees.

The table below summarizes the Group's exposure to foreign currency exchange risk at 31 December. Included in the table are the Group's assets and liabilities at carrying amounts, categorized by currency.

	EUR	USD	Other currencies	Totel foreign currencies	Local currency	Total
As of 31 December 2006						
Assets						
Cash and balances with the Central Bank	9,027,990	364,244	21,876	9,414,110	3,690,842	13,104,952
Loans and advances to banks	532,869	73,451	9,612	615,932	361,237	977,169
Loans and advances to customers	21,629,602	–	–	21,629,602	2,095,307	23,724,909
Derivative financial assets	–	–	–	–	6,611	6,611
Intangible assets	–	–	–	–	9,697	9,697
Property and equipment	–	–	–	–	935,698	935,698
Deferred income tax assets	–	–	–	–	154,598	154,598
Other assets	58,335	21,621	5	79,961	134,283	214,244
Total assets	**31,248,796**	**459,316**	**31,493**	**31,739,605**	**7,388,273**	**39,127,878**
Liabilities						
Deposits from banks	1,841,625	91,023	1,446	1,934,094	20,003	1,954,097
Due to customers	14,900,217	613,166	29,005	15,542,388	3,463,070	19,005,458
Other borrowed funds	14,185,001	–	–	14,185,001	–	14,185,001
Other liabilities	223,046	47,541	19,679	290,266	269,226	559,492
Retirement benefit obligations	–	–	–	–	26,081	26,081
Equity	–	–	–	–	3,397,749	3,397,749
Total liabilities and equity	**31,149,889**	**751,730**	**50,130**	**31,951,749**	**7,176,129**	**39,127,878**
Net balance sheet position	**98,907**	**(292,414)**	**(18,637)**	**(212,144)**	**212,144**	**–**
As of 31 December 2005						
Total assets	21,148,082	495,888	5,529	21,649,499	1,758,560	23,408,059
Total liabilities and equity	18,899,819	876,846	–	19,776,665	3,631,394	23,408,059
Net balance sheet position	**2,248,263**	**(380,958)**	**5,529**	**1,872,834**	**(1,872,834)**	**–**

As of 31 December 2006 the Group's open currency position in USD currency was hedged in the amount RSD 292,081 thousand (the net open currency position in USD after hedging was RSD 334 thousand). Open currency positions in other currencies were hedged in the amount of RSD 14,181 thousand (the net open currency position in other currencies after hedging was RSD 4,184 thousand). The Group undertook only economic hedging transactions during the reporting period.

B.2. Interest rate risk

The Group takes on exposure to the effects of fluctuations in the prevailing levels of market interest rates on its financial position and cash flows. Interest margins may increase as a result of such changes but may reduce or create losses in the event that unexpected movements arise. Interest rates are based on market rates and the Group reprices its rates regularly.

Risk management activities are aimed at optimizing net interest income, given market interest rate levels consistent with the Group's business strategies. In managing maturity structure, senior management considers among others:

- macro- and microeconomic forecasts,
- forecasts in liquidity conditions and
- anticipated trends in interest rates.

The interest rate risk present in the gap between the repricing maturities of long-term borrowings linked to floating rates, and the repricing maturities of loans disbursed at floating interest rates is prudently hedged with fixed-for-floating interest rate swaps. As of December 31 2006 the Group had outstanding interest rate swaps of EUR 15.8 million. The Group undertook only economic hedging transactions during the reporting period.

The table below summarizes the effective interest rate by major currencies for monetary financial instruments not carried at fair value through profit or loss:

			2006			2005
in %	**RSD**	**EUR**	**USD**	**RSD**	**EUR**	**USD**
Assets						
Cash and balances with the Central Bank	2.50	–	–	2.97	–	–
Loans and advances to banks	16.67	4.08	–	6.65	3.19	–
Loans and advances to customers	26.73	16.56	–	–	16.68	–
Reverse repo placements	11.50	–	–	–	–	–
Other placements with the Central Bank	10.26	–	–	3.57	–	–
Liabilities						
Deposits and loans from banks	12.23	7,63	–	8.37	3.38	3.57
Due to customers						
Current accounts	1.69	–	–	1.43	–	–
Savings accounts	7.89	2.36	1.49	4.70	2.29	1.47
Term deposits	9.96	4.40	2.95	9.20	4.60	3.51
Other borrowed funds	–	6.63	–	–	5.32	–

The table below summarizes the Group's exposure to interest rate risks. Included in the table are the Group's assets and liabilities at carrying amounts, categorized by the earlier of contractual repricing or maturity dates.

	Up to 30 days	**1 – 6 months**	**6 – 12 months**	**More than 12 months**	**Non-interest bearing assets**	**Total**
Assets						
Cash and balances with the Central Bank	3,467,334	–	–	–	9,637,618	13,104,952
Loans and advances to banks	977,169	–	–	–	–	977,169
Loans and advances to customers	10,267,298	3,727,845	3,470,598	6,075,490	183,678	23,724,909
Derivative financial assets	–	–	–	–	6,611	6,611
Intangible assets	–	–	–	–	9,697	9,697
Property and equipment	–	–	–	–	935,698	935,698
Deferred income tax assets	–	–	–	–	154,598	154,598
Other assets	–	–	–	214,244	214,244	
Total assets	**14,711,801**	**3,727,845**	**3,470,598**	**6,075,490**	**11,142,144**	**39,127,878**
Liabilities						
Deposits from banks	1,891,948	62,149	–	–	–	1,954,097
Due to customers	7,351,363	6,115,807	3,548,743	1,782,019	207,526	19,005,458
Other borrowed funds	8,417,088	3,540,927	0	2,113,250	113,736	14,185,001
Other liabilities	–	–	–	–	559,492	559,492
Retirement benefit obligations	–	–	–	–	26,081	26,081
Equity	–	–	–	–	3,397,749	3,397,749
Total liabilities	**17,660,399**	**9,718,883**	**3,548,743**	**3,895,269**	**4,304,584**	**39,127,878**
Interest sensitivity gap	**(2,948,598)**	**(5,991,038)**	**(78,145)**	**2,180,221**	**6,837,560**	**–**
As of 31 December 2005						
Total assets	4,446,743	1,592,034	5,403,955	5,363,559	6,601,768	23,408,059
Total liabilities	**5,834,070**	**9,893,043**	**2,746,471**	**2,411,848**	**2,522,627**	**23,408,059**
Interest sensitivity gap	**(1,387,327)**	**(8,301,009)**	**2,657,484**	**2,951,711**	**4,079,141**	**–**

C. Liquidity risk

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

The Group has a diversified funding base which includes:
- customer deposits with wide ranges of maturity
- money market deposits
- loans from foreign banks and financial institutions
- subordinated debt
- share capital

The Group continually assesses liquidity risk by identifying and monitoring changes in the level of funding required in order to meet business goals and targets set within the terms of the Group's overall strategy.
The table below analyzes the assets and liabilities of the Group, assigning them to relevant maturity groupings based on the remaining period at balance sheet date to the contractual maturity date.

	Less than 1 month	1 – 3 months	3 – 12 months	More than 1 year	Total
Assets					
Cash and balances with the Central Bank	13,104,952	–	–	–	13,104,952
Loans and advances to banks	977,169	–	–	–	977,169
Loans and advances to customers	1,378,295	2,116,717	7,734,668	12,495,229	23,724,909
Derivative financial assets	–	–	–	6,611	6,611
Intangible assets	–	–	–	9,697	9,697
Property and equipment	–	–	–	935,698	935,698
Deferred income tax assets	–	–	–	154,598	154,598
Other assets	–	–	–	214,244	214,244
Total assets	**15,460,416**	**2,116,717**	**7,734,668**	**13,816,077**	**39,127,878**
Liabilities					
Deposits from banks	1,891,948	62,149	–	–	1,954,097
Due to customers	7,558,889	3,205,884	6,458,665	1,782,020	19,005,458
Other borrowed funds	146,389	0	1,857,921	12,180,691	14,185,001
Other liabilities	–	–	–	559,492	559,492
Retirement benefit obligations	–	–	–	26,081	26,081
Equity	–	–	–	3,397,749	3,397,749
Total liabilities	**9,597,226**	**3,268,033**	**8,316,586**	**17,946,033**	**39,127,878**
Net liquidity gap	**5,863,190**	**(1,151,316)**	**(581,918)**	**(4,129,956)**	**–**
As of 31 December 2005					
Total assets	8,282,619	1,661,466	5,779,730	7,684,244	23,408,059
Total liabilities	5,779,420	2,332,331	6,922,189	8,374,119	23,408,059
Net liquidity gap	**2,503,199**	**(670,865)**	**(1,142,459)**	**(689,875)**	**–**

The maturities of assets and liabilities and the ability to replace, at an acceptable cost, interest-bearing liabilities as they mature, are important factors in assessing the liquidity of the Group and its exposure to changes in interest rates and exchange rates.
Liquidity requirements to support calls under guarantees and standby letters of credit are considerably less than the amount of the commitment because the Group does not generally expect the third party to draw funds under the agreement. The total outstanding contractual amount of commitments to extend credit does not necessarily represent future cash requirements, since many of these commitments will expire or terminate without being funded.

D. Fair values of financial assets and liabilities

The following table summarizes the carrying amounts and fair values of those financial assets and liabilities not presented on the Group's balance sheet at their fair value. Bid prices are used to estimate fair values of assets, whereas offer prices are applied for liabilities.

	Carrying value		Fair value	
	2006	2005	2006	2005
Financial liabilities				
Loans and advances to customers	23,724,909	15,532,733	23,660,539	15,431,347
Loans and advances to banks	977,169	388,638	977,169	388,638
Financial liabilities				
Deposits and loans from banks	1,954,097	1,568,696	1,954,097	1,568,696
Due to customers	19,005,458	12,981,844	19,010,026	13,004,776
Other borrowed funds	14,185,001	6,505,172	14,185,001	5,146,182

Fair value is the amount at which a financial instrument could be exchanged in a current transaction between willing parties, other than in a forced sale or liquidation, and is best evidenced by a quoted market price. The estimated fair values of financial instruments have been determined by the Group using available market information, where it exists, and appropriate valuation methodologies. However, judgment is necessarily required to interpret market data to determine the estimated fair value.

Loans and advances to banks
The fair value of placements with and loans to other banks approximately equals the carrying amount since they all have less than a six-month maturity and therefore no calculation is needed.

Loans and advances to customers
The fair value of loans and advances to customers is their expected cash flow discounted at current market rates. Current market rates are the interest rates that would be charged as of year end 2006. Loans and advances to customers are stated net of provisions for impairment.

Deposits and loans from banks
The fair value of liabilities to banks approximately equals the carrying amount since they all have less than a six-month maturity and therefore no calculation is needed.

Due to customers
The estimated fair value of deposits with no stated maturity, which includes non-interest-bearing deposits, is the amount repayable on demand.
The estimated fair value of term deposits is calculated by discounting the cash flows at agreed dates with today's rates on deposit that have more than a six-month maturity and where the actual interest rate is not the same as the agreed rate for these deposits. Since the volume of deposits for which this is the case is very small, Management believes that the difference between the fair value and the carrying amount is immaterial.

Other borrowed funds
The fair value of liabilities to international financial institutions shows that the Group, based on its current position in the market, its strong shareholders and the results it has achieved, was able to obtain very good terms and conditions on the long-term loans it has contracted. Their fair value is smaller than their carrying amount, discounted by the interest rate that ProCredit Holding would charge.

5. Net interest income

	2006	2005
Interest income		
Cash and balances with the Central Bank	25,795	64,595
Reverse repo placements	59,200	8,437
Loans and advances to banks	111,656	11,646
Loans and advances to customers	3,827,708	2,317,027
	4,024,359	**2,401,705**
Interest expenses		
Deposits from banks	272,679	36,669
Due to customers	698,968	337,436
Other borrowed funds	544,977	222,877
	1,516,624	**596,982**
Net interest income	**2,507,735**	**1,804,723**

Interest income accrued on impaired financial assets is RSD 275 thousand (2005: 132 thousand).

6. Net fee and commission income

	2006	2005
Fee and commission income		
Payment transfer business	243,196	183,166
Guarantee business	41,311	19,404
Other fees	77,290	29,318
	361,797	**231,888**
Fee and commission expense		
Payment transfer business	42,320	29,954
Loan administration and guarantee business	0	15
Other fees	14,934	3,711
	57,254	**33,680**
Net fee and commission income	**304,543**	**198,208**

Other fee income includes fees on traveller's cheques in the amount of RSD 770 thousand (2005: RSD 507 thousand), other fees from customers in the amount of RSD 18,151 thousand (2005: RSD 19,402 thousand) and fees from card business in the amount of RSD 58,369 thousand (2005: RSD 9,409 thousand).

7. Net trading income

	2006	2005
Translation (losses)/gains	(201,436)	123,215
Transaction gains	181,593	120,149
Interest rate swaps	(6,487)	–
Foreign exchange swaps	(117)	(137)
Total net trading income	**(26,447)**	**243,227**

8. Other operating income

	2006	2005
Net gains from disposals of property and equipment	884	23,626
Gains and losses from securities	–	285
Other	23,181	36,350
	24,065	**60,261**

The position 'other' includes income from reimbursed costs for bills of exchange in the amount of RSD 12,642 thousand (2005: RSD 9,380 thousand), income from reimbursed costs for e-banking in the amount of RSD 4,662 thousand (2005: RSD 588 thousand), and income from reimbursed costs incurred for other group banks in the amount of RSD 3,077 thousand (2005: RSD 9,572 thousand). It also includes income from other reimbursed costs.

9. Impairment charge for credit losses

	2006	2005
Charge for the year on loans to customers (note 14)	478,351	265,808
Release of provision on loans to customers (note 14)	(292,327)	(57,991)
Provisions for commitments	36,636	22,985
Total impairment provision	**222,660**	**230,802**

10. Other operating expenses

	2006	2005
Staff costs		
Wages and salaries	979,203	664,527
State pension contributions	103,807	69,380
Other social security costs	65,115	43,520
Other staff costs	99,244	22,364
Total staff costs	**1,247,369**	**799,791**
Office rent	286,607	206,192
Office supplies and other office utilities	111,864	70,185
Marketing and representation	161,902	153,643
Depreciation and amortization	165,422	118,502
Communication expenses	71,101	48,552
Legal and advisory expenses	64,793	49,664
Security	48,147	30,623
Other taxes	82,137	37,781
Insurance expenses	48,062	12,507
Transport expenses	35,577	24,111
Training expenses	29,663	5,424
Other service expenses	71,764	51,553
Expenses for royalties on software	23,410	10,307
Expenses for repairs and maintenance	12,876	7,718
Other administrative expenses	39,597	37,530
Total	**2,500,291**	**1,664,083**

Other staff costs include fringe benefits in the amount of RSD 51,704 thousand (2005; RSD 22,363 thousand), provisions for retirement benefit obligations in the amount of RSD 26,081 thousand (2005: RSD NIL) and other employee benefits in the amount of RSD 21,459 thousand (2005: RSD NIL).

11. Income tax expense

	2006	2005
Current income tax	–	–
Deferred income tax credit (Note 18)	95,261	16,181
Total income tax credit	**95,261**	**16,181**

The tax on the Group's profit before tax differs from the theoretical amount that would arise using the official rate as follows:

	2006	2005
Profit before tax	86,944	411,534
Tax calculated at a tax rate of 10% (2005: 10%)	8,694	41,153
Penalty interest	401	5
Fines and penalties	277	49
Accounting depreciation above tax depreciation	2,840	4,989
Other non-deductible expenses	11,002	16,204
Utilized tax credits	(23,214)	(62,400)
Unutilized tax credits	95,261	16,181
Current tax	**95,261**	**16,181**

According to Serbian tax law, the Group is entitled to use tax credits based on the amounts invested in property and equipment and the number of new employees hired, and to reduce the current income tax liability. Tax credits on new employees hired can be used by the Group only in the year when declared. Tax credit on new investments in property and equipment can be carried forward for a period of 10 years. In order to be eligible to use these investment tax credits, the Group should not dispose of the respective property and equipment items during a period of three years from the year when the tax credit was declared.

12. Cash and balances with the Central Bank

	2006	2005
Cash on hand	403,446	308,115
Mandatory reserve	10,022,373	5,948,018
Balances with the Central Bank other than mandatory reserve deposits	2,679,133	678,780
Total (Note 27)	**13,104,952**	**6,934,913**

Balances with the National Bank of Serbia other than mandatory reserves are repo placements and overnight placements with the NBS amounting to RSD 2,359,457 thousand (2005: 637,450 thousand). The NBS placements break down as follows:

- Reverse repo placements with maturity of 14 days - RSD 900,000 thousand (2005: RSD 637,450 thousand), interest rate 14%,
- Reverse repo placements with maturity of 63 days – RSD 1,459,230 thousand (2005: RSD NIL), interest rate 14–14.35%,
- Other balances (overnight placements with the National Bank of Serbia) amounted to RSD 319,903 thousand (2005: 41,330 thousand).

The National Bank of Serbia (NBS) regulations relating to the mandatory reserve were changed several times during 2006: the mandatory reserve requirements were raised and the base for calculating the reserve was enlarged. At the end of December the mandatory reserve in local currency was calculated by applying the rate of 15% (at the beginning of the year 18%) to the average daily amount of the Group's deposit base in local currency in the preceding month. At the end of December the mandatory reserve in foreign currency for borrowings from abroad with a maturity of more than two years and deposits in foreign currency were calculated by applying the rate of 40% to the average daily amount of the Bank's deposit base in foreign currency in the preceding month and applying the rate of 60% to the average daily amount of Bank' borrowings from abroad with a maturity of up to two years. Mandatory reserves on subordinated debt are calculated by applying the rate of 20% to the average daily liabilities for subordinated debt in the preceding month, and for leasing agreements by applying the rate of 20% to ProCredit Leasing's average daily borrowings from abroad in the preceding month. Mandatory reserves can be used by the Group in its day-to-day operations. However, the Group is required to maintain the minimum monthly average balance of mandatory reserves. As of 31 December 2006 and 2005, the Group was in compliance with the above mentioned mandatory reserve regulations.
The NBS pays interest at the rate of 2.5% on mandatory reserves in RSD and does not pay any interest on mandatory reserves in foreign currency.

13. Loans and advances to banks

	2006	2005
Nostro accounts (Note 27)	229,507	111,600
Nostro covered letters of credit and guarantees	86,656	–
Money market placements (Note 27)	661,006	277,038
Total loans and advances to banks	**977,169**	**388,638**

Nostro accounts represent the account balances with Commerzbank, American Express Bank, Dresdner Bank and ProCredit Bank Bulgaria.
Money market placements in the amount of RSD 661,006 thousand (2005: RSD 277,037 thousand) are overnight deposits with: Commerzbank in the amount of RSD 252,800 thousand, American Express Bank in the amount of RSD 47,879 thousand and Raiffeisen Bank in the amount of RSD 360,327 thousand.

14. Loans and advances to customers

	2006	2005
Corporate customers	14,341,522	7,307,502
Retail customers, small and medium-sized enterprises	9,170,633	7,958,757
Retail customers, private individuals	736,878	554,238
Other customers	465,290	465,033
Total loans and advances to customers	**24,714,323**	**16,285,530**
Unearned future finance income on finance leases	(254,079)	(194,524)
Deferred fee income	(270,736)	(195,661)
Allowance for impairment	(464,599)	(362,612)
Net loans to customers	**23,724,909**	**15,532,733**

Accrued interest amounts to RSD 197,455 thousand (2005: RSD 135,524 thousand).

Allowance for losses on loans and advances

Movements in allowance for losses on loans and advances are as follows:

	2006	2005
Balance at 1 January	**362,612**	**197,646**
Provision for loan impairment (note 9)	478,351	265,808
Loans written off	(57,440)	(52,389)
Release of loan impairment provision (note 9)	(292,327)	(57,991)
Exchange rate differences	(26,597)	9,538
Balance 31 December	**464,599**	**362,612**

Loans and advances to customers include finance lease receivables:

	2006	2005
Gross investment in finance leases:		
No later than 1 year	342,849	168,055
Later than 1 year and no later than 5 years	917,614	576,081
Later than 5 years	37,189	49,088
	1,297,652	**793,224**
Unearned future finance income on finance leases	**(254,079)**	**(194,524)**
Net investment in finance leases	**1,043,573**	**598,700**
No later than 1 year	242,311	102,077
Later than 1 year and no later than 5 years	766,233	451,815
Later than 5 years	35,029	44,808
	1,043,573	**598,700**

15. Derivative financial assets

Financial assets at fair value through profit or loss include currency swaps and interest rate swaps. Currency swaps are commitments to exchange one set of cash flows for another. The risk is monitored on an ongoing basis with reference to the current fair value, and the liquidity of the market. Interest rate swaps are used to exchange commitments with floating interest rates for commitments with fixed interest rates.
As of 31 December 2006 the Group had four foreign currency swap agreements with Commerzbank AG and one with American Express Bank LDN. The Group entered into foreign currency swap agreements in order to hedge its open currency position. (Note 4.B.1 Foreign exchange risk). The foreign currency swaps are economic hedges only and hedge accounting is not being applied.
As of 31 December 2006 the Group had fixed-for-floating interest rate swaps with Commerzbank AG in the amount of EUR 15.8 million. The Group entered into interest rate swap agreements in order to hedge its open gap between the repricing maturities of long-term borrowings linked to floating rates, and the repricing maturities of loans disbursed at floating interest rates (Note 4.B.2 Interest rate risk).

Financial assets and liabilities at fair value through profit or loss were as follows:

	Fair value			
	Assets		Liabilities	
	2006	2005	2006	2005
Foreign currency swaps	124	189	7	51
Interest rate swaps	6,487	–	–	–
Total	**6,611**	**189**	**7**	**51**

16. Intangible assets

Movements in intangible assets for the years 2005 and 2006 are stated in the table below:

	Software
Acquisition cost	
Balance, 1 January 2005	28,581
Additions	1,018
Disposals	(8,640)
Balance, 31 December 2005	**20,959**
Accumulated amortization	
Balance, 1 January 2005	9,774
Disposals	(608)
Charge for the year	3,987
Balance, 31 December 2005	**13,153**
Net book value, 31 December 2005	**7,806**
Acquisition cost	
Balance, 1 January 2006	21,407
Additions	6,287
Balance, 31 December 2006	**27,694**
Accumulated amortization	
Balance, 1 January 2006	13,424
Charge for the year	4,573
Balance, 31 December 2006	**17,997**
Net book value, 31 December 2006	**9,697**

17. Property and equipment

Movements in tangible assets for the years 2005 and 2006 are stated in the table below:

	Equipment	Leasehold improvements	Assets under construction and other fixed assets	Total fixed assets
Acquisition cost				
Balance, 1 January 2005	251,294	63,949	32,878	348,121
Additions	–	7,563	194,440	202,003
Transfers	146,576	–	(146,576)	–
Disposals	(37,711)	–	(41,742)	(79,453)
Balance, 31 December 2005	**360,159**	**71,512**	**39,000**	**470,671**
Accumulated depreciation				
Balance, 1 January 2005	50,470	1,707	12,063	64,240
Disposals	(10,887)	–	(27,059)	(37,946)
Charge for the year	84,807	–	29,708	114,515
Balance, 31 December 2005	**124,390**	**1,707**	**14,712**	**140,809**
Net book value, 31 December 2005	**235,769**	**69,805**	**24,288**	**329,862**
Acquisition cost				
Balance, 1 January 2006	360,159	71,512	39,000	470,671
Additions	44,649	14,812	710,054	769,515
Transfers	281,816	97,484	(379,300)	–
Disposals	(11,306)	–	(635)	(11,941)
Balance, 31 December 2006	**675,318**	**183,808**	**369,119**	**1,228,245**
Accumulated depreciation				
Balance, 1 January 2006	124,390	1,707	14,712	140,809
Disposals	(8,522)	–	(589)	(9,111)
Charge for the year	114,913	28,091	17,845	160,849
Balance, 31 December 2006	**230,781**	**29,798**	**31,968**	**292,547**
Net book value, 31 December 2006	**444,537**	**154,010**	**337,151**	**935,698**

As of 31 December 2006 the Group had RSD 269,751 thousand in assets under construction (2005: RSD 8,535 thousand) due to investment in a new head office building which is planned for completion in 2008.

18. Deferred income tax assets

Deferred income taxes are calculated on all temporary differences under the liability method using an effective tax rate of 10% (2005: 10%).

Deferred tax assets are attributable to the following items:

	2006	2005
Tax loss carried forward (expiring in the period from 1 to 5 years)	12,412	15,495
Tax credit carried forward (expiring in the period from 1 to 5 years)	2,296	2,296
Tax credit carried forward (expiring in the period over 5 years)	139,890	41,545
As of 31 December	**154,598**	**59,336**

Movements in the deferred income tax account are as follows:

	2006	2005
As of 1 January	59,336	43,155
Income statement credit (Note 11)	95,262	16,181
As of 31 December	**154,598**	**59,336**

Deferred income tax assets are recognized for tax losses carried forward and investment tax credits only to the extent that realization of the related tax benefit is probable.

19. Other assets

	2006	2005
Advances paid	9,816	15,196
Other assets and receivables	115,245	60,540
Other prepayments and deferred expenditure	89,183	78,846
	214,244	**154,582**

Other prepayments and deferred expenditure consist of the following expenses:

- Interest expenses paid in advance to the clients using Pro-Advance deposit products in the amount of RSD 28,298 thousand (2005: RSD 29,018 thousand).
- Expenses paid in advance that are related to rent, insurance, marketing and magazine subscriptions in the amount of RSD 55,024 thousand (2005: RSD 49,828 thousand).
- Other claims to ProCredit Holding represent the invoiced cost of advertising in the name of ProCredit Holding in the amount of RSD 5,861 thousand (2005:RSD NIL).

20. Deposits from banks

	2006	2005
Money market deposits	1,835,564	1,226,301
Other banks' deposits	118,533	–
Short-term liabilities to banks belonging to the ProCredit group	–	342,395
	1,954,097	**1,568,696**

Money market deposits include:

	EUR	RSD '000	Interest rate	Due date
Erste Bank a.d. Novi Sad	1,000,000	79,000	10.10%	12 Jan. 2007
Raiffeisen Bank a.d. Beograd	4,000,000	316,000	10.00%	29 Jan. 2007
Hypo alpe adria bank a.d. Beograd	4,000,000	316,000	9.85%	17 Jan. 2007
Erste Bank a.d. Novi Sad	1,000,000	79,000	10.10%	5 Jan. 2007
Hypo alpe adria bank a.d. Beograd	1,000,000	79,000	9.80%	15 Jan. 2007
Societe Generale Bank	1,000,000	79,000	10.00%	15 Jan. 2007
Poljoprivredna banka Agro banka a.d. Beograd	4,000,000	316,000	5.20%	3 Jan. 2007
Cacanska banka	500,000	39,500	5.25%	3 Jan. 2007
Raiffeisen Bank a.d. Beograd	4,500,000	355,500	10.00%	12 Jan. 2007
Raiffeisen Bank a.d. Beograd	1,000,000	79,000	10.00%	29 Jan. 2007
Agroindustrijska komercijalna banka AIK banka a.d. Nis	1,200,000	94,800	5.30%	3 Jan. 2007
		1,832,800		
Accrued interest		2,764		
Total		**1,835,564**		

Position 'Other banks' deposits' includes term deposits from banks in the process of bankruptcy: MB Privredno kreditna banka AD – RSD 62,149 thousand; Credibel Banka – RSD 20,000 thousand and Union banka – RSD 36,384 thousand.

21. Due to customers

	2006	2005
Large corporate customers:		
– Current/settlement accounts	1,472,922	913,748
– Term deposits	823,571	450,030
SMEs:		
– Current/settlement accounts	1,912,323	923,815
– Term deposits	2,118,332	1,365,158
Retail customers:		
– Current/demand accounts	3,063,279	2,242,478
– Term deposits	9,197,899	6,831,739
Other liabilities	195,869	120,402
	18,784,195	12,847,370
Accrued interest on deposits	221,263	132,575
Total deposits	**19,005,458**	**12,979,945**

22. Other borrowed funds

Other borrowed funds include long-term borrowed funds from international financial institutions. The table below summarizes other borrowed funds as of 31 December 2006:

	Initial loan in EUR	Carrying value in EUR 2006	Maturity	RSD '000 2006	RSD '000 2005
European Bank for Reconstruction and Development (EBRD), London	27,229,011	20,557,253	2001-2009	1,624,023	2,194,935
Kreditanstalt fuer Wiederaufbau (KfW), Frankfurt am Main	3,000,000	750,000	2003-2007	59,250	1,216,104
Commerzbank AG, Frankfurt am Main	2,500,000	2,500,000	2002-2007	197,500	213,750
International Finance Corporation, Washington DC	11,016,398	4,493,589	2002-2008	354,994	619,678
Instituto de Credito Oficial, San Salvador	15,000,000	15,000,000	2005-2015	1,185,000	1,282,500
Financierings-Maatschappij voor Ontwikkelingslanden (FMO), The Hague	63,000,000	63,000,000	2006-2013	4,977,000	256,500
ProCredit Holding AG, Frankfurt am Main	14,750,000	14,750,000		1,165,250	684,000
ProCredit Holding subordinated debt	12,000,000	12,000,000	2006-2016	948,000	–
European Fund for Southeast Europe (EFSE), Frankfurt am Main	52,800,000	46,054,762	2005-2011	3,638,326	–
	–	**179,105,604**	–	**14,149,343**	**6,467,467**
Accrued interest				137,293	39,604
Deferred fees				(101,635)	
Total				**14,185,001**	**6,507,071**

The European Fund for Southeast Europe was founded in 2006. Kreditanstalt fuer Wiederaufbau (KfW), as one of shareholders, transferred its rights and obligations for 10 individual loan agreements between KfW and ProCredit Bank to the newly established fund in the amount of EUR 11,973,442.

In 2006 ProCredit Holding loaned ProCredit Bank EUR 12 million of subordinated debt in 2 instalments. Subordinated debt describes debt that is unsecured or has a lesser priority than that of an additional debt claim on the same asset. It has a maturity of 10 years and according to its nature and capital characteristics it can be transferred to equity.

The Group is obliged to comply with a number of debt covenants set in the borrowing contracts, such as risk weighted capital adequacy, single client exposure ratio, aggregate large exposure ratio, group exposure ratio, related party exposure ratio, maturity gap to available capital ratio, open credit exposure ratio, liquid assets to total assets ratio, and unhedged open foreign currency position in any currency and in aggregate.

One of the most significant debt covenants is the risk weighted capital adequacy ratio, which as at 31 December 2006 was as follows:

in %	Required (higher than)	Actual
European Bank for Reconstruction and Development	10	15.58
International Finance Corporation	10	15.58
FMO (loan to ProCredit Bank)	12	15.53
FMO (loan to ProCredit Leasing)	10	15.94

The methodology used for calculating the risk weighted capital adequacy ratio varies according to the specific requirements of the loan agreements.
During the reporting period the Group was not in breach of debt covenants with respect to its borrowed funds.

23. Other liabilities

	2006	2005
Liabilities to employees	11,028	2,663
Taxes, contributions and other charges	25,216	23,156
Liabilities to suppliers	63,089	37,442
Received coverage based on unrealized international payments	248,189	155,328
Impairment of credit commitments	62,742	26,106
Liabilities for dividends	79,000	–
Derivative financial liabilities	7	51
Other	70,221	5,726
	559,492	**250,472**

The position 'other' includes: Provisions for unused vacation – RSD 21,124 thousand (2005: NIL), liabilities for agreed foreign currency deals – RSD 23,470 thousand (2005: NIL), other due payments – RSD 4,145 thousand (2005: RSD 2,955 thousand), other liabilities to group companies – RSD 7,576 thousand (2005: NIL), and other deferred liabilities – RSD 13,906 thousand (2005: RSD 2,771 thousand).

24. Retirement benefit obligations

Retirement benefit obligations are paid after regular retirement of employee. The employee's right to receive this benefit is conditional on his or her remaining in the employ of the Group until becoming entitled to take retirement. The expected volume of funds needed to cover the costs of such benefits is accumulated during the period of the employee's working life. The amount of the retirement benefit obligation is estimated yearly by an independent certified actuary by applying the projected credit sample. The net present value of this liability is determined by discounting future net cash outflows, applying the interest rate on long-term bonds which have the same currency and approximately the same maturity as the retirement benefit obligations.
Retirement benefit obligations which mature more than 12 months after the balance sheet date are discounted to net present value.

	2006	2005
Retirement benefit obligation	26,081	–
	26,081	**–**

25. Share capital

Based on the public bid to acquire 400,000 to 800,000 shares of ProCredit Bank a.d. Beograd, issued by ProCredit Holding on 13 August 2005, ProCredit Holding acquired 800,000 shares from IFC and FMO.
Based on a Decision of the Shareholders' Meeting dated 5 July 2005, the Bank distributed its fourth issue of ordinary shares for the purpose of increasing its capital (number of shares: 800,400 with a nominal value of CSD 240,120 thousand). The shares were subscribed and paid for at a price which is higher than their nominal value and thus the total amount of equity paid by the shareholders was CSD 338,969 thousand. The equity increase was registered with the Agency for Legal Entities Belgrade under registration number BD. 93435/2005 as of 31 October 2005.
Based on a Decision of the Shareholders' Meeting dated 20 April 2005 the Bank distributed shares for the purpose of their redenomination. The nominal value of each share was changed from CSD 300.00 to CSD 1,000.00, and this change was registered in the Central Registry on 29 November 2005. Subsequently, the total number of shares was 1,320,120.
Based on a Decision of the Shareholders' Meeting dated 6 July 2006 the Group distributed the fifth issue of ordinary shares for the purpose of increasing its capital (number of shares: 600,000 with a nominal value of RSD 600,000 thousand). The shares were subscribed and paid for at a price which is higher than their nominal value and thus the total amount of equity paid by the shareholders was RSD 634,463 thousand. The equity increase was registered with the Agency for Legal Entities Belgrade under registration number BD 185971 / 2006 as of 15 November 2006. The shareholder structure remained unchanged following the equity increase.
Based on a public bid to acquire shares in ProCredit Bank a.d. Beograd, issued by ProCredit Holding on 6 December 2006, in accordance with the decision of the Security and Exchange Commission No. 4/0-32-4222/6-06, ProCredit Holding acquired 81,810 shares from KfW.

The ownership structure of the Group as at 31 December 2006 was as follows:

	Number of shares		Share in %	
	2006	**2005**	**2006**	**2005**
ProCredit Holding AG	1,100,080	700,080	57.29	53.03
European Bank for Reconstruction and Development (EBRD)	320,020	220,020	16.67	16.67
Commerzbank AG	320,020	220,020	16.67	16.67
Kreditanstalt fuer Wiederaufbau (KfW)	180,000	180,000	9.37	13.63
	1,920,120	**1,320,120**	**100.00**	**100.00**

As of 31 December 2006 the Group had no plans to issue new shares in 2007.

26. Retained earnings

According to the Central Bank resolution on the classification of banks' balance sheet assets and off-balance sheet items, starting from 30 June 2006, the Group has been obliged to allocate from retained earnings to a special account reserve in equity the difference between the amounts of allowances for loans and advances to banks and to customers, calculated based on the Group's internal rules and Central Bank provisioning regulations, respectively.
As at 31 December 2006, the amount of special banking risk provisions amounted to RSD 313,871 (31 December 2005: NIL). This amount will be allocated from retained earnings to the special banking reserves account within equity, subject to approval by the Bank's shareholders, and will not be distributable to shareholders.

27. Cash and cash equivalents

Cash and cash equivalents	**2006**	**2005**
Cash and balances with the Central Bank (Note 12)	13,104,952	6,934,913
Nostro accounts with other banks (Note 13)	229,507	111,600
Money market placements (Note 13)	661,006	277,038
	13,995,465	**7,323,551**

28. Contingent liabilities and commitments

The following table indicates the contractual amounts of the Group's off-balance sheet financial instruments that commit it to extend credit to customers:

	2006	**2005**
Payments and guarantees	1,710,549	1,096,151
Performance guarantees	390,694	241,236
Acceptances and endorsements	16,322	22,357
Loan commitments	1,380,011	378,705
Letters of credit (documentary business)	577,192	203,192
Balance as at 31 December	**4,074,768**	**1,941,641**

As of 31 December 2006 the Group does not have any capital or operating lease commitments.

29. Related party transactions

The Group is controlled by ProCredit Holding AG (incorporated in Germany), which owns 57.29% of the ordinary shares. The remaining 42.71% of the shares are held by the European Bank for Reconstruction and Development (EBRD), Commerzbank AG and Kreditanstalt fuer Wiederaufbau (KfW). ProCredit Bank Albania and ProCredit Bank Bulgaria are subsidiaries of ProCredit Holding.
In the normal course of business, the Group enters into transactions with its shareholders and other microfinance institutions in Central and Eastern Europe.

	2006	2005
Nostro accounts		
Commerzbank AG	73,364	47,019
ProCredit Bank Bulgaria	11,424	6,069
Deposits from banks		
ProCredit Bank Albania	–	85,866
ProCredit Bank Bulgaria	–	256,529
Other borrowed funds		
ProCredit Holding	2,113,250	684,000
Commerzbank AG	197,500	213,750
Other receivables PCH	5,861	–
Liabilities for dividends PCH	53,416	–
Liabilities for dividends Commerzbank AG	25,584	–
Accrued interest payable PCH	26,526	1,900

The volumes of related party transactions and related expenses for the year are as follows:

	2006	2005
Deposits from banks		
Loans outstanding at 1 January	342,395	315,540
Loans issued during year	2,536,448	572,042
Loan repayments during the year	(2,878,843)	(545,187)
Loans outstanding at 31 December	**–**	**342,395**
Other borrowed funds		
Loans outstanding at 1 January	897,750	197,213
Loans issued during year	1,454,412	684,000
Exchange rate differences	(40,630)	16,537
Loan repayments during the year	–	–
Loans outstanding at 31 December	**2,311,532**	**897,750**
Interest expenses	**127,222**	**13,474**

The policy of the Group is to reimburse the Members of the Board of Directors for their travel expenses incurred in connection with Board Meetings. No salaries or any other contributions are paid in connection with membership of this body.
In 2006 the Group offered short-term employee benefits in the gross amount of RSD 5,425 thousand to key management staff (2005: NIL) who are members of the Executive Board of the Bank, and post-employment benefits in the amount of RSD 971 thousand (2005: NIL), representing the Bank's contribution to the State Pension plan and other social contributions. In addition during 2006 the Group paid to key management staff the amount of RSD 22,120 thousand (2005: RSD 28,728 thousand) representing management fees.

As of 31 December 2006 Executive Board members did not have any loans or loan commitments except commitments for credit and debit cards in the amount of RSD 70 thousand (2005: NIL).

30. Events after balance sheet date

During the period up to and including 20 April 2007, no post-balance sheet events occurred which have any substantial impact on the consolidated financial statements for the year ending 31 December 2006.

31. Exchange Rates

The official exchange rates as of 31 December 2006 and 2005 were as follows:

	2006	2005
USD	59.9757	72.2189
EUR	79.0000	85.5000

Contact Addresses

Head Office

Belgrade
Bulevar despota Stefana 68c
Tel. +381 11 2077 906
Fax +381 11 2077 905
info@procreditbank.co.yu

Belgrade Branches

Belgrade Branch I
Gospodar Jevremova 9
Tel. +381 11 3025 625
Fax +381 11 3025 620

Belgrade Branch II
Vojvode Milenka 38
Tel. +381 11 3617 533
Fax +381 11 3613 399

Belgrade Branch III
Bulevar kralja Aleksandra 240
Tel. +381 11 2422 218
Fax +381 11 3809 272

Belgrade Branch IV (main branch)
Bulevar despota Stefana 68c
Tel. +381 11 2077 888
Fax +381 11 2077 861

Belgrade Branch V
Novi Beograd, Goce Delčeva 29
Tel. +381 11 3194 400
Fax +381 11 3194 400

Belgrade Branch VII
Obilićev venac 26
Tel. +381 11 2635 303
Fax +381 11 328 3624

Belgrade Branch VIII
Bulevar vojvode Mišića 12
Tel. +381 11 2067 592
Fax +381 11 2067 592

Belgrade Branch IX
Novi Beograd, Bulevar AVNOJ-a 65
Tel. +381 11 2120 210
Fax +381 11 2120 214

Belgrade Branch X
Zemun, Glavna 47
Tel. +381 11 3168 655
Fax +381 11 3168 656

Belgrade Branch XI
Novi Beograd, Milutina Milankovića 9
Tel. +381 11 3012 750
Fax +381 11 3012 751

Belgrade Branch XII
Mileševska 65
Tel. +381 11 3089 443
Fax +381 11 3089 405

Belgrade Branch XIII
Banovo brdo, Požeška 60
Tel. +381 11 3057 030
Fax +381 11 3057 034

Regional Branches

Bačka Palanka
Kralja Petra I 21
Tel: +381 21 754 902
Fax +381 21 754 904

Bečej
Moše Pijade 3
Tel. +381 21 691 3220
Fax +381 6913 220

Čačak
Sinđelićeva 35
Tel. +381 32 226 556
Fax +381 32 228 336

Inđija
Kralja Petra I 13
Tel. +381 22 510 911
Fax +381 22 510 912

Jagodina
Gine Pajević bb
Tel. +381 35 244 695
Fax +381 35 244 698

Kikinda
Trg srpskih dobrovoljaca 2
Tel. +381 230 401 110
Fax +381 230 401 110

Kragujevac Branch I
Kralja Petra I 3
Tel. +381 34 302 175
Fax +381 34 302 175

Kragujevac Branch II
Kneza Mihaila 49
Tel. +381 34 308 888
Fax +381 34 308 818

Kraljevo
Cara Lazara 44
Tel. +381 36 317 290
Fax +381 36 317 290

Kruševac
Mirka Tomića 99
Tel. +381 37 418 480
Fax +381 37 418 490

Leskovac
Bulevar oslobođenja bb
Tel. +381 16 212 392
Fax +381 16 212 397

Loznica
Vere Blagojević F/9
Tel. +381 15 877 113
Fax +381 15 877 105

Niš Branch I
Svetozara Markovića 10
Tel. +381 18 257 845
Fax +381 18 505 380

Niš Branch II
Dušanova 21
Tel. +381 18 514 345
Fax +381 18 514 344

Niš Branch III
Vizantijski bulevar 84
Tel. +381 18 206 816
Fax +381 18 206 817

Novi Pazar Branch I
Stefana Nemanje 54
Tel. +381 20 316 584
Fax +381 20 316 591

Novi Pazar Branch II
28. novembra 93
Tel. +381 20 318 221
Fax +381 20 318 221

Novi Sad Branch I
Narodnog Fronta 73a
Tel. +381 21 4895 700
Fax +381 21 4895 727

Novi Sad Branch II
Bulevar cara Lazara 7b
Tel. +381 21 455 711
Fax +381 21 458 122

Novi Sad Branch III
Jovana Dučića 7
Tel. +381 21 6791 751
Fax +381 21 6791 010

Novi Sad Branch IV
Laze Telečkog 28
Tel. +381 21 4726 426
Fax +381 21 4726 430

Obrenovac
Miloša Obrenovića 105
Tel. +381 11 8725 835
Fax +381 11 8725 833

Pančevo
Petra Drapšina 4-6
Tel. +381 13 331 491
Fax +381 13 331 492

Pirot
Srpskih vladara 48
Tel. +381 10 313 033
Fax +381 10 313 036

Požarevac
Tabačka čaršija 12
Tel. +381 12 543 150
Fax +381 12 543 156

Prijepolje
Valterova bb
Tel. +381 33 716 040
Fax +381 33 716 050

Smederevo
Vojvode Đuše 7
Tel. +381 26 640 160
Fax +381 26 640 121

Sombor
Venac Radomira Putnika 24
Tel. +381 25 26 480
Fax +381 25 26 484

Sremska Mitrovica
Svetog Dimitrija 35
Tel. +381 22 615 022
Fax +381 22 636 215

Stara Pazova
Kralja Petra 22
Tel. +381 22 316 613
Fax +381 22 316 612

Subotica Branch I
Cara Dušana 3
Tel. +381 24 622 501
Fax +381 24 622 505

Subotica Branch II
Pazinska 3
Tel. +381 24 670 075
Fax +381 24 673 705

Šabac
Cara Dušana 1
Tel. +381 15 360 050
Fax +381 15 360 022

Užice
Dositejeva 4
Tel. +381 31 510 135
Fax +381 31 513 457

Valjevo
Doktora Pantića 118
Tel. +381 14 244 723
Fax +381 14 244 725

Vranje
Lenjinova 20
Tel. +381 17 414 332
Fax +381 17 414 668

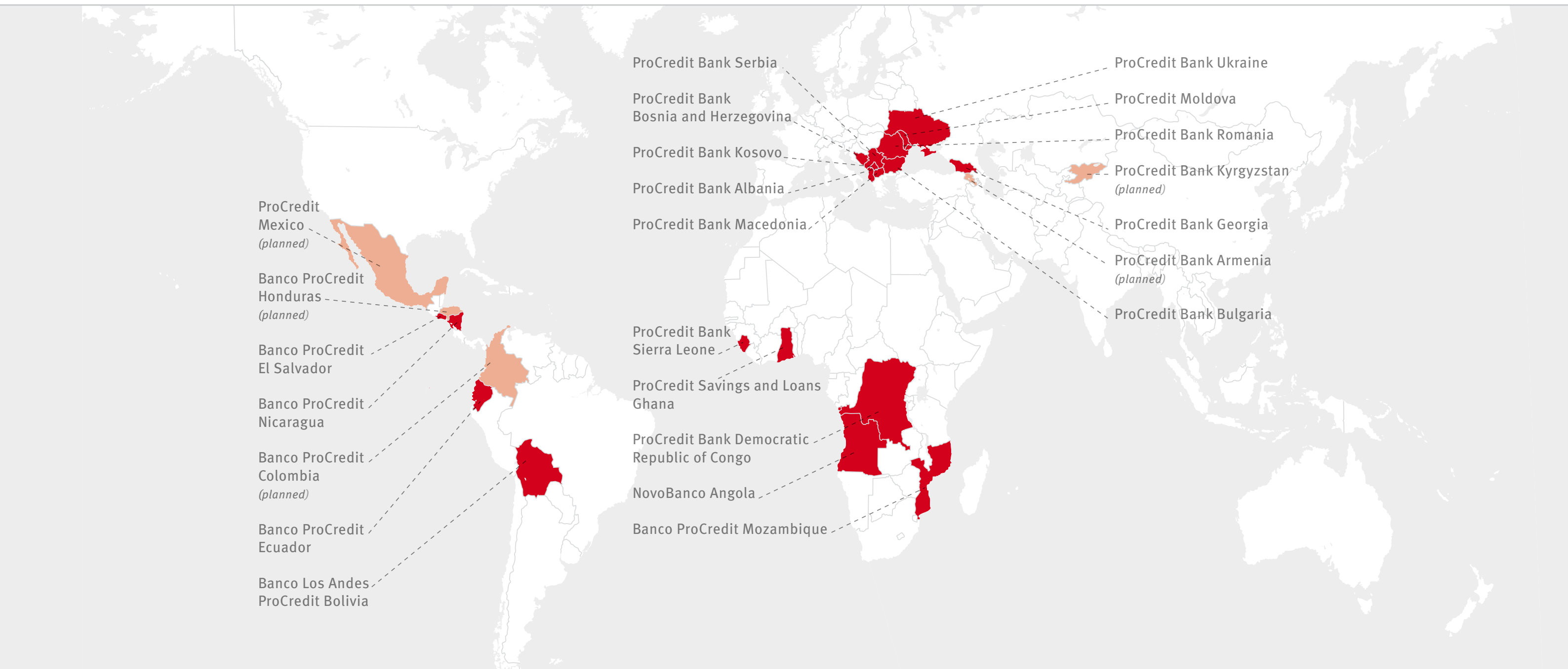
Vršac Branch I
Trg Save Kovačevića 3
Tel. +381 13 801 350
Fax +381 13 801 360

Vršac Branch II
Ive Milutinovića 46
Tel. +381 13 801 380
Fax +381 13 801 381

Zaječar
Nikole Pašića 87
Tel. +381 19 444 850
Fax +381 19 444 878

Zrenjanin
Kralja Aleksandra 10
Tel. +381 23 511 780
Fax +381 23 511 780

ProCredit Leasing
Novi Beograd
Milutina Milankovića 9
Tel. +381 11 3012 700
Fax +381 11 3012 713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