Banca Tercas – Cassa di Risparmio della Provincia di Teramo s.p.a.

2005 ANNUAL REPORT

Board of Directors' Report
on the management trend

(abstract)

THE ECONOMIC BACKGROUND

The International Picture

During the year 2005, the worldwide economy continued to expand in a significant way. This was, above all, due to the growth which took place in the United States, Japan and China. The estimates of the International Monetary Fund indicate an increase of about 4.3% in the worldwide GDP.
The continuing development at a worldwide level came about notwithstanding the increase of geopolitical tension and natural calamities which, nevertheless, did not curb the growth of international exchanges. Because of the vigour of global growth, there was considerable movement in the price of oil and raw materials. The crude oil prices drove up consumer prices in many countries. However, globally, inflationary tension remained contained.
The GDP increased by 3.5% in the United States. It was supported, in particular, by private consumption (more than 3%), by the investments of companies (+8%) and by public expenditure (+1.7%). The great increase in the prices of oil products only marginally influenced the trend of the real American economy which, on the whole, registered an increase in employment and a rise in the value of real estate. This increased the liquid assets of families and, as a result, consumption. Nonetheless, in parallel, the tendency to save, which has lost about five percentage points in the last ten years, decreased.
Japan confirmed the favourable dynamics emphasized last year. Productive activities increased by 2.7%. Family consumption increased (+3.5%) and this was sustained by two fundamental factors: the tendency of the labour market and the perceiving that the end of the deflation phase was giving way to the dynamics of slightly positive prices. Exportation again began to expand and there was an improvement in the climate of confidence felt by companies and the propensity for investments. The industrial sector showed an annual performance of +5%.
The main Asian economies continued expanding at elevated rates during the course of the year. China, in particular, persists in its elevated growth rate (+9.9%), which is mainly correlated to the steady tendency of internal demand, export and investments.

The Euro Zone and Italy

The economic expansion of the Euro zone during 2005 was rather contained, even if during the last few months there was a certain improvement in the general economic picture with the GDP closing the year at +1.3%. The economic trend among the member countries was rather heterogeneous and it highlighted the delay in the Italian economic situation.
Internal demand and, in particular, family expenditure were the driving force of growth in France and Spain. On the contrary, with stagnant internal demand, the productive activity in Germany was driven by exchange with foreign countries.

The area’s reduced economic growth and inflation contained at around 2% favoured the ECB (European Central Bank) decision to leave the reference rate unchanged at 2% until December 1, 2005. This is when the first increase of 25 basis points was deliberated to precede the weak signs of the recovery of price increases. On March 2, 2006, the same rate was brought to 2.5%, in recognition of the fact that dear oil, the prices of energy products and the strengthening of the recovery of the European economy can put price stability at risk.

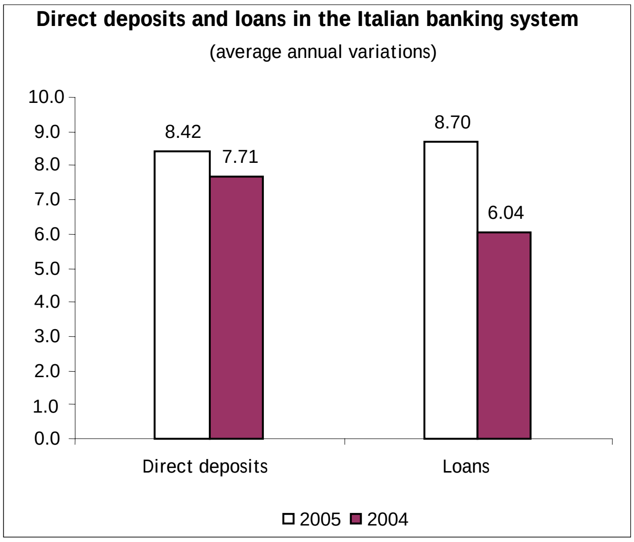
The Italian economy continues its long phase of stagnation. According to the Central Institute of Statistics, the rhythm of the recovery phase for the second quarter was reduced during the following period and slowed down greatly in the fourth quarter. The GDP did not increase and the deficit/GDP ratio was 4.1%.

There was a continuation in the decline in investments (-1.9% in the third quarter) and production (-1.8% yearly), which was, however, in connection with a slight recovery in family consumption (+1.4% yearly in the third quarter) and the rise in employment.

The unemployment rate continued to decrease and dropped to about 7.5%. On the contrary, in other large Euro zone countries (Germany and France) the unemployment rate remained practically stable at around 9%.

The main qualitative indicators have been signalling an improvement in the economic picture since the end of the year and throughout all of 2006. According to the International Monetary Fund estimates, the increase in the GDP in Italy should be 1.5% and in the Euro zone 1.8%.

The Italian Banking System



The survey carried out by ABI (The Italian Bank Association) indicates the tendency of a rather brilliant expansion of the assets administered by the Italian banking system for the year described. Direct bank deposits in Euros increased by 8.42%. This was in a more accelerated way than the previous year (+7.71%). The volume of bonds issued by the banks increased by 9.88% whereas customer deposits increased by 7.51%. There was also a net recovery for repurchase agreements. Loans grew by 8.7%, which was superior to 2004. This increase is the result, in particular, of a lively tendency of the medium and long-term ones, which have increased by 13%. The short-term element turned out to be less brilliant and was +2.8% compared to the previous year.

Financial market tendencies

International financial markets closed the year 2005 with positive performances. In the United States, *Standard & Poor’s 500* increased by 3% (+7.6% in 2004), *Nikkei 225* from the Tokyo stock exchange bounced to 40.2% (+8.9% in 2004) and in Europe the *Dow Jones Euro Stoxx* showed a variation of 22.5 %.

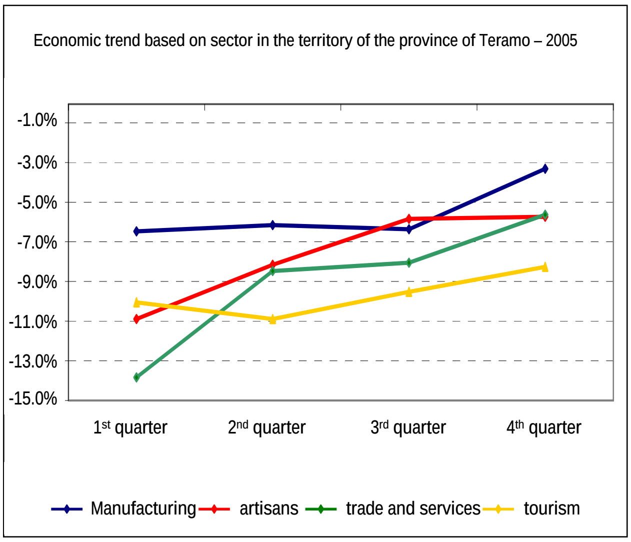
The Italian indexes showed a good rise: Mib30 index +14.6%, Mibtel index +14.4% (+18.1 in 2004), S&P/MIB index +16.4% (+14.9% in 2004). An all-time high was reached for the exchange of shares with an equivalent of 953 milliard euros and with the highest growth rate of share exchange in Europe for contracts and countervalue. It is first place as well for the growth rate of standard contracts for stock derivatives. The amount of dividends paid in the year 2005 was 26.2 milliard. This was superior to the already generous levels in 2004.

While the stock market experienced outstanding appreciation, the year 2005 turned out to be substantially negative for the bond market. In the European *bond* market, the uncertainty connected to the economic cycle led to a marked reduction in yield during the first part of the year.

The economic picture in the regions of Abruzzo, Marche and Molise

For the year 2005, the information regarding the region of Abruzzo indicates situations, which are not completely comforting, in a complex national and international background. There was only a slight growth in the economy in Abruzzo. The increase in the GDP tends to confirm itself at +0.3% compared to the preceding year and shows weak signs of recovery after the decrease of 0.8% registered in 2004.

There are substantial decreases in production in sectors which have a considerable impact on the territory. These are the textile, clothing, leather-shoe and wood-furniture sectors. There is a continuing crisis in the electronics and communications industry involving extensive areas of our territory (L'Aquila, Sulmona, Avezzano, the province of Pescara). The result is an increasing gap between the internal and coastal zones in the region. There was, on the other hand, a noteworthy contribution made by the medium and high technology sectors: pharmaceutical chemistry, rubber and plastic and the metal industry.



In 2005, there was a difference in tendency in the main manufacturing sectors in the province of Teramo. Production increased in the metal and food sectors. It, instead, decreased in the construction and chemistry sectors. There continue to be negative signs in the textile-clothing (-12.3%) and leather-shoe (-6.7%) sectors. There is a timid sign of recovery of operational margins, in an economic sense, in the trade and services sector. Retail trade, the tertiary sector and transport are the sectors which boast the greatest recovery, which is beginning to be found, at more moderate rates, even in tourism and in the wholesale business.

In the region of Marche, only in the final part of the year, did the economy show signs of recovery. The fourth quarter shows recovery in the manufacturing industry: there was an increase of 1.9% in production during the same period in 2004 and the tendency of sales in real terms increased by 3.6%. There were positive results in all the main sectors.

The improvement in productive and commercial activity was in part sustained by the dynamics of sales prices both internally and abroad while, apparently, the tendency of purchase costs does not seem to have influenced the conditions of offer.

THE APPLICATION OF THE INTERNATIONAL IAS IFRS ACCOUNTING PRINCIPLES TO THE INDIVIDUAL AND CONSOLIDATED BALANCE SHEETS OF TERCAS JOINT STOCK COMPANY

The increasing globalization of the economy and financial markets has been posing the problem of making the "accounting language" used to describe the extent of companies, uniform for some time. The intention was to standardize the countless information which economic operators give to their shareholders, bondholders and, in general, to all those who, for various reason, have economic relations with them.

It was desired in the main Western countries which, because of their nature, are characterized by increasing economic and social integration. This need was met by means of the European Commission's legislative acknowledgement of the International Accounting Standards, which are more commonly known by the abbreviation I.A.S.. The aim of the "new" principles is, in fact, to create a common and uniform language for the drawing up of balance sheets. This makes the company data as transparent as possible as well as comparable. This complex system of norms was acknowledged by the European Union with a series of measures , which are in the form of European community regulations. This was done after speaking with the I.A.S.B.. This is the organ, which has the task of compiling and updating the norms during the course of time. The aim is to make them as compatible as possible with the specific norms, which are already existent, in the single countries.

These regulations, which took effect as of July 19,2002 with n. 1606, were initially directed towards the largest companies. The drawing up of the information contained in the accounting documents, based on the IAS, was initially imposed only for the consolidated balance sheets of companies, which were quoted and on the rise. This was done so that the necessary cultural revolution for all the people responsible would be gradual. Moreover, regulation 1606 of the European Economic Community provided for a list of subjects to which the member states could attribute the option or obligation of the adoption of the new principles.

The European Community provisions have been integrated with a series of national dispositions. Among these, there is Law decree 38 dated February 28, 2005, which also addressed the regulations for the fiscal aspects arising from the application of the new evaluation criteria.

Law decree 38/05 regulated the options provided for by the introduction of the IAS. It extended the area of application for the new principles and identified four well defined categories to which they are applicable:

a) quoted companies different from insurance companies;
b) companies having financial instruments diffused among the public;
c) banks and financial brokers under supervision;
d) insurance companies.

Quoted companies and companies having financial instruments diffused among the public were obliged to draw up consolidated balance sheets based on IAS as of the year 2005. Only for individual balance sheets was there the option of choosing whether to avail oneself of the new dispositions. In fact, the legislator obliges these companies to the mandatory drawing up of the individual IAS balance sheet as of 2006. Banks and financial brokers under supervision have the same deadlines and obligations.

With reference to the balance sheets of the banks and companies under supervision, the legislator gave authority to the Central Bank of Italy on the subject of the planning of statements and supplementary notes. The Supervisory organ consequently published the final version of the IAS balance sheet layout and of the relevant instructions in December 2005. This provides for a reduced and simplified version for 2005 so as to favour its initial application.

Since, as parent bank, Tercas joint stock company is obliged to draw up its consolidated balance sheet based on IAS – IFRS, it has opted to apply IAS to its individual balance sheet as well. This option was chosen, taking into account the advantages in terms of the coherence and reliability of the data produced for the drawing up of the balance sheets (individual and consolidated), and the long term advantages deriving from a rapid changeover to the accounting language. In a company background marked by great dynamism, the advantages are considered to be greater than the disadvantages deriving from a greater work load on the single administrative departments as well as the uncertainties, with particular reference to norms, deriving from such a rapid changeover to the new system of regulations.

THE BANK'S SITUATION

The application of the IAS IFRS accounting principles and the contents of the management report

It should be pointed out that all the data relating to 2004, which is included in the Management Report statements and supplementary note, does not include the application of IAS 32 and 39 (financial instruments) to that year's balance sheet. The reason is that they must be applied as of January 1, 2005, since the bank did not avail itself of the option to adopt the principles in advance. Consequently, the comparison of data between the two years may, in some cases, not be completely homogeneous. This, however, should not relevantly modify the operational remarks being discussed here..

Intermediate Assets

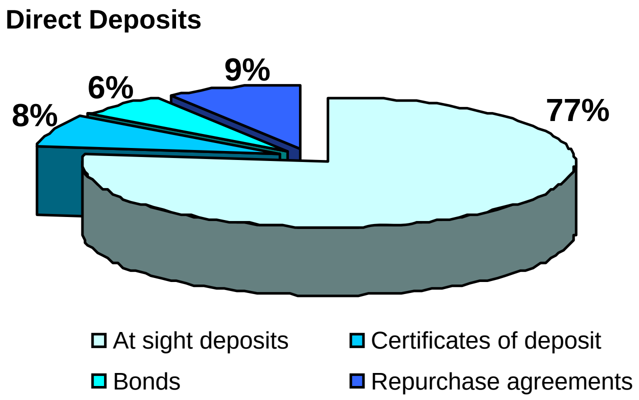
	Year	Year	Variations 04-05	
	2005	2004	Absolute	%
Direct customer deposits	2,135	1,889	246	13.0
Indirect customer deposits	1,738	1,636	102	6.2
Total customer deposits	3,873	3,525	348	9.9

At the end of the year the consistency of overall customer deposits reached 3,873 million euros, thus realizing a 9.9% increase. The accentuated dynamics of direct deposits (+13%) greatly influenced this data compared to the 6.2% increase of indirect deposits.

Direct deposits

During 2005, direct deposits grew significantly in comparison to 2004, with an increase of 13%.

	Year	Year	Variations 04-05	
	2005	2004	Absolute	%
Deposits, CDs and bonds	1,943	1,788	155	8.6
At sight deposits	*1,648*	*1,559*	*89*	*5.7*
Certificates of deposit	*168*	*200*	*(32)*	*(16.0)*
Bonds	*126*	*28*	*98*	*349.1*
Repurchase agreements	192	101	91	91.1
Direct deposits	**2,135**	**1,889**	**246**	**13.0**



The highest percentage increases were in the bond department (+349.1%) and in the repurchase agreement department (+91.1). With regards to this, it should be pointed out that, among the repurchase agreements, there is a sum of over 100 million euros deriving from relations with a non-banking financial institution. In accordance with supervisory norms, this is considered ordinary clientele. Certificates of deposit declined (-16%) as a result of commercial action carried out so as to favour the growth of the bond department. In fact, during the course of last year, a total of about 100 million euros worth of debenture loans were issued. This brought the quota of deposits with expirations (certificates of deposit and bonds) to 13.8%.

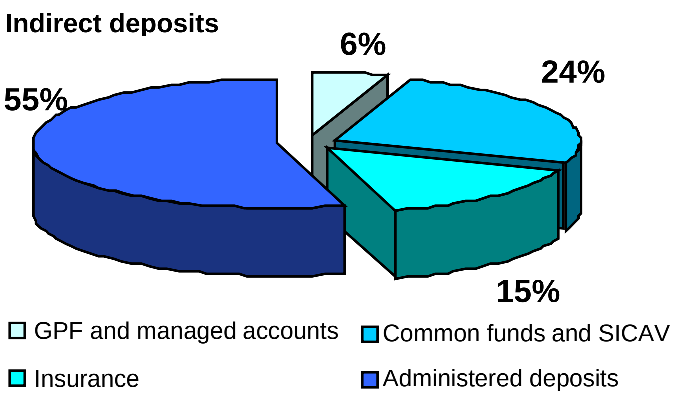
The good result in the at sight deposits (+9%) confirms the capacity of the bank to build customer loyalty notwithstanding a very competitive market.

Indirect deposits

	Year	Year	Variations 04-05	
	2005	**2004**	**Absolute**	**%**
Managed deposits	791	694	97	10.8
GPF (Financial portfolio management) and Managed accounts	*108*	*97*	*(11)*	*11.3*
Common funds and SICAV	*425*	*400*	*47*	*11.8*
Insurance	*258*	*197*	*61*	*31.0*
Administered deposits	947	942	5	0.5
Indirect deposits	**1,738**	**1,636**	**102**	**6.2**

Indirect deposits showed an increase of 6.2%. confirming themselves at a quota of 1,738 million euros. This was the result of the good trend of the managed accounts (+14%). Administered deposits, instead, were substantially stable and were maintained at 2004 levels (947 million euros).

The placing of GPF (Financial Portfolio Management) TERCAS products, which was begun in the last quarter of the year, had considerable success. At the end of the year they amounted to 22 million euros.



The Sicav Tercas also met with customer approval. They increased by 46%, confirming the funds managed at 76 million.

At the end of the year, the insurance component showed a stock of premium deposits equal to 258 million. This was an increase of 60 million euros (+31%) compared with the end of the previous year.

	Year	Year	Variations 04-05	
	2005	**2004**	**Assoluta**	**%**
Current accounts and financing	575	476	99	20.9
Loans – personal loans	993	732	261	35.7
Debit Items	34	14	20	146.8
Deteriorated Assets	40	56	(16)	(27.9)
Other loans	115	93	21	23.0
Total Customer loans	**1,757**	**1,371**	**386**	**28.2**

At the end of 2005, lending aggregates reached 1,757 million euros, with an increase of 28.2% as compared to the past year. The greatest performance was again for medium and long-term loans. This was due both to the effects of commercial initiatives aimed at acquiring long term relations and to the persisting of the positive trend of the real estate market.

Among customer loans, there are capitalization policies for an overall amount of 33 million euros as compared to the 7 from last year.

The greatest exposure is for the subsidiary Terleasing, which has items representing about 5% of the bank's total loans..

Deteriorated Assets

The net value of deteriorated assets decreased significantly as compared to 2004. With regards to this, it should be pointed out that, during the reclassification of the balance in terms of IAS, the bank also inserted overdue credit among its risk items, in accordance with the supervisory regulations. Taking into account that the devaluation criteria of the risk items is different because of the application of the IAS 32 and 39 as of January 1, 2005, the deteriorated assets of the bank, after devaluation, are the following:

Deteriorated Assets	Year	Year	Variations 04-05	
	12/31/2005	**12/31/2004**	**Absolute**	**%**
Non performing loans	8.7	9.7	(1.0)	(10.6)
Problem loans	19.1	24.3	(5.2)	(21.4)
Overdue credit	12.5	21.5	(9.0)	(41.8)
Restructured credit	0.1	0	0.1	Not available
Total deteriorated assets	**40.4**	**55.5**	**(15.1)**	**(27.2)**

The decrease in value of non-performing loans is due both to a contained entry in the sector and to the updating of their value in FTA on January 1,2005. The dynamics of problem loans, which was substantially stable during the year, shows a decrease This is, above all, due to the registering of portfolio and specific devaluation in this section as opposed to being previously registered together with live credit. The decrease in the value of overdue credit is connected to a certain volatility of this section in addition to specific portfolio corrections, which were carried out in order to take the IAS into account.

On the whole, even after the effects of the transition to IAS, the deteriorated credit section shows a comforting trend both in terms o the value attributed to the different portfolios and in terms of the likelihood of its recovery.

Financial market assets

	Year	Year	Variations 04-05	
	2005	**2004**	**Absolute**	**%**
Financial assets held for trading	640.3	701.0	(60.7)	(8.6)
Financial assets available for sale	11.6	5.4	6.2	114.5
Total financial assets	**651.9**	**706.4**	**(54.5)**	**(7.7)**

At the end of 2005, the bank portfolio amounted to 640.3 million euros. 51.7% of this was made up of government and foreign securities, 45.5% was made up of "investment grade" finance and corporate bonds and the remaining 2.8% was made up of interest rate shares, funds and derivatives.

RISK MANAGEMENT

Risk management activity was aimed at guaranteeing a constant watch over the main risks and giving effective support to the decision making process. This was done by means of the rigorous and timely measurement of risks related to market, credit, rate and liquidity in addition to the ones which are strictly operational.

With this in mind and with the aim of assuring a unitary vision of governance activity, a specific operational unit with a central structure was formally established. This unit has been assigned the task of monitoring market, credit and rate risks as well as corporate planning and typical management control tasks.

Market Risk Control

Market risk is measured not only according to the provisions in Title IV, Chapter III of Supervisory Instructions but also by means of the measuring of the Value at Risk (VAR). This is calculated on a daily basis and used as reference to verify that the operating limits attributed to the specific sector of activity are respected

During 2005, the average daily *VAR,* in reference to all of the bank securities portfolio, turned out to be 541 thousand euros. This figure, together with the average duration, which is equal to 0.359, and the connected precautionary hypothesis of calculation (confidence interval 99% and 10-day temporal outlook), is proof of the contained risk of the securities assets. The calculations are worked out by using the specific application criteria furnished by Bloomberg.

Credit Risk Control

Continuous and careful monitoring of the bank credit exposure was, as usual, also carried out last year. The instrument used, which is called Credit Position Control (CPC), permits the evaluation of the tendency of relations with customers. This is done by verifying a great number of indicators and operating aspects. These differ according to the type of customer, technical form and gravity.
In addition to being a valid early-warning signal, it permits the calculating of a synthetic risk index for each single position and is detectable by branch office, area or even the entire institution. The CPC index is also the tendency component of the complex rating model that the bank is carrying out in cooperation with the information systems supplier.

For the year, the results confirm a contained risk profile with a positive reduction of the average trend assessment from 13 (in 2004) to 10 (on a scale which goes from -100 to +100, where zero represents the absence of behavioural abnormalities and +100 represents the maximum risk). There was a positive evolution of credit quality for all sectors.
In particular, the effectiveness of the corporate segment is once again confirmed with an average assessment of 5. This is a further improvement as compared to the already contained value (of 8) from the previous year.

Operational Risks and Internal Controls

The internal control area has the responsibility of overseeing the regular tendency of operations, processes and risks for the bank, of evaluating that the internal control system works as well as of guaranteeing the safeguarding of asset value and protecting from losses. It is also responsible for the reliability and integrity of information regarding accounting and management and ensuring that operations comply with the policies established by the company's governing body and with internal and external regulations.
The administrative body and board of auditors for the bank are periodically informed of the evaluations made after the necessary controls. The abnormalities found are promptly signalled to the parties concerned so that prompt action for improvement is taken. There are, afterwards, subsequent verifications of the situation. 52 on the spot verifications were made during the year. 44 of them were made among the branches and 17 were made in relation to the entire operations. The subsidiary Terleasing was also subjected to inspection.

Shareholders' equity

	Year	Year	Variations 04-05	
	12/31/005	12/31/2004	Absolute	%
Company capital	26.0	26.0	0.0	0.0
Issuance premium	45.5	45.5	0.0	0.0
Reserves	181.4	174.3	7.2	4.1
Evaluation reserves	9.0	4.9	4.1	84.1
Operating profit	16.7	15.5	1.2	8.0
Shareholders' equity	**278.6**	**266.2**	**12.5**	**4.7**

ANALYSIS OF THE RESULTS

Overall income trend

	Year	Year	Variations 04-05	
	12/31/2005	12/31/2004	Absolute	%
Interest margin	77.7	71.4	6.3	8.8
Net commission	28.5	25.9	2.6	10.1
Earnings margin	111.2	104.0	7.2	6.9
Operating results	30.0	27.7	2.3	8.4
Operating profit	16.7	15.5	1.2	8.0

The balance sheet closed on December 31, 2005 with a net profit of 16.7 million euros, which is an increase of 8.01% from the previous year.

The interest margin

	Year	Year	Variations 04-05	
	2005	**2004**	**Absolute**	**%**
Interest income customers	78.8	68.9	9.9	14.4
Interest expense customers	17.7	16.9	0.7	4.6
Net Interest customers	**61.1**	**51.9**	**9.1**	**17.7**
Interest income on securities	17.1	18.4	(1.2)	(6.8)
Interest expense on securities	1.3	0.5	(0.8)	(151.5)
Net interest securities	**15.8**	**17.8**	**(2.0)**	**(11.4)**
Interest income banks	1.9	2.1	(0.1)	(7.6)
Interest expense banks	0.8	0.1	0.6	438.6
Net interest banks	**1.1**	**2.0**	**(0.8)**	**(41.6)**
Other interest income	0.1	0.1	0	(3.3)
Negative balance of hedging differentials	(0.5)	(0.5)	0	(0.9)
Interest margin	**77.7**	**71.4**	**6.3**	**8.9**

Notwithstanding the contraction of the rate spread, the interest margin increased by 8.86%. This was mainly due to the increase of interest from customers (+17.70%), which fundamentally derived from the greater amount of funds managed.

On the whole, the interest income increased by 9.54%, the interest expense by 12.20%. In particular, the cost of deposits was affected by the sales , during the year, of about 100 million euros worth of bonds.

The earnings margin

	Year	Year	Variations 04-05	
	12/31/2005	**31/12/2004**	**Absolute**	**%**
Interest margin	**77.7**	**71.4**	6.3	8.8
Dividends on stocks and securities	0.5	0.6	(0.1)	(13.6)
Net commission	28.4	25.9	2.6	10.0
Commission earned	30.7	28.0	2.7	9.6
Commission paid	2.3	2.2	0.1	4.3
Net result for trading actiivites	2.6	3.7	(1.1)	(30.1)
Gains/losses on disposal of:	1.8	2.4	(0.6)	(23.5)
a) credit	0.0	0.0	0	0
b) financial assets available for sale	1.8	2.4	(0.6)	(23.7)
c) financial assets held to maturity	0.0	0.0	0	0
d) financial liabilities	0.0	0.0	0	0
Earnings margin	**111.1**	**103.9**	**7.1**	**6.9**

Management performance

	Year	Year	Variations 04-05	
	12/312005	**12/31/2004**	**Absolute**	**%**
Earnings Margin	**111.1**	**103.9**	**7.1**	**6.9**
Administrative expenses	80.0	70.6	9,4	13,3
Personnel expenses	*49.3*	*45.9*	3.4	7.4
Other administrative expenses	*30.8*	*24.7*	6.0	24.5
Value adjustments on tangibile and intangibile real assets	2.0	2,3	(0.3)	(13.9)
Other expenses/income	10.3	7,6	2.7	35.5
Net value adjustment for deterioration of:	(4.1)	(5.1)	1.1	*(21.3)*
a) credit	(3.8)	(4.9)	1.1	*22.7*
b) financial assets available for sale	0.0	0.1	(0.1)	*(100.0)*
c) financial assets held to maturity	0.0	0.0	0.0	*0.0*
d) financial assets	(0.3)	(0.4)	0.1	*23.4*
Net allowance for risk and charges funds	(5.4)	(5.8)	0.4	(6.6)
Profit (Loss) from disposal of investments	0.1	0.1	0.0	(22.7)
Management performance	**30.0**	**27.7**	**2.3**	**8.4**

A rigorous cost control policy was put into effect during the year both for personnel expenses and expenses which were strictly administrative. There was a cut in administrative expenses which were considered non-strategic. The purpose was to free resources which could be used for the strengthening of the commercial network, marketing and initiatives aimed at improving the quality of service for customers.

Net Profit

	Year	Year	Variations 04-05	
	12/31/2005	**12/31/2004**	**Absolute**	**%**
Management performance	**30.0**	**27.7**	**2.3**	**8.4**
Tax on operating income	13.3	12.2	1.1	8.9
Tax rate	*44.5%*	*44.0%*	0.5	1.1
Net Profit	**16.7**	**15.5**	**1.2**	**8.0**

The good capital adequacy of the bank has a 15% solvency ratio that is superior to every benchmark. In addition the future public offer for sale of the holdings held by the foundation will presumably take place during 2006. These factors represent the opportunity to considerably increase the payout index (ration between the dividends paid and net profit for the year) in the years to come even so as to avoid further increasing already solid asset items.

THE GROWTH OF OPERATIVENESS

The Standard and Poor Rating

During the course of the year, the Standard and Poor rating agency was asked to assign an overall evaluation on the operativeness of the bank.

This evaluation is made taking into account economic-financial and strategic-managerial criteria. A detailed analysis is made of the sector the company operates in and its competitive positioning. It uses a scale which goes from AAA (maximum quality of the subject studied) to D (extreme vulnerability) for long term evaluations and from A-1 to D for short term ones. The outlook indicates the medium-long term potential course. In short, the rating allows you to communicate your credit merit in a clear and synthetic way. In other words it provides an authoritative reference which is universally accepted by the market and investors.

During November of this year, S & P gave Tercas its “BBB+” credit rating for long-term and the corresponding A-2 rating for short-term, with stable prospects.

Firstly, this evaluation reflects the visibility of the name in the local territory, the strong capitalization and the liquidity profile. Secondly, it reflects the stable prospects for the growth of the operativeness of the Bank and, at the same time, maintenance of a solid financial profile. According to S&P, the specific credit risk is in line with the other regional Italian banks with the same rating. The profitability is adequate and is in line with the average and the balance sheet offers good capital ratios.

The Basel II Project

During 2005, there continued to be the intervention considered necessary to comply with the general principles imposed by the New Agreement on Capital, which is better known as Basel II.

The activities planned with the supplier of computer services are in an advanced stage. In particular, the projects in progress aim at::

- the creation of internal rating models
- the use of risk mitigation techniques
- the measurement of the overall exposure to credit and market risks in terms of CAR
- the monitoring of management by means of correct performance indicators for risk
- the quantification of the risk exposure of interest and liquidity by means of the ALM method

With reference to the regulations, the activities, which are currently in progress, are consistent with the aim of adopting an “IRB” foundation” type approach in the medium term. At the same time, work is being done to implement all the changes necessary to comply with the provisions connected to the “Standard” approach by January 1, 2007.

The advancement of the rating system is satisfactory: the preparatory phases for the constructing of the historical series have been concluded; discriminant functions for the evaluation of the balance sheet have been defined; the assessment of the tendency has been started; the methodological revision of the rating model necessary to guarantee the compliance with Basel II is in progress.

From a strictly operational point of view, the implementation of automatic scoring systems for acceptance have begun. The regulations for the granting of some loans will be attached to these. The initiative is a part of a more ample project for the revision of the credit policy. It is aimed at reducing the response time, optimizing the use of the appropriate resources and, at the same time, maximizing the relational approach for the segments of clients of greatest interest.

In regards to the calculation of the Minimum Capital Requirements, the estimates made highlight a limited impact from the New Agreement on Capital. The greater absorption can be attributed to the dimensional growth of the assets and to the quantification, for the first time, of the quotas of capital to be held in view of operational risks.

ALM (Asset and Liability Management)

An ALM system was developed in cooperation with Prometeia (a financial consulting association) and with the Cooperative Service Centre. It is expressed in terms of economic capital value and interest margin and permits the measuring of the impact made on the entire year's balance sheet by interest rate variations.

The Present Value analysis is integrated with what is required by the document issued by the Basel Committee "Principles for the Management and supervision of Interest Rate Risk"; assuming that there is a standardized shock rate equal to 200 p.b. and verifying that the impact on economic value is within 20% of the amount of the base and supplementary capital.

The Delta Margin analysis is carried out in such a way as to highlight the specific contribution of the "beta" and "stickiness" factors of the at sight items.

The project was completed during the last part of the year: the first report regards the standing on the first weekday of 2006. The exposure to interest rate risk is monitored monthly and presented to the administrative and bank supervisory bodies every three months

The System of Controls from a Distance (S.C.D.)

During 2003, the bank created a system of controls from a distance to be used as support for the traditional methods of on-the-spot verifications. They permit the highlighting of eventual operational abnormalities by means of the monitoring of the activities carried out by the Operative Unit, based on the information taken from the bank informative system.

There are different sectors monitored and the essence of the control is to verify the compliance with the internal dispositions given, to look into alert signals to be investigated and to evaluate the functioning of the control system with reference to organizational intervention and procedural modifications.

The characteristics of the SCD are: continuity, which permits controlling without interruption; timeliness, which allows the highlighting, in real time, of eventual operative or behavioural abnormalities in the area being controlled; traceability, which guarantees the historical conservation of the data analysed.

It was technically defined as a list of indicators for each operative segment, which are useful in discovering abnormal situations based on their shifting from the chosen risk threshold variance and on the importance of the phenomenon observed. The system, which is already functional and operational, is subject to continual revision depending on the information available and the operational segments to be subjected to control. It is an effective support to the activity of on-the-spot verification which is, at any rate, necessary to identify eventual irregularities taking place with regards to respect for the regulations and instructions given.

COMMERCIAL AND MARKETING STRATEGIES

During 2005, activities were characterized by the organizational and strategic renewal of the commercial area due to the introduction of a new manager and the revision of the business model. The aim is to strengthen the commercial effectiveness of the bank for its leading customers, which are families and small businesses, by means of an improvement in the quality of service offered and a process of optimization of the productive and distributional structure.

Segmentation

The traditional territorial structure of the sales offices are run by an area manager who has the task of optimizing the handling of relations with the branch offices. As a support to this, there was the division of commercial management based on client segment served. This latter process led to the choosing of a person “designed” for each branch office who becomes the only reference point for bank-client relations. In this way, the service offered is improved. The medium term aim of Tercas is to strengthen its role as “the only bank” for its client, by proposing itself as a point of reference partner even for the fulfilment of the most complex credit and financial needs.

During 2005, the process of client segmentation was begun with the establishing of two services (Corporate and Retail) in the commercial area. They are responsible for guiding, managing and monitoring the people assigned to operating in the territory. Once this process becomes completely operative, it will permit a better approach with the client based on his specific needs in addition to the subdividing of company clients according to an approach which is more adequate for the bank operations.

The product unit

2005 was a particularly important year for marketing activity.

After thorough analysis of retail client needs, a current account packaged called “Conto DaVVero” was launched on the market. This current account is dedicated to private citizens and includes many products and services, which are either free or advantageous. Conto DaVVero is composed of three lines so as to better meet the clients’ needs. It is based on the different levels of the use of bank services, in terms of current account, means of payment, loans, investments and additional services. The success of this “all included” account has been demonstrated both in terms of quantity by the number of accounts opened, and in terms of quality by the satisfaction shown by the branch office personnel and clients.

Further progress was made in savings management by means of new bond issues and the launching of GPF Tercas as a means of upselling compared to the traditional savings administrated. The aim of this transformation process is twofold: to guarantee customers a return which is more proportionate to their expectations and to stabilize the profitability of the bank.

STRATEGIC PLAN

During the last part of the year, the 2006-2008 Industrial Plan was developed. It was approved by the Board of Directors at the meeting on January 26, 2006.

In line with the company mission, Tercas intends to further strengthen its identity as an independent bank, which produces value for its stakeholders, as a confirmation of its being at the service of the territory, of families and of the local economy.

In regards to the main areas of intervention of the plan, they concern:

- Strengthening of the commercial area
- Improvement in the level of efficiency and productivity
- Search for greater financial efficiency
- Improvement of human resources

In particular, the strategic Plan has determined that the elements where a great gap has been accumulated with regards to the reference benchmark is in the revenue and efficiency aspects connected to commercial activity. The development of evolutional strategies to be undertaken will be concentrated on these. These strategies take shape in the updating and enriching of product and service offers. Above all, they are aimed at personal loans, loans to families and insurance policies. They also take shape in the enlarging, strengthening and optimizing of the current distribution network and in the strengthening of the organizational structure and the means which support and monitor commercial policies (subdividing of clients, budget). Moreover, relations with local bodies and trade associations (Confidi) will be examined and strengthened. These manoeuvres will take place so as to boost commercial action and gain market shares in the new offices as well.

Greater efficiency and productivity will be obtained by means of a reconverting of personnel and a redistribution of workloads thanks to further automation of data processing systems. There will also be a new branch model with the assigning of experts responsible for corporate and private banking. Moreover, much attention will be paid to the reducing of costs, and, above all, the reducing of administrative costs.

Human resources will be improved by means of interventions, which will serve as support for personal development. The aim is to stimulate customer orientation and attention on the obtaining results.

The bank strategy is also oriented towards an ambitious dimensional growth for internal lines: territorial expansion will be carried out in the three year period from 2006-2008. 22 branch offices will be opened both in zones already covered so as to increase the bank presence (region of Marche), and according to the developmental lines determined (regions of Lazio and southern Romagna)

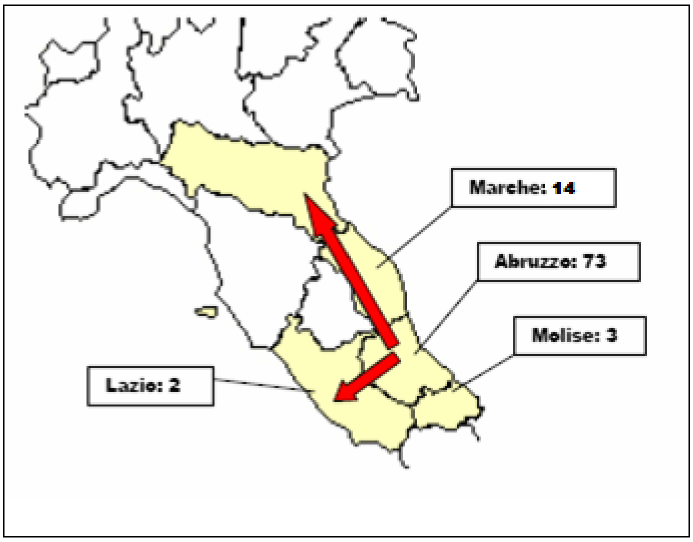
THE TERRITORIAL STRUCTURE AND THE HUMAN RESOURCES

The network

On December 31, the bank had a network of 92 branch offices, which were distributed as follows:

Number of branch offices per province		
	2005	**2004**
Teramo	64	61
Chieti	3	3
Pescara	3	3
L’Aquila	3	3
Campobasso	3	3
Ascoli Piceno	6	6
Macerata	3	3
Ancona	4	3
Pesaro	1	0
Roma	2	0
Total	**92**	**85**
- of which new openings	7	3

Even though the bank confirmed its characteristic as territory bank with the opening of three new branch offices in the province of Teramo, two new branch offices were opened in Rome and one in the province of Ancona in line with its strategies of geographical diversification.



Personnel

On December 31, 2005, the bank staff was made up of 765 employees.730 were full time and 35 were part-time. 458 employees were male and 307 were female.

During the course of the year, there was a net increase of 2 people. This was due to the hiring of 15 people, so as to handle the effort connected to the plan for the opening of new branch offices and the 13 retirements.

On December 31, 2005, 72% of the personnel (551 people) was employed with the commercial network, while the remaining 28% (214 people) was employed at the central offices.

The success of a bank, above all when it has to cope with a significant operational and organizational restructuring process, depends on the ability to manage and improve human resources. In regards to this, the interventions carried out, as well as the ones programmed, aim at a better planning of the workforce, at the containment of costs and at stimulating personnel motivation.

Training activities can be quantified in the allocation of 1.873 days per person. This is the case both for courses organized inside the bank and participation in encounters outside of the bank.

In order to sustain the great organizational and operational changes of the bank, intense training activities aimed at bridging the gap of competences as compared to the new professional figures required and based on the key roles to be covered in the structure, are provided for in the year in progress as well.

In regards to the first point, it should be pointed out that the ambitious internal line development plan requires the maintaining of a workforce, which is in line with the expected development, both in terms of quality and quantity. It was, therefore necessary to start up an optimization course for the staff of the productive units by means of the introducing of new resources and, in part, by means of the professional reallocation and reconverting of those already on duty.

At the same time, the need to elevate profitability targets imposes a rigorous policy of cost containment and control. In regards to personnel management, this meant the adoption of a strategy for the containment of overtime and the progressive replacement of resources belonging to the more advanced age groups.

This context was the beginning of incentives for the retiring of personnel having the greatest seniority. There were 30 employees who retired. !6 retired during 2005 and the remaining 14 during the first part of 2006. As a result, the average age has been reduced to 42.9 years. The overall expense of this process was 1.3 million euros, and it was completely paid for in the year being discussed.

The retirement with incentives, although on a purely voluntary basis, was met with interest by employees and can eventually again be proposed during 2006.

Interventions carried out in regards to the management of work performance have shown considerable results: on the whole, the overtime hours worked during the year decreased by about 20%, which is equivalent to 24,036 units.

In order to maintain the pressure for results high and to stimulate personnel commitment, the institute decided to redesign the incentives system. This was done according to the guidelines adopted by the Board of Administrators during the meeting held on January 26, 2006. Transparent mechanisms, which connect incentives to the results reached, were studied.

The inspiring principles were obtained directly from the company mission and can be summed up in:

- Valuable production
- Transparency
- Meritocracy

The assigning of the bonus is subject to the reaching of specific aims in terms of quantity and quality in keeping with the company plans and programs. Particular attention was placed on the attaining of adequate results in terms of customer satisfaction, organizational efficiency and risk profile containment.

With this system, which applies to all the management and network personnel, the bank sets out to promote the active participation of resources in the company strategies for dimensional growth and the reaching of greater standards of quality.

Note for the reading of balance sheet data

In the following balance sheet layout, the data from the year 2004 is displayed for comparison. It has been redetermined as a result of the adoption of the new IAS-IFRS accounting principles. An exception to this are the IFRS 4 and the ones relating to the financial instruments regulated by the IAS 32 and 39 principles, for which there is only the reclassification of the new tabular system

BALANCE SHEET TERCAS S.P.A.(JOINT-STOCK COMPANY) - 2005

STATEMENT OF ASSETS AND LIABILITIES ON DECEMBER 31, 2005			
	Assets	**2005**	**2004**
10.	Cash and cash equivalents	19.588.490	18.165.737
20.	Financial assets held for trading	640.316.401	700.969.690
30.	Financial assets designated as fair value	0	0
40.	Available for sale Financial assets	11.577.079	5.396.580
50.	Held to maturity financial assets	0	0
60.	Loans to banks	196.947.040	109.534.758
70.	Loans to customers	1.757.452.715	1.370.567.329
80.	Hedging derivatives	0	0
90.	Changes in fair value of financial assets in hedged portfolios	0	0
100.	Shareholdings	13.041.757	12.919.435
110.	Tangible assets	30.256.685	31.121.619
120.	Intangible assets	215.989	229.120
	of which:		
	- goodwill		0
130.	Tax assets	14.344.106	12.421.940
	a) current	5.089.952	5.984.041
	b) deferred	9.254.154	6.437.899
140.	Non-current assets and disposal groups held for sale		0
150.	Other assets	46.602.400	41.256.662
	Total Assets	**2.730.342.662**	**2.302.582.869**

	liabilities and shareholders' equity	2005	2004
10.	Due to banks	122.076.814	15.158.206
20.	Due to customers	1.840.430.078	1.660.355.589
30.	Securities issued	294.439.820	228.439.953
40.	Financial liabilities held for trading	1.977.410	2.535.715
50.	Financial liabilites designated as fair value	0	0
60.	Hedging derivatives	0	0
70.	Changes in fair value of financial liabilities in hedged portfolios	0	0
80.	tax liabilities	10.674.336	10.410.877
	a) current	8.096.055	7.069.553
	b) deferred	2.578.281	3.341.325
90.	Liabilities in disposal groups held for sale	0	0
100.	other liabilities	133.556.055	77.123.708
110.	Employee severance pay	21.558.763	20.316.136
120.	Provisions for risks and charges:	27.997.388	23.125.002
	a) retirement benefits and other obligations	7.335.282	7.474.227
	b) other funds	20.662.106	15.650.775
130.	Revaluation reserves	8.966.774	4.870.861
140.	Redeemable shares	0	0
150.	Capital instruments	0	0
160.	Reserves	181.432.329	174.250.921
170.	Share premium	44.544.408	44.544.408
180.	Capital	26.000.000	26.000.000
190.	Own shares	0	0
200.	Profit (Loss) for the year	16.688.489	15.451.492
	Total liabilities	**2.730.342.662**	**2.302.582.869**

INCOME STATEMENT ON DECEMBER 31, 2005

	Income statement items	2005	2004
10.	Interest income and similar revenues	98.082.182	89.541.719
20.	Interest expenses and similar charges	(20.333.831)	(18.123.428)
30.	**Interest income**	**77.748.351**	**71.418.291**
40.	Commission income	30.737.766	28.033.124
50.	Commission expense	(2.259.408)	(2.165.673)
60.	**Net commission**	**28.478.359**	**25.867.451**
70.	Dividends and similar revenues	526.793	609.899
80.	Net profits (losses) on trading activities	2.556.854	3.660.779
90.	Net profits (losses) from hedge accounting		0
100.	Profits/losses from the disposal of:	1.845.468	2.412.287
	a) loans and receivables		0
	b) available-for-sale financial assets	1.841.006	2.412.287
	c) held-to-maturity investments	0	0
110.	d) financial liabilities	4.462	0
	Profilts/losses on financial assets and liabiliites designated at fair value		0
120.	**Net income**	**111.155.825**	**103.968.707**
130.	Net value adjustment for impairment losses on:		
	a) loans	(3.782.900)	(4.891.261)
	b) available-for-sale financial assets	0	96.686
	c) held-to-maturity investments	0	0
	d) other financial assets	(270.528)	(353.199)
140.	**Net result of financial activities**	**(4.053.428)**	**(5.147.775)**
150.	Administrative costs:	(80.038.579)	(70.647.939)
	a) personnel expenses	(49.287.222)	(45.958.790)
	b) other administrative expenses	(30.751.357)	(24.689.149)
160.	Net provisions for risks and charges	(5.442.702)	(5.828.322)
170.	Net adjustments to tangible assets	(1.898.316)	(2.236.986)
180.	Net adjustments to intangible assets	(92.369)	(76.521)
190.	Other operating expenses/income	10.328.560	7.587.112
200.	**Operating costs**	**(77.143.407)**	**(71.202.656)**
210.	Profits/losses on investments in associates	0	0
220.	Net result of fair value adjustments to tangible and intangible assets	0	0
230.	Value adjustment on goodwill	0	0
240.	Profits (losses) on disposal of investments	53.094	68.728
250	**Operating Profit (Loss) before tax from continuing operations**	**30.012.084**	**27.687.004**
260.	Income tax related to continuing operations for the period	(13.323.596)	(12.235.511)
270.	**Net Profit (Loss) after tax from continuing operations**	**16.688.489**	**15.451.492**
280.	Net Profit (Loss) from disontinued operations	0	0
290.	**Profit (Loss) for the period**	**16.688.489**	**15.451.492**

TERCAS INDIVIDUAL FINANCIAL STATEMENT
Direct Method

A. OPERATIONS	Amount	
	2005	2004
1. Management activities (+/-)	**20.818.668**	**20.511.701**
- interest received	98.045.153	89.504.546
- interest paid (-)	(20.333.831)	(18.123.428)
- dividends and similar revenues (+)	0	0
- net commissions (+/-)	28.478.359	28.033.123
- personnel costs (-)	(46.679.859)	(45.463.513)
- net premiums collected	0	0
- other insurance income/charges	0	0
- other costs (-)	(30.751.357)	(24.689.149)
- other income (write-backs +)	4.751.327	1.768.174
- duties and taxes paid (-)	(12.691.124)	(10.518.052)
- costs/income on groups of assets being disposed	0	0
net of taxes (+/-)	0	0
2. Liquid assets generated/absorbed by financial assets (+/-)	**(363.571.572)**	**(113.682.076)**
- financial assets held for trading (capital gains)	63.985.288	(10.052.294)
- financial assets designated as fair value	0	0
- available for sale financial assets (capital gains)	(4.339.493)	(1.538.557)
- due from customers	(386.885.386)	(149.544.792)
- due from banks: repayable on demand	(87.412.282)	43.336.278
- due from banks: other loans	0	0
- other financial assets / liabilities	51.080.301	4.117.289
3. Liquid assets generated / absorbed by financial liabilities (+/-)	**350.703.873**	**102.618.389**
- due to banks: repayable on demand	106.918.608	4.889.517
- due to banks: other debts	0	0
- due to customers	180.074.489	109.155.768
- securities issued	65.999.866	(11.176.786)
- financial liabilities held for trading	(558.305)	789.469
- financial liabilities evaluated at fair value	0	0
- other liabilities (FTFR)	(1.730.785)	(1.039.579)
Net liquid assets generated / absorbed by operations (+/-)	**7.950.969**	**9.448.014**
B. INVESTMENTS		
1. Liquid assets generated by (+)	**581.162**	**678.626**
- sale of investments	0	0
- dividends received from investments	526.793	609.899
- sale of financial assets held to maturity	0	0
- sale of tangible assets	54.369	68.727
- sale of intangible assets	0	0
- sale of subsidiaries and divisions	0	0
2. Liquid assets absorbed by (-)	**(1.190.506)**	**(1.621.000)**
- purchase of investments (Terleasing spa)	(122.322)	0
- purchase of financial assets held to maturity	0	0
- purchase of tangible assets	(1.068.184)	(1.621.000)
- purchase of subsidiaries and divisions	0	0
Net liquid assets generated/absorbed by investments (+/-)	**(609.344)**	**(942.374)**
C. FUNDING ACTIVITIES		
- issue/purchase of own shares	0	0
- dividend distribution and other uses (special allocation fund)	(5.918.872)	(5.741.906)
Net liquidity generated/absorbed by funding activities (+/-)	**(5.918.872)**	**(5.741.906)**
NET LIQUID ASSETS GENERATED / ABSORBED DURING THE YEAR (+/-)	**1.422.753**	**2.763.734**

Key
(+) generated
(-) absorbed

RECONCILIATION		
Items	**Amount 2005**	**Amount 2004**
Opening balance of cash and cash equivalents	**18.165.737**	**15.402.003**
Net total liquid asset generated/absorbed during the year	1.422.753	2.763.734
Cash and cash equivalents: effect of variations in exchange rates	0	0
Closing balance of cash and cash equivalents	**19.588.490**	**18.165.737**