



Financial Statements and Independent Auditor's
Report

ARDSHININVESTBANK closed joint stock
company

31 December, 2007

Contents

	Page
Independent auditor's report	1
Income statement	3
Balance sheet	4
Statement of changes in equity	5
Statement of cash flows	6
Accompanying notes to the financial statements	7

Independent auditor's report

Գրանթ Թորնթոն Ամյո ՍՊԸ

ՀՀ, ք. Երեւան 0012
Վաղարշյան 8/1

Հ. +374 10 260 964

Ֆ. +374 10 260 961

Grant Thornton Amyot LLC

8/1 Vagharshyan Str.
0012 Yerevan, Armenia

T +374 10 260 964

F +374 10 260 961

www.gta.am

To the Shareholders of Closed Joint Stock Company ARDSHININVESTBANK:

We have audited the accompanying financial statements of Ardshininvestbank CJSC (the “Bank”), which comprise the balance sheet as at December 31, 2007, and the income statement, statement of changes in equity and cash flow statement for the year then ended, and a summary of significant accounting policies and other explanatory notes.

Management's responsibility for the financial statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with 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 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 Bank'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 Bank's internal control.

An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

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

Opinion

In our opinion, the financial statements give a true and fair view of the financial position of the Bank as of December 31, 2007, and of its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards.

03 March 2008

Yerevan

Income statement

In thousand Armenian drams		Year ended December 31, 2007 (audited)	Year ended December 31, 2006 (audited)
	Notes		
Interest and similar income	6	8,199,371	4,743,574
Interest and similar expense	6	(2,242,086)	(1,300,865)
Net interest income		5,957,285	3,442,709
Fee and commission income	7	2,224,622	1,982,751
Fee and commission expense		(12,183)	(31,979)
Net fee and commission income		2,212,439	1,950,772
Gains less losses from trading in foreign currencies		1,402,711	1,099,769
Gains less losses on investments available for sale		449,107	476,893
Other income	8	106,842	69,473
Impairment charge for credit losses	9	(266,853)	(297,397)
Staff costs	10	(2,485,112)	(2,103,476)
Depreciation of property and equipment		(556,673)	(476,103)
Amortization of intangible assets		(6,567)	(4,938)
Other expenses	11	(1,657,838)	(1,502,642)
Profit before income tax		5,155,341	2,655,060
Income tax expense	12	(1,028,219)	(554,340)
Profit for the year		4,127,122	2,100,720

The accompanying notes on pages 7 to 47 are an integral part of these financial statements.

Balance sheet

In thousand Armenian drams	Notes	As of December 31, 2007 (audited)	As of December 31, 2006 (audited)
ASSETS			
Cash and balances with CBA	13	14,034,501	12,527,134
Amounts due from other financial institutions	14	10,048,506	12,638,535
Loans and advances to customers	15	54,496,618	23,405,293
Investments available for sale	16	7,347,420	14,665,005
Property, plant and equipment	17	6,333,441	5,330,469
Intangible assets	18	100,241	108,780
Other assets	19	930,047	475,840
TOTAL ASSETS		93,290,774	69,151,056
LIABILITIES AND EQUITY			
Liabilities			
Amounts due to financial institutions	20	12,292,227	1,503,859
Amounts due to customers	21	61,082,892	55,882,612
Current income tax liabilities		604,964	92,290
Deferred income tax liabilities	12	287,366	292,966
Other liabilities	22	340,188	225,143
Other provisions	23	4,160	10,470
Total liabilities		74,611,797	58,007,340
Equity			
Share capital	24	13,802,404	7,391,552
Share premium		1,711,179	8,430
Statutory general reserve		616,430	362,353
Other reserves		1,298,110	1,308,149
Retained earnings		1,250,854	2,073,232
Total equity		18,678,977	11,143,716
TOTAL LIABILITIES AND EQUITY		93,290,774	69,151,056

The financial statements from pages 3 to 47 were signed by the Bank's Chairman of Executive Board and Chief Accountant on 29.02.08. The accompanying notes on pages 7 to 47 are an integral part of these financial statements.

Aram Andreasian
Chairman of Executive Board

Manvel Sahakyan
Chief accountant

Statement of changes in equity

In thousand Armenian drams	Share capital	Share premium	Statutory general reserve	Revaluation reserve of securities available for sale	Revaluatio n reserve of PPE	Retained earnings	Total
Balance as of January 1, 2006 (audited)	3,020,024	-	248,891	84,208	1,222,369	4,434,441	9,009,933
Adjustment to reserve on disposal of PPE	-	-	-	-	(93)	-	(93)
Net unrealized gains from changes in fair value	-	-	-	357,815	-	-	357,815
Net gains realized to net profit on disposal of available-for-sale instruments	-	-	-	(375,782)	-	-	(375,782)
Effect of deferred taxes	-	-	-	3,593	16,039	-	19,632
Total income and expense recognized directly in equity	-	-	-	(14,374)	15,946	-	1,572
Profit for the year	-	-	-	-	-	2,100,720	2,100,720
Total income and expense for the year	-	-	-	(14,374)	15,946	2,100,720	2,102,292
Increase in share capital	4,371,528	-	-	-	-	-	4,371,528
Share premium	-	8,430	-	-	-	-	8,430
Distribution to reserve	-	-	113,462	-	-	(113,462)	-
Dividends to shareholders	-	-	-	-	-	(4,348,467)	(4,348,467)
Balance as of December 31, 2006 (audited)	7,391,552	8,430	362,353	69,834	1,238,315	2,073,232	11,143,716
Net unrealized gains from changes in fair value	-	-	-	445,070	-	-	445,070
Net gains realized to net profit on disposal of available-for-sale instruments	-	-	-	(437,714)	-	-	(437,714)
Effect of deferred taxes	-	-	-	(1,471)	(15,924)	15,924	(1,471)
Total income and expense recognized directly in equity	-	-	-	5,885	(15,924)	15,924	5,885
Profit for the year	-	-	-	-	-	4,127,122	4,127,122
Total income and expense for the year	-	-	-	5,885	(15,924)	4,143,046	4,133,007
Increase in share capital	6,410,852	-	-	-	-	-	6,410,852
Share premium	-	1,702,749	-	-	-	-	1,702,749
Dividends to shareholders	-	-	-	-	-	(4,711,347)	(4,711,347)
Distribution to reserve	-	-	254,077	-	-	(254,077)	-
Balance as of December 31, 2007 (audited)	13,802,404	1,711,179	616,430	75,719	1,222,391	1,250,854	18,678,977

Statement of cash flows

In thousand Armenian drams	Year ended December 31, 2007 (audited)	Year ended December 31, 2006 (audited)
Cash flows from operating activities		
Interest received	8,181,717	4,618,278
Interest paid	(2,128,810)	(1,275,368)
Fees and commissions received	2,224,622	1,982,751
Fees and commissions paid	(12,183)	(31,979)
Realised gains less losses from dealing in foreign currencies	1,402,711	1,099,769
Other income received	209,662	368,168
Salaries and benefits paid	(2,512,064)	(1,940,049)
Other operating expenses paid	(1,609,224)	(305,599)
Cash flows from operating activities before changes in operating assets and liabilities	5,756,431	4,515,971
<i>Net (increase)/decrease in operating assets</i>		
Amounts due from other financial institutions	(415,144)	-
Loans and advances to customers	(33,570,142)	2,006,687
Other assets	(359,145)	12,813
<i>Increase/(decrease) in operating liabilities</i>		
Amounts due to financial institutions	5,152,257	343,727
Amounts due to customers	9,553,681	12,668,123
Other liabilities	109,919	(1,802,594)
Net cash flow from operating activities before income tax	(13,772,143)	17,744,727
Income tax paid	(522,617)	(731,476)
Net cash from/(used in) operating activities	(14,294,760)	17,013,251
Cash flows from investing activities		
Purchase of investment securities	(11,366,859)	(5,333,663)
Proceeds from sale and redemption of investment securities	19,146,576	-
Purchase of property and equipment and intangible assets	(1,589,446)	(883,817)
Proceeds from sale of property and equipment	12,170	36,620
Net cash from/(used in) investing activities	6,202,441	(6,180,860)
Cash flow from financing activities		
Proceeds from issue of share capital	6,410,852	4,371,528
Share premium	1,702,749	8,430
Loans redeemed from financial institutions	5,316,958	281,068
Dividends paid to shareholders	(4,711,347)	(4,348,466)
Net cash flow from financing activities	8,719,212	312,560
Effect of exchange rate changes on cash and cash equivalents	(2,394,678)	(70,120)
Net increase/(decrease) in cash and cash equivalents	(1,767,785)	11,074,831
Cash and cash equivalents at the beginning of the year	24,444,280	13,369,449
Cash and cash equivalents at the end of the year (Note 13)	22,676,495	24,444,280

Accompanying notes to the financial statements

1 Principal activities

Ardshininvestbank CJSC (the “Bank”) is a closed joint-stock bank , which was incorporated in the Republic of Armenia in 2003. The Bank is regulated by the legislation of RA and conducts its business under license number 83, granted on 25 February 2003 by the Central Bank of Armenia (the “CBA”).

The Bank accepts deposits from the public and extends credit, transfers payments in Armenia and abroad, exchanges currencies and provides other banking services to its commercial and retail customers. Its main office is in Yerevan and it has 51 branches in Yerevan and in different regions and one representative office in Paris.

The registered office of the Bank is located at: 13/1 Grigor Lusavorichi str., Yerevan, Armenia.

2 Armenian business environment

Armenia continues to undergo political and economic changes. As an emerging market, Armenia does not possess a developed business and regulatory infrastructure that generally exists in a more mature free market economy. Consequently, operations carried out in Armenia involve certain risks that are not typically associated with those in developed countries.

The Bank could be affected, for the foreseeable future, by these risks and their consequences. The accompanying financial statements do not include any adjustments that may result from the future clarification of these uncertainties. Such adjustments, if any, will be reported in the Bank’s financial statements in the period when they become known and estimable.

In addition, economic conditions continue to limit the volume of activity in the financial markets. Market quotations in generally illiquid markets may not be reflective of the values for financial instruments, which would be determined in an efficient, active market involving many willing buyers and willing sellers.

3 Basis of preparation

3.1 Statement of compliance

The financial statements of the Bank have been prepared in accordance with International Financial Reporting Standards (“IFRS”) as developed and published by the International Accounting Standards Board (IASB), and Interpretations issued by the International Financial Reporting Interpretations Committee (“IFRIC”).

3.2 Basis of measurement

The financial statements have been prepared on a fair value basis for financial assets and liabilities at fair value through profit or loss and available for sale assets, except those for which a reliable measure of fair value is not available. Other financial assets and liabilities are stated at amortized cost and non-financial assets and liabilities are stated at historical cost, with the exception of buildings, which are stated at revalued amount.

3.3 Functional and presentation currency

Functional currency of the Bank is the currency of the primary economic environment in which the Bank operates. The Bank's functional currency and the Bank's presentation currency is Armenian Drams ("AMD"), since this currency best reflects the economic substance of the underlying events and transactions of the Bank. The Bank prepares statements for regulatory purposes in accordance with legislative requirements and Accounting Standards of the Republic of Armenia. These financial statements are based on the Bank's books and records as adjusted and reclassified in order to comply with IFRS. The financial statements are presented in thousands of AMD, which is not convertible outside Armenia.

3.4 Reclassifications

Where necessary, comparative figures have been adjusted to conform to changes in presentation in the current year.

3.5 New standards and interpretations

Certain new IFRSs became effective for the Bank from 1 January 2007. Listed below are those new or amended standards or interpretations which are or in the future could be relevant to the Bank's operations and the nature of their impact on the Bank's accounting policies.

IFRS 7, Financial Instruments: Disclosures and a complementary Amendment to IAS 1 Presentation of Financial Statements - Capital Disclosures (effective from 1 January 2007).

The IFRS 7 introduced new disclosures to improve the information about financial instruments, including about quantitative aspects of risk exposures and the methods of risk management. The new quantitative disclosures provide information about the extent of exposure to risk, based on information provided internally to the entity's key management personnel. Qualitative and quantitative disclosures cover exposure to credit risk, liquidity risk and market risk including sensitivity analysis to market risk. IFRS 7 replaced IAS 30, Disclosures in the Financial Statements of Banks and Similar Financial Institutions, and some of the requirements in IAS 32, Financial Instruments: Disclosure and Presentation. The Amendment to IAS 1 introduced disclosures about the level of an entity's capital and how it manages capital. The adoption of IFRS 7 and the amendment to IAS 1 had no impact on the reported profits or financial position of the Bank. The new disclosures are made in these financial statements and in accordance with the transitional requirements of the standards, the Bank has provided full comparative information.

Other new standards or interpretations. The Bank has adopted the following other new standards or interpretations:

- IFRIC 7, *Applying the Restatement Approach under IAS 29* (effective for periods beginning on or after 1 March 2006);
- IFRIC 8, *Scope of IFRS 2* (effective for periods beginning on or after 1 May 2006);
- IFRIC 9, *Reassessment of Embedded Derivatives* (effective for annual periods beginning on or after 1 June 2006);
- IFRIC 10, *Interim Financial Reporting and Impairment* (effective for annual periods beginning on or after 1 November 2006).

The effect of these changes on the financial statements of the Bank is not significant.

At the date of authorization of these financial statements, the following Standards and Interpretations to the Bank were issued but not yet effective:

- IFRIC 12 *Service Concession Arrangement* (effective January 1, 2008)
- IFRIC 13 *Customer Loyalty Programmes* (effective July 1, 2008)
- IFRIC 14 *IAS 19 The Limit on a Defined Benefit Asset, Minimum Funding Requirements and their Interaction* (effective January 1, 2008)
- IAS 23 *Borrowing Costs (revised 2007)* (effective January 1, 2009)
- IFRS 8 *Operating Segments* (effective January 1, 2009)

4 Summary of significant accounting policies

The following significant accounting policies have been applied in the preparation of the financial statements. The accounting policies have been consistently applied.

4.1 Recognition of income and expenses

Revenue is recognized to the extent that it is probable that the economic benefits will flow to the Bank and the revenue can be reliably measured. Expense is recognized to the extent that it is probable that the economic benefits will flow from the Bank and the expense can be reliably measured. The following specific criteria must also be met before revenue is recognized:

Interest income and expense

Interest income and expense for all interest-bearing financial instruments, except for those classified as held for trading or designated at fair value through profit or loss, are recognised within 'interest income' and 'interest expense' in the income statement using the effective interest method.

Once the recorded value of a financial asset or a group of similar financial assets has been reduced due to an impairment loss, interest income continues to be recognized using the original effective interest rate applied to the new carrying amount.

Fee and commission income and expense

Loan origination fees for loans issued to customers are deferred (together with related direct costs) and recognised as an adjustment to the effective yield of the loans. Fees, commissions and other income and expense items are generally recorded on an accrual basis when the service has been provided. Portfolio and other management advisory and service fees are recorded based on the applicable service contracts. Asset management fees related to investment funds are recorded over the period the service is provided. The same principle is applied for wealth management, financial planning and custody services that are continuously provided over an extended period of time.

Net trading income

Net trading income comprises gains less losses related to trading assets and liabilities, and includes all realized and unrealized fair value changes, interest, dividends and foreign exchange differences related to trading assets and liabilities. Net trading income also includes gains less losses from trading in foreign currencies.

Rental income

Rental income is accounted for on a straight-line basis over the lease term on ongoing leases and is recorded in the income statement in "Other income".

4.2 Foreign currency translation

Transactions in foreign currencies are initially recorded in the functional currency rate ruling at the date of the transactions. Gains and losses resulting from the translation of trading assets are recognised in the statement of income in net trading income, while gains less losses resulting from translation of non-trading assets are recognized in the statement of income in other income or other expense. Monetary assets and liabilities denominated in foreign currencies are retranslated at the functional currency rate of exchange ruling at the balance sheet date.

Changes in the fair value of monetary securities denominated in foreign currency classified as available for sale are analysed between translation differences resulting from changes in the amortised cost of the security and other changes in the carrying amount of the security. Translation differences related to changes in the amortised cost are recognised in profit or loss, and other changes in the carrying amount are recognised in equity.

Non-monetary items that are measured in terms of historical cost in a foreign currency are translated using the exchange rates at the dates of the initial transactions. Non-monetary items measured at fair value in a foreign currency are translated using the exchange rates at the date when the fair value was determined. Translation differences on non-monetary items, such as equities held at fair value through profit or loss, are reported as part of the fair value gain or loss. Translation differences on non-monetary items, such as equities classified as available-for-sale financial assets, are included in the fair value reserve in equity.

Differences between the contractual exchange rate of a certain transaction and the prevailing average exchange rate on the date of the transaction are included in gains less losses from trading in foreign currencies in net trading income.

The exchange rates at year-end used by the Bank in the preparation of the financial statements are as follows:

	December 31, 2007	December 31, 2006
AMD/1 US Dollar	304.22	363.50
AMD/1 Euro	446.96	478.73

4.3 Taxation

Income tax on the profit for the year comprises current and deferred tax. Income tax is recognized in the income statement except to the extent that it relates to items recognized directly in equity, in which case it is recognized in equity.

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

Deferred tax assets and liabilities are calculated in respect of temporary differences using the liability method. Deferred income taxes are provided for all temporary differences arising between the tax bases of assets and liabilities and their carrying values for financial reporting purposes, except where the deferred income tax arises from the initial recognition of goodwill or of an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit nor taxable profit or loss.

A deferred tax asset is recorded only to the extent that it is probable that taxable profit will be available against which the deductible temporary differences can be utilised. Deferred tax assets and liabilities are measured at tax rates that are expected to apply to the period when the asset is realised or the liability is settled, based on tax rates that have been enacted or substantively enacted at the balance sheet date.

Deferred income tax is provided on temporary differences arising on investments in subsidiaries, associates and joint ventures, except where the timing of the reversal of the temporary difference can be controlled and it is probable that the temporary difference will not reverse in the foreseeable future.

The Republic of Armenia also has various operating taxes, which are assessed on the Bank's activities. These taxes are included as a component of other expenses in the statement of income.

4.4 Cash and cash equivalents

Cash and cash equivalents comprise cash on hand, balances on correspondent accounts with the Central Bank of Armenia (excluding those funds deposited for the settlement of ArCa payment cards), and amounts due from other banks, which can be converted into cash at short notice and which are subject to an insignificant risk of changes in value.

Cash and cash equivalents are carried at amortised cost.

4.5 Amounts due from other financial institutions

In the normal course of business, the Bank maintains advances or deposits for various periods of time with other banks. Loans and advances to banks with a fixed maturity term are subsequently measured at amortized cost using the effective interest method. Those that do not have fixed maturities are carried at amortized cost based on maturities estimated by management. Amounts due from other financial institutions are carried net of any allowance for impairment losses.

4.6 Financial instruments

The Bank recognizes financial assets and liabilities on its balance sheet when it becomes a party to the contractual obligation of the instrument. Regular way purchases and sales of financial assets and liabilities are recognised using settlement date accounting. Regular way purchases of financial instruments that will be subsequently measured at fair value between trade date and settlement date are accounted for in the same way as for acquired instruments.

When financial assets and liabilities are recognised initially, they are measured at fair value, plus, in the case of investments not at fair value through profit or loss, directly attributable transaction costs.

After initial recognition all financial liabilities, other than liabilities at fair value through profit or loss (including held for trading) are measured at amortized cost using effective interest method. After initial recognition financial liabilities at fair value through profit or loss are measured at fair value.

The Bank classified its financial assets into the following categories: loans and receivables, financial instruments at fair value through profit or loss, available-for-sale financial instruments and held-to-maturity investments. The classification of investments between the categories is determined at acquisition based on the guidelines established by the management. The Bank determines the classification of its financial assets after initial recognition and, where allowed and appropriate, re-evaluates this designation at each financial year-end.

Financial assets at fair value through profit or loss

This category has two subcategories: financial assets held for trading and those designated at fair value through profit or loss. A financial asset is classified in this category if acquired for the purpose of selling in the short-term or if so designated by management from the initial acquisition of that asset.

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 amortised cost for such as loans and advances to customers or banks and debt securities in issue;
- Certain investments, such as equity investments, that 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 are designated at fair value through profit and loss; and
- Financial instruments, such as debt securities held, containing one or more embedded derivatives significantly modify the cash flows, are designated at fair value through profit and loss.

Derivatives are also classified as held for trading unless they are designated as effective hedging instruments. Gains or losses on financial assets held for trading are recognised in the statement of income.

Held-to-maturity investments

Held-to-maturity investments are financial assets with fixed or determinable payments and fixed maturities that the Bank's management has the positive intention and ability to hold to maturity. Were the Bank to sell other than insignificant amount of held-to-maturity assets not close to their maturity, the entire category would be reclassified as available-for-sale. Held-to-maturity investments are carried at amortized cost using the effective interest rate method, less any allowance for impairment.

Loans and receivables

Loans and receivables are financial assets with fixed or determinable payments, which arise when the Bank provides money directly to a debtor with no intention of trading the receivable.

Loans granted by the Bank with fixed maturities are initially recognized at fair value plus related transaction costs. Where the fair value of consideration given does not equal the fair value of the loan, for example where the loan is issued at lower than market rates, the difference between the fair value of consideration given and the fair value of the loan is recognized as a loss on initial recognition of the loan and included in the income statement as losses on origination of assets. Subsequently, the loan carrying value is measured using the effective interest method. Loans to customers that do not have fixed maturities are accounted for under the effective interest method based on expected maturity. Loans to customers are carried net of any allowance for impairment losses.

Available-for-sale financial instruments

Investments available for sale represent debt and equity investments that are 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. After initial recognition available-for sale financial assets are measured at fair value with gains or losses being recognised as a separate component of equity until the investment is derecognised or until the investment is determined to be impaired at

which time the cumulative gain or loss previously reported in equity is included in the statement of income. However, interest calculated using the effective interest method is recognised in the statement of income. Dividends on available-for-sale equity instruments are recognised in profit or loss when the Bank's right to receive payment is established.

The fair value of investments that are actively traded in organised financial markets is determined by reference to quoted market bid prices at the close of business on the balance sheet date. For investments where there is no active market, fair value is determined using the market value model or discounted cash flow analysis. Otherwise the investments are stated at cost less any allowance for impairment.

4.7 Impairment of financial assets

The Bank assesses at each balance sheet date whether a financial asset or group of financial assets is impaired.

Assets carried at amortised cost

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 ("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.

Criteria used to determine that there is objective evidence of an impairment loss may include indications that the borrower or a group of borrowers is experiencing significant financial difficulty (for example, equity ratio, net income percentage of sales), default or delinquency in interest or principal payments, breach of loan covenants or conditions, deterioration in the value of collateral, the probability that they will enter bankruptcy or other financial reorganization and where observable data indicate that there is a measurable decrease in the estimated future cash flows, such as changes in arrears or economic conditions that correlate with defaults.

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

If there is objective evidence that an impairment loss on financial assets carried at amortised cost has been incurred, the amount of the loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows (excluding future credit losses that have not been incurred) discounted at the financial asset's original effective interest rate (i.e. the effective interest rate computed at initial recognition). The carrying amount of the asset shall be reduced through use of an allowance account. The amount of the loss shall be recognised in the statement of income. If a loan or held-to-maturity investment has a variable interest rate, the discount rate for measuring any impairment loss is the current effective interest rate determined under the contract. The Bank may measure impairment on the basis of an instrument's fair value using an observable market price.

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

For the purpose of a collective evaluation of impairment, financial assets are grouped on the basis of the Bank's internal credit grading system that considers credit risk characteristics such as asset type, industry, geographical location, collateral type, past-due status and other relevant factors.

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 Bank to reduce any differences between loss estimates and actual loss experience.

Loans together with the associated allowance are written off when there is no realistic prospect of future recovery and all collateral has been realized or has been transferred to the Bank. If, in a subsequent year, the amount of the estimated impairment loss increases or decreases because of an event occurring after the impairment was recognized, the previously recognized impairment loss is increased or reduced by adjusting the allowance account. If future write-off is later recovered, the recovery is credited to the allowance account.

Renegotiated loans

Where possible, the Bank seeks to restructure loans rather than to take possession of collateral. This may involve extending the payment arrangements and the agreement of new loan conditions. Once the terms have been renegotiated, the loan is no longer considered past due. Management continuously reviews renegotiated loans to ensure that all criteria are met and that future payments are likely to occur. The loans continue to be subject to an individual or collective impairment assessment, calculated using the loan's original effective interest rate.

Available-for-sale financial assets

If an available-for-sale asset is impaired, an amount comprising the difference between its cost (net of any principal payment and amortisation) and its current fair value, less any impairment loss previously recognised in the statement on income, is transferred from equity to the statement of income.

Reversals in respect of equity instruments classified as available-for-sale are not recognised in the statement of income. Reversals of impairment losses on debt instruments are reversed through the statement of income if the increase in fair value of the instrument can be objectively related to an event occurring after the impairment loss was recognised in profit or loss.

4.8 Derecognition of financial assets and liabilities

Financial assets

A financial asset (or, where applicable a part of a financial asset or part of a group of similar financial assets) is derecognised where:

- the rights to receive cash flows from the asset have expired;
- the Bank has transferred its rights to receive cash flows from the asset, or retained the right to receive cash flows from the asset, but has assumed an obligation to pay them in full without material delay to a third party under a 'pass-through' arrangement; and
- the Bank either (a) has transferred substantially all the risks and rewards of the asset, or (b) has neither transferred nor retained substantially all the risks and rewards of the asset, but has transferred control of the asset.

Where the Bank has transferred its rights to receive cash flows from an asset and has neither transferred nor retained substantially all the risks and rewards of the asset nor transferred control of the asset, the asset is recognised to the extent of the Bank's continuing involvement in the asset. Continuing involvement that takes the form of a guarantee over the transferred asset is measured at the lower of the original carrying amount of the asset and the maximum amount of consideration that the Bank could be required to repay.

Where continuing involvement takes the form of a written and/or purchased option (including a cash-settled option or similar provision) on the transferred asset, the extent of the Bank's continuing involvement is the amount of the transferred asset that the Bank may repurchase, except that in the case of a written put option (including a cash-settled option or similar provision) on an asset measured at fair value, the extent of the Bank's continuing involvement is limited to the lower of the fair value of the transferred asset and the option exercise price.

Financial liabilities

A financial liability is derecognised when the obligation under the liability is discharged or cancelled or expires.

Where an existing financial liability is replaced by another from the same lender on substantially different terms, or the terms of an existing liability are substantially modified, such an exchange or modification is treated as a derecognition of the original liability and the recognition of a new liability, and the difference in the respective carrying amounts is recognised in the statement of income.

4.9 Repurchase and reverse repurchase agreements

Sale and repurchase agreements ("repos") are treated as secured financing transactions. Securities sold under sale and repurchase agreements are retained in the balance sheet and, in case the transferee has the right by contract or custom to sell or repledge them, reclassified as securities pledged under sale and repurchase agreements and faced as the separate balance sheet item. The corresponding liability is presented within amounts due to financial institutions or customers. Securities purchased under agreements to resell ("reverse repo") are recorded as amounts due from other financial institutions or loans and advances to customers as appropriate and are not recognized on the balance sheet. The difference between sale and repurchase price is treated as interest and accrued over the life of repo agreements using the effective yield method.

4.10 Securities lending and borrowing

Securities lending and borrowing transactions are usually collateralised by securities or cash. The transfer of the securities to counterparties is only reflected on the balance sheet if the risks and rewards of ownership are also transferred. Cash advanced or received as collateral is recorded as an asset or liability.

Securities borrowed are not recognized on the balance sheet, unless they are sold to third parties, in which case the obligation to return the securities is recorded as a trading liability and measured at fair value with any gains or losses included in “Net trading income”.

4.11 Leases

Operating - Bank as lessee

Leases of assets under which the risks and rewards of ownership are effectively retained by the lessor are classified as operating leases. Lease payments under an operating lease are recognised as expenses on a straight-line basis over the lease term and included into other operating expenses.

4.12 Property, plant and equipment

Property, plant and equipment (“PPE”) are recorded at historical cost less accumulated depreciation. The Bank’s buildings are stated at fair value less accumulated depreciation. If the recoverable value of PPE is lower than its carrying amount, due to circumstances not considered to be temporary, the respective asset is written down to its recoverable value.

Depreciation is calculated using the straight-line method based on the estimated useful life of the asset. The following depreciation rates have been applied:

	Useful life (years)	Rate (%)
Buildings	20	5
Computers	1	100
Vehicles	5	20
Other fixed assets	5	20

Leasehold improvements are capitalized and depreciated over the shorter of the lease term and their useful lives on a straight-line basis. Assets under the course of construction are not depreciated.

Repairs and maintenance are charged to the income statement during the period in which they are incurred. The cost of major renovations is included in the carrying amount of the asset when it is probable that future economic benefits in excess of the originally assessed standard of performance of the existing asset will flow to the Bank. Major renovations are depreciated over the remaining useful life of the related asset.

Gains and losses on disposals are determined by comparing proceeds with carrying amount and are included in operating profit.

Any revaluation surplus is credited to the revaluation reserve for property and equipment included in the revaluation reserve for property and equipment in equity section of the balance sheet, except to the extent that it reverses a revaluation decrease of the same asset previously recognised in the

statement of income, in which case the increase is recognised in the statement of income. A revaluation deficit is recognised in the statement of income, except that a deficit directly offsetting a previous surplus on the same asset is directly offset against the surplus in the revaluation reserve for property and equipment.

When revalued assets are sold, the amounts attributed to disposed item of assets and included in the revaluation reserve are transferred to retained earnings.

4.13 Intangible assets

Intangible assets include computer software, licences and other.

Intangible assets acquired separately are measured on initial recognition at cost. Following initial recognition, intangible assets are carried at cost less any accumulated amortisation and any accumulated impairment losses. The useful lives of intangible assets are assessed to be either finite or indefinite. Intangible assets with finite lives are amortised over the useful economic lives of 10 years and assessed for impairment whenever there is an indication that the intangible asset may be impaired. Amortisation periods and methods for intangible assets with finite useful lives are reviewed at least at each financial year-end.

Intangible assets with indefinite useful lives are not amortised, but tested for impairment annually either individually or at the cash-generating unit level. The useful life of an intangible asset with an indefinite life is reviewed annually to determine whether indefinite life assessment continues to be supportable.

The goodwill generated from purchases represents the part of the purchase value that exceeds the fair value of the purchased net definable assets. The goodwill is not amortised, but tested for impairment at least once a year.

4.14 Assets held for sale

A non-current asset is classified as held for sale if it is highly probable that the asset's carrying amount will be recovered through a sale transaction rather than through continuing use. Such sale transaction shall be principally completed within one year from the date of classification of an asset as held for sale.

Assets held for sale are measured at the lower of its carrying amount and fair value less costs to sell. If the fair value less costs to sell of an asset held for sale is lower than its carrying amount, an impairment loss is recognized in the income statement as loss from assets held for sale. Any subsequent increase in an asset's fair value less costs to sell is recognized to the extent of the cumulative impairment loss that was previously recognized in relation to that specific asset.

4.15 Grants

Grants relating to the assets are included in other liabilities and are credited to the income statement on a straight line basis over the expected lives of the related assets.

4.16 Borrowings

Borrowings, which include amounts due to the Government, amounts due to financial institutions, amounts due to customers, are initially recognised at the fair value of the consideration received less directly attributable transaction costs. After initial recognition, borrowings are subsequently measured at amortised cost using the effective interest method. Gains and losses are recognised in

the statement of income when the liabilities are derecognised as well as through the amortisation process.

4.17 Pensions

The Bank does not have any pension arrangements separate from the State pension system of the Republic of Armenia, which requires current contributions by the employer calculated as a percentage of current gross salary payments; such expense is charged in the period the related salaries are earned.

4.18 Financial guarantees

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, in “Other liabilities”, being the premium received. Subsequently to initial recognition, the Bank’s liability under each guarantee is measured at the higher of the amortised premium and the best estimate of expenditure required to settle any financial obligation arising as a result of the guarantee.

4.19 Provisions

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

4.20 Share capital

Share capital

Ordinary shares are classified as equity. External costs directly attributable to the issue of new shares, other than on a business combination, are shown as a deduction from the proceeds in equity. Any excess of the fair value of consideration received over the par value of shares issued is recognised as additional paid-in capital.

Dividends

Dividends are recognised as a liability and deducted from equity at the balance sheet date only if they are declared before or on the balance sheet date. Dividends are disclosed when they are proposed before the balance sheet date or proposed or declared after the balance sheet date but before the financial statements are authorised for issue.

4.21 Offsetting

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

5 Critical accounting estimates and judgements

The preparation of financial statements in conformity with IFRS requires management to make judgments, estimates and assumptions that affect the application of policies and the reported amounts of assets and liabilities, income and expense. The estimates and associated assumptions are based on historical experience and various other factors that are believed to be reasonable under the circumstances, the results of which form the basis of making the judgements about carrying values

of assets and liabilities that are not readily apparent from other sources. Although these estimates are based on management's best knowledge of current events and actions, actual results ultimately may differ from these estimates.

The most significant areas of judgements and estimates with regards to those financial statements are presented below:

Classification of investment securities

Securities owned by the Bank comprise, securities issued by the Central Bank of Armenia, Armenian state and corporate bonds and corporate shares. Upon initial recognition, the Bank designates securities as financial assets with recognition of changes in fair value through profit or loss, held to maturity financial assets or available-for-sale financial assets recognition of changes in fair value through equity.

Related party transactions

In the normal course of business the Bank enters into transactions with its related parties. These transactions are priced predominantly at market rates. Judgement is applied in determining if transactions are priced at market or non-market interest rates, where there is no active market for such transactions. The basis for judgement is pricing for similar types of transactions with unrelated parties and effective interest rate analysis.

Allowance for impairment of loans and receivables

The Bank reviews its problem loans and advances at each reporting date to assess whether an allowance for impairment should be recorded in the income statement. In particular, judgement by management is required in the estimation of the amount and timing of future cash flows when determining the level of allowance required. Such estimates are based on assumptions about a number of factors and actual results may differ, resulting in future changes to the allowance.

In addition to specific allowances against individually significant loans and advances, the Bank also makes a collective impairment allowance against exposures which, although not specifically identified as requiring a specific allowance, have a greater risk of default than when originally granted. This take into consideration factors such as any deterioration in country risk, industry, and technological obsolescence, as well as identified structural weaknesses or deterioration in cash flows.

Tax legislation

Armenian tax legislation is subject to varying interpretations. Refer to Note 25.

Impairment of available-for-sale equity investments

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

6 Interest and similar income and expense

In thousand Armenian drams	2007	2006
Loans and advances to customers	7,169,871	4,238,578
Debt investment securities available-for-sale	254,027	139,694
Amounts due from other financial institutions	351,419	296,681
Reverse repurchase transactions	13,562	22,269
Other interest income	16,583	194
Interest accrued on impaired financial assets	393,909	46,158
Total interest and similar income	8,199,371	4,743,574

In thousand Armenian drams	2007	2006
Amounts due to customers	1,871,808	1,271,943
Amounts due to financial institutions	277,349	27,758
Repurchase transactions	92,929	1,164
Total interest and similar expense	2,242,086	1,300,865

7 Fee and commission income and expense

In thousand Armenian drams	2007	2006
Cash collection	54,794	29,563
Wire transfer fees	665,779	504,237
Plastic cards operations	138,826	79,326
Service fee for account maintenance of Municipal and State budgets	47,648	39,440
Guarantees and letters of credit	113,635	72,217
Encashment	1,065,640	1,010,467
Other fees and commissions	138,300	247,501
Total fee and commission income	2,224,622	1,982,751

8 Other income

In thousand Armenian drams	2007	2006
Income from sale of fixed assets	1,486	364
Fines and penalties received	31,653	20,626
Other income	73,703	48,483
Total other income	106,842	69,473

Other income includes recognized income of AMD 456 thousand from lands granted by the State, calculated on the straight-line basis during the useful live of the buildings constructed on the land.

9 Impairment charge/(reversal) of impairment for credit losses

In thousand Armenian drams	2007	2006
Amounts due from other financial institutions (Note 14)	-	(33,087)
Loans and advances to customers (Note 15)	287,733	289,962
Guarantees and other credit related commitments (Note 23)	4,160	10,470
Other assets (Note 19)	(25,040)	30,052
Total impairment charge of impairment for credit losses	266,853	297,397

10 Staff costs

In thousand Armenian drams	2007	2006
Wages and salaries	2,238,550	1,883,166
Social security contributions	246,562	220,310
Total staff costs	2,485,112	2,103,476

11 Other expenses

In thousand Armenian drams	2007	2006
Fixed assets maintenance	89,033	70,941
Advertising costs	66,780	97,909
Business trip expenses	39,703	38,512
Communications	133,183	118,140
Operating lease	111,491	127,248
Taxes, other than income tax, duties	156,355	139,797
Consulting and other services	251,036	176,508
Security	152,187	121,359
Loss on impairment of PPE	7,625	22,875
Loss on disposal of PPE	4,844	-
Representative expenses	31,160	19,771
Office supplies	48,299	28,802
Penalties paid	4,373	4,165
Foreign currency translation net losses of non-trading assets	28,672	70,120
Other expenses	533,096	466,495
Total other expense	1,657,837	1,502,642

12 Income tax expense

In thousand Armenian drams	2007	2006
Current tax expense	1,035,290	573,769
Deferred tax	(7,071)	(19,429)
Total income tax expense	1,028,219	554,340

The corporate income tax within the Republic of Armenia is levied at the rate of 20% (2006: 20%). Differences between IFRS and RA statutory tax regulations give rise to certain temporary differences between the carrying value of certain assets and liabilities for financial reporting purposes and for profit tax purposes. Deferred income tax is calculated using the principal tax rate of 20%.

Numerical reconciliation between the tax expenses and accounting profit is provided below:

In thousand Armenian drams	2007	Effective rate (%)	2006	Effective rate (%)
Profit before tax	5,155,341	-	2,655,060	-
Income tax at the rate of 20%	1,031,068	20	531,012	20
Non-taxable income	(22,611)	(0.4)	(13,013)	(0.5)
Non-deductible expenses	14,028	0.3	22,317	0.9
Foreign exchange negative	5,734	0.1	14,024	0.5
Income tax expense	1,028,219	20	554,340	20.9

Deferred tax calculation in respect of temporary differences:

In thousand Armenian drams	2006	Recognized in income statement	Recognized in equity	2007
Accrued expenses and other liabilities	17,637	6,375	-	24,012
Total deferred tax assets	17,637	6,375	-	24,012
Revaluation of the PPE	(289,554)	16,055	-	(273,499)
Allowances for loan commitments	(3,590)	(5,081)	-	(8,671)
Allowances for impairment for loans and other assets	-	(10,278)	-	(10,278)
Fair value measurement of the securities	(17,459)	-	(1,471)	(18,930)
Total deferred tax liability	(310,603)	696	(1,471)	(311,378)
Net deferred tax liability	(292,966)	7,071	(1,471)	(287,366)

In thousand Armenian drams	2005	Recognized in income statement	Recognized in equity	2006
Accrued expenses and other liabilities	13,674	3,963	-	17,637
Total deferred tax assets	13,674	3,963	-	17,637
Revaluation of the PPE	(305,593)	-	16,039	(289,554)
Adjustment of goodwill	(3,050)	3,050	-	-
Allowances for loan commitments	(11,256)	7,666	-	(3,590)
Accrued income	(4,750)	4,750	-	-
Fair value measurement of the securities	(21,052)		3,593	(17,459)
Total deferred tax liability	(345,701)	15,466	19,632	(310,603)
Net deferred tax liability	(332,027)	19,429	19,632	(292,966)

13 Cash, cash equivalents and balances with CBA

In thousand Armenian drams	2007	2006
Cash on hand	4,758,153	4,392,285
Other money market placements	48,943	12,813
Correspondent account with the CBA	8,677,286	7,794,037
Included in cash and cash equivalents	13,484,382	12,199,135
Deposited funds with the CBA	550,119	327,999
Total cash and balances with the CBA	14,034,501	12,527,134
Cash and balances with the CBA, included in cash flow	13,484,382	12,199,135
Placements with other banks (note 14)	9,192,113	12,245,145
Total cash and cash equivalents	22,676,495	24,444,280

As at 31 December 2007 correspondent account with Central Bank of Armenia represents the obligatory minimum reserve deposits with the CBA, which is computed at 8% of certain obligations of the Bank denominated in Armenian drams and 12% of certain obligations of the Bank, denominated in foreign currency and amounts to AMD 6,761,421 thousand (2006: AMD 4,574,817 thousand). There are no restrictions on the withdrawal of funds from the CBA, however, if minimum average requirement is not met, the Bank could be subject to penalties. Cash on hand, other money market placements, correspondent account, deposited funds with CBA and mandatory reserve deposits are non-interest bearing.

Deposited funds with CBA include a guaranteed deposit for settlements via ArCa payment system.

14 Amounts due from other financial institutions

In thousand Armenian drams	2007	2006
Correspondent accounts with financial institutions	4,626,692	4,963,394
Deposits for less than 90 days	4,565,421	7,281,751
Included in cash and cash equivalents	9,192,113	12,245,145
Loans and reverse repurchase agreements	501,278	377,638
Deposited funds with other financial institutions	25,739	15,752
Other amounts	329,376	-
	856,393	393,390
Total amounts due from other financial institutions	10,048,506	12,638,535

Included in deposited funds with other financial institutions are guarantee deposits placed by the Bank in “HSBC Bank London” for its operations through Master Card system.

As at 31 December 2007 the amounts due from other financial institutions in amounts of AMD 8,271,230 thousand (87%) (2006: AMD 4,168,699 thousand (34%)) were due from five banks, which represent significant concentration.

Fair value of assets pledged and carrying value of loans under reverse repurchase agreements as of 31 December are presented as follows:

In thousand Armenian drams	2007		2006	
	Fair value of collateral	Carrying value of loans	Fair value of collateral	Carrying value of loans
Securities issued by the CBA	501,204	500,935	-	-
Total assets pledged and loans under reverse repurchase agreements	501,204	500,935	-	-

During 2007, the Bank placed with and simultaneously received short-term funds from Armenian banks in various currencies (these amounts are included in other amounts). As of December 31, 2007, the Bank placed a deposit of USD 1,000 thousand, including the equivalent of AMD 708 thousand interests receivable, which is related to deposit received from the same bank (See Note 20).

The movement in allowance for impairment losses on amounts due from other financial institutions was as follows:

In thousand Armenian drams	Total
At January 1, 2006	33,087
Reversal (note 9)	(33,087)
At December 31, 2006	<u>-</u>
At December 31, 2007	<u><u>-</u></u>

15 Loans and advances to customers

In thousand Armenian drams	2007	2006
Loans to customers	54,872,808	23,729,251
Overdrafts	397,072	100,755
	55,269,880	23,830,006
Less allowance for loan impairment	(773,262)	(424,713)
Total loans and advances to customers	<u>54,496,618</u>	<u>23,405,293</u>

As of 31 December 2007 accrued interest income included in loans and advances to customers amounted to AMD 374,940 thousand (2006: AMD230,697 thousand).

As of December 31, 2007, the Bank had a concentration of loans represented by AMD 16,420,604 thousand due from the ten largest third party entities and parties related with them (29.7 % of gross loan portfolio) (2006: AMD 6,186,743 thousand or 26 %). An allowance of AMD 38,712 thousand (2006: AMD 181,387 thousand) was made against these loans.

Reconciliation of allowance account for losses on loans and advances by class is as follows:

In thousand Armenian drams					2007
	State owned enterprises	Privately held companies	Individuals	Sole proprietors	Total
At 1 January 2007	-	295,471	117,298	11,944	424,713
Charge for the year (note 9)	3,081	164,478	114,687	5,487	287,733
Amounts written off	-	(39,406)	(71,447)	-	(110,853)
Recoveries	-	100,112	71,557	-	171,669
At 31 December 2007	<u>3,081</u>	<u>520,655</u>	<u>232,095</u>	<u>17,431</u>	<u>773,262</u>
Individual impairment	-	255,781	-	-	255,781
Collective impairment	3,081	264,874	232,095	17,431	517,481
	<u>3,081</u>	<u>520,655</u>	<u>232,095</u>	<u>17,431</u>	<u>773,262</u>
Gross amount of loans individually determined to be impaired, before deducting any individually assessed impairment allowance	-	3,109,047	-	-	3,109,047

In thousand Armenian drams					2006
	State owned enterprises	Privately held companies	Individuals	Sole proprietors	Total
At 1 January 2006	-	117,974	168,320	4,789	291,083
Charge for the year (9)	-	214,053	68,217	7,692	289,962
Amounts written off	-	(94,011)	(489,481)	(1,017)	(584,509)
Recoveries	-	57,455	370,242	480	428,177
At 31 December 2006	<u>-</u>	<u>295,471</u>	<u>117,298</u>	<u>11,944</u>	<u>424,713</u>
Individual impairment	-	152,032	654	6,229	158,915
Collective impairment	-	143,439	116,644	5,715	265,798
	<u>-</u>	<u>295,471</u>	<u>117,298</u>	<u>11,944</u>	<u>424,713</u>
Gross amount of loans individually determined to be impaired, before deducting any individually assessed impairment allowance	-	1,886,900	6,543	62,291	1,955,734

Loans and advances by customer profile may be specified as follows:

In thousand Armenian drams	2007	2006
State owned enterprises	308,138	155,364
Privately held companies	29,596,390	13,638,124
Individuals	23,209,489	9,126,732
Sole proprietors	1,743,125	675,939
Non-commercial institutions	-	3,150
Accrued interest	412,738	230,697
	<u>55,269,880</u>	<u>23,830,006</u>
Less allowance for loan impairment	(773,262)	(424,713)
Total loans and advances to customers	<u>54,496,618</u>	<u>23,405,293</u>

Loans to individuals comprise the following products:

In thousand Armenian drams	2007	2006
Mortgage loans	1,361,410	15,822
Consumer loans	14,057,476	4,058,857
Car loans	6,512,139	1,697,032
Other	1,278,464	3,355,021
Total loans and advances to individuals (gross)	<u>23,209,489</u>	<u>9,126,732</u>

At 31 December 2006 and 2007 the estimated fair value of loans and advances to customers approximates its carrying value. Refer to Note 27.

Credit, currency, liquidity and interest rate analyses of loans and advances to customers are disclosed in Note 29. The information on related party balances is disclosed in Note 26.

16 Available-for-sale investment securities

In thousand Armenian drams	2007	2006
	Available-for-sale	Available-for-sale
Unquoted investments		
Equity securities	1,210	1,332
Shares of Armenian companies	16,003	12,008
Securities issued by the Ministry of Finance of Armenia	4,330,762	3,974,982
Securities issued by the CBA	2,949,432	10,676,683
Corporate bonds	50,013	-
Total investments	<u>7,347,420</u>	<u>14,665,005</u>

All debt securities have fixed coupons.

All unquoted available-for-sale investment securities are recorded at fair value using a valuation technique, which is based on current market rates, as discount rate of the future cash flows of the financial instruments.

Available for sale securities by interest rates and maturity date comprise:

In thousand Armenian drams	2007		2006	
	%	Maturity	%	Maturity
Securities issued the Ministry of Finance of Armenia	4.2-9.4	2008-2020	4.2-9.4	2007-2020
Securities issued by the CBA	5.9-7.4	2008	4.5-6.1	2007
Corporate bonds	9	2008	-	-

17 Property, plant and equipment

In thousand Armenian drams	Land and buildings	Machinery and equipment	Vehicles	Other fixed assets	Assets under construction	Leasehold improvements	Total
COST							
Cost/Revalued amount at January 1, 2006	4,423,555	569,372	140,260	287,984	132,979	103,825	5,657,975
Additions	248,627	219,988	26,007	62,800	457,185	4,852	1,019,459
Disposals	(18,844)	(7,283)	(1,974)	(2,077)	(29,929)	(36,263)	(96,370)
Reclassifications	463	-	-	1,418	10,086	(11,967)	-
At December 31, 2006	4,653,801	782,077	164,293	350,125	570,321	60,447	6,581,064
Additions	17,340	227,563	56,655	127,964	1,123,248	20,276	1,573,046
Disposals	-	(22,792)	(21,045)	(4,459)	-	-	(48,296)
Reclassifications	159,743	-	-	-	(159,743)	-	-
At December 31, 2007	4,830,884	986,848	199,903	473,630	1,533,826	80,723	8,105,814
DEPRECIATION							
At January 1, 2006	301,823	332,827	27,993	118,450	-	17,587	798,680
Depreciation charge	221,120	155,129	29,448	59,006	-	11,400	476,103
Disposals	(2,840)	(6,979)	(1,667)	(2,077)	-	(10,625)	(24,188)
Reclassifications	-	-	-	163	-	(163)	-
At December 31, 2006	520,103	480,977	55,774	175,542	-	18,199	1,250,595
Depreciation charge	226,623	210,926	38,326	71,246	-	9,552	556,673
Disposals	-	(22,792)	(9,621)	(2,482)	-	-	(34,895)
At December 31, 2007	746,726	669,111	84,479	244,306	-	27,751	1,772,373
CARRYING VALUE							
At December 31, 2007	4,084,158	317,737	115,424	229,324	1,533,826	52,972	6,333,441
At December 31, 2006	4,133,698	301,100	108,519	174,583	570,321	42,248	5,330,469

Revaluation of assets

Buildings owned by the Bank were evaluated by an independent appraiser in 2005 using a combination of the market, income and cost methods resulting in a revaluation of AMD 1,527,459

thousand. Management have based their estimate of the fair value of the buildings on the results of the independent appraisal.

The management believes that at 31 December 2007 the fair value of the buildings does not differ significantly from their revalued amounts.

The net book value of buildings that would have been recognised under the historic cost method is AMD 2,569,576 thousand, as at 31 December 2007 (2006: AMD 2,550,395 thousand).

Fully depreciated items

As at 31 December 2007 fixed assets included fully depreciated and amortized assets in amount of AMD 578,905 thousand (2006: AMD 411,173 thousand).

Fixed assets in the phase of installation

As at 31 December 2007 fixed assets included assets in the phase of installation in amount of AMD 198,057 thousand (2006: AMD 178,132 thousand), which are not amortized and are classified in accordance with their type.

18 Intangible assets

In thousand Armenian drams	Licenses	Acquired software licenses	Goodwill	Total
COST				
At January 1, 2006	27,008	6,449	75,528	108,985
Additions	10,800	22,080	-	32,880
At December 31, 2006	37,808	28,529	75,528	141,865
Additions	-	8,100	-	8,100
Adjustment	(2,447)	-	-	(2,447)
At December 31, 2007	35,361	36,629	75,528	147,518
AMORTISATION				
At January 1, 2006	3,643	1,629	-	5,272
Amortisation charge	3,601	1,337	-	4,938
Impairment	-	-	22,875	22,875
At December 31, 2006	7,244	2,966	22,875	33,085
Amortisation charge	2,965	3,602	-	6,567
Impairment	-	-	7,625	7,625
At December 31, 2007	10,209	6,568	30,500	47,277
CARRYING VALUE				
At December 31, 2007	25,152	30,061	45,028	100,241
At December 31, 2006	30,564	25,563	52,653	108,780

19 Other assets

In thousand Armenian drams	2007	2006
Prepayments and other debtors	537,687	190,744
Unamortized insurance premium	20,102	-
Settlements with employees	1,453	-
Amounts receivable	25,579	79,707
Other assets	148,612	99,025
	733,433	369,476
Less allowance for impairment	(1,381)	(3,301)
	732,052	366,175
Prepaid income taxes	944	1,263
Materials	193,213	104,564
Other	3,838	3,838
Total other assets	930,047	475,840

Reconciliation of allowance account for losses on other assets is as follows:

In thousand Armenian drams	Total
At January 1, 2006	3,379
Charge for the year (note 9)	30,052
Amounts written off	(64,557)
Recoveries	34,427
At December 31, 2006	3,301
Reversal (note 9)	(25,040)
Amounts written off	(2,110)
Recoveries	25,230
At December 31, 2007	1,381

20 Amounts due to financial institutions

In thousand Armenian drams	2007	2006
Correspondent accounts of other banks	271,607	326,263
Current accounts of other financial institutions	901,900	523,103
Loans and deposits from financial institutions	6,209,956	654,493
Loans from international financial institutions	4,576,234	-
Other amounts	332,530	-
Total amounts due to financial institutions	12,292,227	1,503,859

Loans from international financial institutions include the loan from International Finance Corporation.

All deposits from financial institutions have fixed interest rates.

Loans received from international and other financial institutions have variable interest rates.

During 2007, the Bank placed with and received short-term funds from Armenian banks in various currencies (these amounts are included in other amounts). As of December 31, 2007, the Bank received 332,530 AMD thousand as deposit, which relate to deposit granted to the same bank in USD (See Note 14)

The Bank has not had any defaults of principal, interest or other breaches with respect to its liabilities during the period (2006: nil).

21 Amounts due to customers

In thousand Armenian drams	2007	2006
Government of the RA		
Current/Settlement accounts	1,942	2,327
Time deposits	1,372,048	1,516,327
	1,373,990	1,518,654
Corporate customers		
Current/Settlement accounts	28,582,674	23,368,095
Time deposits	12,416,750	17,903,251
	40,999,424	41,271,346
Retail customers		
Current/Demand accounts	3,859,119	3,215,953
Time deposits	14,850,359	9,876,659
	18,709,478	13,092,612
Total amounts due to customers	61,082,892	55,882,612

As at 31 December 2007 included in amounts due to RA government are deposits from World Bank “Businesses Development Program”, “Urban Heating Program”, “Agriculture Improvement Support Program”, and from the International Fund for Agricultural Development “Rural Areas Economic Development Programme” and related to them accrued interest.

Deposits carry fixed interest rates.

As at 31 December 2007 included in amounts due to customers are deposits amounting to AMD 32,702 thousand (2006: AMD 109,428 thousand), AMD 326,041 thousand (2006: AMD 165,039 thousand), held as security against letters of credit and guarantees issued correspondingly. The fair value of those deposits approximates the carrying amount.

At 31 December 2007 the aggregate balance of top ten customers of the Bank (including relating parties, see Note 26) amounts to AMD 30,191,104 thousand (2006: AMD 23,251,434 thousand) or 49.4 % of total customer accounts (2006: 43%)

22 Other liabilities

In thousand Armenian drams	2007	2006
Accounts payables	92,564	40,086
Tax payable, other than income tax	127,307	52,080
Revenues of future periods	34,041	77,776
Grants related to assets	3,244	-
Due to personnel	83,026	51,392
Other	6	3,809
Total other liabilities	340,188	225,143

23 Other provisions

The movement in other provisions was as follows:

In thousand Armenian drams	2007	2006
At January 1	10,470	-
Arising during the year	4,160	10,470
Utilized	(10,470)	-
At December 31	4,160	10,470

Included within other provisions are:

Provisions of AMD 4,160 thousand have been made in respect of costs arising from guarantees issued by the Bank. 2006: a provision of AMD 10,470 thousand have been made for the reimbursement of costs arising from the collaterals.

24 Equity

As at 31 December 2007 the Bank's registered and paid-in share capital was AMD 13,802,404 thousand. In accordance with the Bank's statutes, the share capital consists of 179,252 ordinary shares, all of which have a par value of AMD 77,000 each.

The respective shareholdings as at 31 December 2007 and 2006 may be specified as follows:

In thousand Armenian drams	2007		2006	
	Paid-in share capital	% of total paid-in capital	Paid-in share capital	% of total paid-in capital
Business Investment Center Ltd	7,168,084	51.9%	4,420,790	59.8
International Business Center CJSC	2,389,387	17.3%	1,473,596	19.9
Rasco Armenia CJSC	2,389,387	17.3%	1,473,596	19.9
International Finance Corporation	1,380,302	10.0%	-	-
Andreasyan Aram	238,854	1.7%	11,785	0.2
Safaryan Karen	51,590	0.4%	11,785	0.2
Mkrtumyan Rudik	36,960	0.3%	-	-
"Region" investment financial corporation CSJC	36,960	0.3%	-	-
Zaqaryan Khachik	36,960	0.3%	-	-
Karapetyan Karen	36,960	0.3%	-	-
Sahakyan Manvel	18,480	0.1%	-	-
Pakhomov Alexandr	18,480	0.1%	-	-
	13,802,404	100	7,391,552	100

As at 31 December 2007, the Bank did not possess any of its own shares.

The holders of ordinary shares are entitled to receive dividends as declared and are entitled to one vote per share at annual and general meetings of the Bank.

In 2007 the shareholders of the Bank increased its share capital by AMD 6,410,852 thousand (2006: AMD 4,371,528 thousand).

The share capital of the Bank was contributed by the shareholders in Armenian Drams and they are entitled to dividends and any capital distribution in Armenian Drams

At the Shareholders' Meeting in April 2007, the Bank declared dividends in respect of the year ended December 31, 2006, totaling AMD 1,968,805 thousand (AMD 15,370 thousand per share).

At the Shareholders' Meeting in November 2007, the Bank declared interim dividends in respect of the financial performance for the first nine months of the year 2007, totaling AMD 2,742,542 thousand on ordinary shares (AMD 17,000 thousand per share).

Distributable among shareholders reserves equal the amount of retained earnings, determined according to the Armenian legislation. Non-distributable reserves are represented by a reserve fund, which is created as required by the statutory regulations, in respect of general banking risks, including future losses and other unforeseen risks or contingencies. The reserve has been created in accordance with the Bank's statutes that provide for the creation of a reserve for these purposes of not less than 15% of the Bank's share capital reported in statutory books.

25 Contingent liabilities and commitments

Tax and legal matters

The taxation system in Armenia is characterized by frequently changing legislation, which is often unclear, contradictory and subject to interpretation. Often, differing interpretations exist among various taxation authorities and jurisdictions.

Management believes that the Bank has complied with all regulations and has completely settled all its tax liabilities.

As of 31 December 2007 there were no legal actions and complaints taken against the Bank.

In 2006 the Bank has made a provision of AMD 10,470 thousand for the reimbursement of the costs from the return of collaterals that has been implemented during the year 2007.

Loan commitment, guarantee and other financial facilities

In the normal course of business, the Bank is a party to financial instruments with off-balance sheet risk in order to meet the needs of its customers. These instruments, involving varying degrees of credit risk, are not reflected in the balance sheet.

As of 31 December the nominal or contract amounts were:

In thousand Armenian drams	2007	2006
Undrawn loan commitments	3,311,000	4,270,083
Unused credit cards	805,256	302,124
Unused overdrafts	846,546	448,073
Letters of credit	1,125,786	104,357
Guarantees	5,282,290	2,180,138
Total credit related commitments	11,370,878	7,304,775

Operating lease commitments – Bank as a lessee

In the normal course of business the Bank enters into commercial lease agreements for office equipment, central office and branch facilities.

The future aggregate minimum lease payments under non-cancellable operating leases are as follows:

In thousand Armenian drams	2007	2006
Not later than 1 year	286	8,946
Later than 1 year and not later than 5 years	89,902	263,594
Later than 5 years	142,386	-
Total operating lease commitments	232,574	272,540

Capital commitments

The Bank had capital commitments totalling AMD 453,440 thousand as at 31 December 2007. The Bank's Management has already allocated the necessary resources in respect of this commitment. The Bank's Management believes that future net revenues and funding will be sufficient to cover this and any similar such commitments.

Insurance

Starting from 2005 the Bank is member of the obligatory deposit insurance system. The system operates under the Armenian laws and regulations and is governed by the Law on Guarantee of Physical Persons Deposits. Insurance covers Bank's liabilities to individual depositors for the

amount up to AMD 2,000 thousand (up to AMD 1,000 thousand for deposits in foreign currency) for each individual in case of business failure and revocation of the banking license.

26 Transactions with related parties

In accordance with IAS 24 *Related Party Disclosures*, parties are considered to be related if one party has ability to control the other party or exercise significant influence over the other party in making financial or operational decisions. For the purpose of the present financial statements, related parties include shareholders, members of Bank's Management as well as other persons and enterprises related with and controlled by them respectively.

The Bank's parent is the Business Investment Center Ltd. The ultimate controlling party of the Bank is Chairman of the Board of the Bank - K. Safaryan, who is a related party with other shareholders of the Bank, as well as with the shareholders of the parent company.

A number of banking transactions are entered into with related parties in the normal course of business. These include loans, deposits and foreign currency transactions. These transactions were carried out on commercial terms and at market rates.

The volumes of related party transactions, outstanding balances at the year end, and related expense and income for the year are as follows:

In thousand Armenian drams	2007		2006	
	Shareholders	Key management personnel	Shareholders	Key management personnel
<i>Loans</i>				
Loans outstanding at January 1, gross	3,635	61,541	-	95,780
Loans issued during the year	1,311,019	232,315	4,158	1,411,829
Loan repayments during the year	(1,215,977)	(293,623)	(523)	(1,446,068)
Loans outstanding at December 31, gross	98,677	233	3,635	61,541
Less: allowance for loan impairment	(987)	(2)	(36)	(604)
Loans outstanding at December 31	97,690	231	3,599	60,937
Interest income on loans	22,440	1,764	57	51,380
<i>Deposits</i>				
Deposits at January 1	266,356	14,002,175	39,899	522,108
Deposits received during the year	262,596,341	3,950,922	35,174,297	220,527,009
Deposits repaid during the year	(247,143,294)	(17,317,067)	(34,947,840)	(207,046,942)
Deposits at December 31	15,719,403	636,030	266,356	14,002,175
Interest expense on deposits	111,028	3,762	2,973	49,665
<i>Amounts due to other financial institutions</i>				
At January 1	-	-	-	-
Increase	104,304,990	-	-	-
Decrease	(94,181,130)	-	-	-
At December 31	10,123,860	-	-	-
Interest Expense	74,688	-	-	-

In thousand Armenian drams	2007		2006	
	Shareholders	Key management personnel	Shareholders	Key management personnel
Commitments and guarantees				
At January 1	-	24,130	-	-
Commitments and guarantees issued	3,000	-	-	59,386
Commitments and guarantees received	(3,000)	(24,130)	-	(35,256)
At December 31	-	-	-	24,130
Income on issued guarantees	30	724	-	431
Other transactions				
Sale of buildings	-	-	36,000	-
Purchase of fixed assets	-	-	589	-
Purchase of inventory	3,496	-	2,777	-
Capital construction	346,674	-	193,276	-
Other expenses				
Consulting and other services	359,439	-	200,899	-
Rent expense	15,456	-	9,685	-

The loans issued to directors and other key management personnel are repayable over one year and have interest rates of 16% (2006: 16%). The loans advanced to the directors are collateralised by their salaries.

Compensation of key management personnel was comprised of the following:

In thousand Armenian drams	2007	2006
Salaries and other short-term benefits	1,099,575	861,283
Social security costs	76,855	24,764
Total key management compensation	1,176,430	886,047

27 Fair value of financial instruments

Amounts due from and to financial institutions

For assets and liabilities maturing within one month, the carrying amount approximates fair value due to the relatively short-term maturity of these financial instruments. For the assets and liabilities maturing in over one month, the fair value was estimated as the present value of estimated future cash flows discounted at the appropriate year-end market rates.

Loans and advances to customers

The fair value of floating rate instruments is normally their carrying amount. The estimated fair value of fixed interest rate instruments is based on estimated future cash flows expected to be received discounted at current interest rates for new instruments with similar credit risk and

remaining maturity. Discount rates used depend on credit risk of the counterparty and ranged from 15.3% to 18.3% per annum.

28 Maturity analysis of assets and liabilities

The table below shows an analysis of assets and liabilities analyzed according to when they are expected to be recovered or settled. See Note 29.3 for the Bank's contractual undiscounted repayment obligations.

In thousand Armenian drams	2007							
	Demand and less than 1 month	From 1 to 3 months	From 3 to 12 months	Subtotal less than 12 months	From 1 to 5 years	More than 5 years	Subtotal over 12 months	Total
ASSETS								
Cash and balances with CBA	13,484,382	-	-	13,484,382	-	550,119	550,119	14,034,501
Amounts due from other financial institutions	10,022,767	-	-	10,022,767	-	25,739	25,739	10,048,506
Loans and advances to customers	4,342,834	7,609,145	22,748,537	34,700,516	18,966,641	829,461	19,796,102	54,496,618
Investments available for sale	993,627	2,077,927	927,836	3,999,390	2,341,111	1,006,919	3,348,030	7,347,420
	<u>28,843,610</u>	<u>9,687,072</u>	<u>23,676,373</u>	<u>62,207,055</u>	<u>21,307,752</u>	<u>2,412,238</u>	<u>23,719,990</u>	<u>85,927,045</u>
LIABILITIES								
Amounts due to financial institutions	1,506,041	5,359,887	311,611	7,177,539	3,213,314	1,901,374	5,114,688	12,292,227
Amounts due to customers	41,887,972	6,116,883	11,219,691	59,224,546	1,573,060	285,286	1,858,346	61,082,892
	<u>43,394,013</u>	<u>11,476,770</u>	<u>11,531,302</u>	<u>66,402,085</u>	<u>4,786,374</u>	<u>2,186,660</u>	<u>6,973,034</u>	<u>73,375,119</u>
Net position	<u>(14,550,403)</u>	<u>(1,789,698)</u>	<u>12,145,071</u>	<u>(4,195,030)</u>	<u>16,521,378</u>	<u>225,578</u>	<u>16,746,956</u>	<u>12,551,926</u>
Accumulated gap	<u>(14,550,403)</u>	<u>(16,340,101)</u>	<u>(4,195,030)</u>		<u>-12,326,348</u>	<u>12,551,926</u>		<u>-</u>

In thousand Armenian drams								2006
	Demand and less than 1 month	From 1 to 3 months	From 3 to 12 months	Subtotal less than 12 months	From 1 to 5 years	More than 5 years	Subtotal over 12 months	Total
ASSETS								
Cash and balances with CBA	12,199,135	-	-	12,199,135	-	327,999	327,999	12,527,134
Amounts due from other financial institutions	12,233,321	270,555	103,313	12,607,189	-	31,346	31,346	12,638,535
Loans and advances to customers	1,234,346	2,897,954	10,164,109	14,296,409	9,107,771	1,113	9,108,884	23,405,293
Investments available for sale	1,143,329	5,572,667	5,202,269	11,918,265	1,540,342	1,206,398	2,746,740	14,665,005
	26,810,131	8,741,176	15,469,691	51,020,998	10,648,113	1,566,856	12,214,969	63,235,967
LIABILITIES								
Amounts due to financial institutions	1,402,714	70,617	30,528	1,503,859	-	-	-	1,503,859
Amounts due to customers	40,674,418	4,098,489	8,492,006	53,264,913	2,617,565	134	2,617,699	55,882,612
	42,077,132	4,169,106	8,522,534	54,768,772	2,617,565	134	2,617,699	57,386,471
Net position	(15,267,001)	4,572,070	6,947,157	(3,747,774)	8,030,548	1,566,722	9,597,270	5,849,496
Accumulated gap	(15,267,001)	(10,694,931)	(3,747,774)		4,282,774	5,849,496		

29 Risk management

The Bank'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 Bank's aim is therefore to achieve an appropriate balance between risk and return and minimise potential adverse effects on the Bank's financial performance.

The Bank's risk management policies are designed to identify and analyse 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 Bank regularly reviews its risk management policies and systems to reflect changes in markets, products and emerging best practice.

Risk management is carried out by a Banking Risk Analysis Department under policies approved by the Board of Directors. The BRAD identifies, evaluates and hedges financial risks in close co-operation with the Bank's operating units. The Board provides written 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.

29.1 Credit risk

The Bank takes on exposure to credit risk, which is the risk that a counterparty will cause a financial loss for the Bank by failing to discharge an obligation. Credit risk is the most important risk for the Bank's business; management therefore carefully manages its exposure to credit risk. Credit

exposures arise principally in lending activities that lead to loans and advances, and investment activities that bring debt securities and other bills into the Bank's asset portfolio. There is also credit risk in off-balance sheet financial instruments, such as loan commitments. The credit risk management and control are centralised in Bank's BRAD and credit department reported to the Board of Directors and head of each business unit regularly.

29.1.1 Maximum exposure to credit risk without taking account of any collateral and other credit enhancements

The table below represents a worse case scenario of credit risk exposure to the Bank at 31 December 2007 and 2006, without taking account of any collateral held or other credit enhancements attached. For on-balance-sheet assets, the exposures set out above are based on net carrying amounts as reported in the balance sheet.

In thousand Armenian drams	Notes	Gross maximum exposure as of December 31, 2007	Gross maximum exposure as of December 31, 2006
Cash and balances with CBA	13	14,034,501	12,527,134
Amounts due from other financial institutions	14	10,048,506	12,638,535
Loans and advances to customers	15	54,496,618	23,405,293
Investments available for sale	16	7,347,420	14,665,005
Total		85,927,045	63,235,967
Credit related commitments	25	11,370,878	7,304,775
Total credit risk exposure		97,297,923	70,540,742

When financial instruments are recorded at fair value the amounts shown above represent the current credit risk exposure but not the maximum risk exposure that could arise in the future as a result of changes in values.

29.1.2 Risk concentrations of the maximum exposure to credit risk

Geographical sectors

The following table breaks down the Bank's main credit exposure at their carrying amounts, as categorized by geographical region as of 31 December.

In thousand Armenian drams	Armenia	OECD countries	Other non-OECD countries	Total
Cash and balances with CBA	14,034,501	-	-	14,034,501
Amounts due from other financial institutions	926,936	8,402,650	718,920	10,048,506
Loans and advances to customers	54,309,236	-	187,382	54,496,618
Investments available for sale	7,346,210	1,210	-	7,347,420
As at 31 December 2007	76,616,883	8,403,860	906,302	85,927,045
As at 31 December 2006	50,988,646	11,836,417	410,904	63,235,967

Assets have been classified based on the country in which the counterparty is located.

Industry sectors

The following table breaks down the Bank's main credit exposure at their carrying amounts, as categorized by the industry sectors of the counterparties as of 31 December.

In thousand Armenian drams	Financial institutions	Manufacturing	Agriculture	Construction	Energy	Commercial sector	Consumer sector	Service sector	Other	Total
Cash and balances with CBA	14,034,501	-	-	-	-	-	-	-	-	14,034,501
Amounts due from other financial institutions	10,048,506	-	-	-	-	-	-	-	-	10,048,506
Loans and advances to customers	-	13,502,317	1,918,979	4,944,426	1,180,277	5,982,085	20,614,254	2,945,453	3,408,827	54,496,618
Investments available for sale	7,296,197	-	-	-	-	50,013	-	-	1,210	7,347,420
As at 31 December 2007	31,379,204	13,502,317	1,918,979	4,944,426	1,180,277	6,032,098	20,614,254	2,945,453	3,410,037	85,927,045
As at 31 December 2006	39,829,342	5,216,764	766,765	3,209,851	684,744	3,313,935	8,793,054	1,136,652	284,860	63,235,967

29.1.3 Risk limit control and mitigation policies

The Bank manages, limits and controls concentrations of credit risk wherever they are identified – in particular, to individual counterparties and groups, and to industries and countries.

The Bank structures the levels of credit risk it undertakes by placing limits on the amount of risk accepted in relation to one borrower, or groups of borrowers, and to geographical and industry segments. Such risks are monitored on a revolving basis and subject to an annual or more frequent review, when considered necessary. Limits on the level of credit risk by product, industry sector and by country are approved quarterly by the Board of Directors.

The exposure to any one borrower including banks and financial organizations is further restricted by sub-limits covering on- and off-balance sheet exposures, and daily delivery risk limits in relation to trading items such as forward foreign exchange contracts. Actual exposures against limits are monitored daily.

Exposure to credit risk is also managed through regular analysis of the ability of borrowers and potential borrowers to meet interest and capital repayment obligations and by changing these lending limits where appropriate.

Some other specific control and mitigation measures are outlined below.

Collateral

The Bank employs a range of policies and practices to mitigate credit risk. The most traditional of these is the taking of security for funds advances, which is common practice. The Bank implements guidelines on the acceptability of specific classes of collateral or credit risk mitigation. The principal collateral types for loans and advances are:

- Mortgages over residential properties;
- Charges over business assets such as premises, inventory and accounts receivable;
- Charges over financial instruments such as debt securities and equities.

Longer-term finance and lending to corporate entities are generally secured; revolving individual credit facilities are generally unsecured. In addition, in order to minimise the credit loss the Bank will seek additional collateral from the counterparty as soon as impairment indicators are noticed for the relevant individual loans and advances.

Collateral held as security for financial assets other than loans and advances is determined by the nature of the instrument. Debt securities, treasury and other eligible bills are generally unsecured.

The analysis of loan portfolio by collateral is represented as follows:

In thousand Armenian drams	2007	2006
Loans collateralized by real estate	28,920,244	9,501,066
Loans collateralized by guarantees of enterprises	380,287	261,831
Loans collateralized by inventories	3,077,504	2,354,743
Loans collateralized by equipment	12,487,695	4,348,776
Loans collateralized by cash or guarantees	1,869,327	332,526
Other collateral	8,534,823	7,031,064
Total loans and advances to customers	55,269,880	23,830,006

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 carry the same credit risk as loans. Documentary and commercial letters of credit – which are written undertakings by the Bank on behalf of a customer authorising a third party to draw drafts on the Bank up to a stipulated amount under specific terms and conditions – are collateralised by the underlying shipments of goods to which they relate and therefore carry less risk than a direct loan.

Commitments to extend credit represent unused portions of authorisations to extend credit in the form of loans.

With respect to credit risk on commitments to extend credit, the Bank is potentially exposed to loss in an amount equal to the total unused commitments.

However, the likely amount of loss is less than the total unused commitments, as most commitments to extend credit are contingent upon customers maintaining specific credit standards. The Bank monitors the term to maturity of credit commitments because longer-term commitments generally have a greater degree of credit risk than shorter-term commitments.

29.1.4 Impairment and provisioning policies

The main considerations for the loan impairment assessment include whether any payments of principal or interest are overdue by more than 90 days or there are any known difficulties in the cash flows of counterparties, credit rating downgrades, or infringement of the original terms of the contract. The Bank addresses impairment assessment into areas: individually assessed allowances and collectively assessed allowances.

Individually assessed allowances

The Bank determines the allowances appropriate for each individually significant loan or advance on an individual basis. Items considered when determining allowance amounts include the sustainability of the counterparty's business plan, its ability to improve performance once a financial difficulty has

arisen, projected receipts and the expected dividend payout should bankruptcy ensue, the availability of other financial support and the realizable value of collateral, and the timing of the expected cash flows. The impairment losses are evaluated at each reporting date, unless unforeseen circumstances require more careful attention.

Collectively assessed allowances

Allowances are assessed collectively for losses on loans and advances that are not significant (including credit cards, residential mortgages and unsecured consumer lending) and for individually significant loans and advances where there is not yet objective evidence of individual impairment. Allowances are evaluated on each reporting date with each portfolio receiving a separate review.

The collective assessment takes account of impairment that is likely to be present in the portfolio even though there is not yet objective evidence of the impairment in an individual assessment. Impairment losses are estimated by taking into consideration of the following information: historical losses on the portfolio, current economic conditions, the approximate delay between the time a loss is likely to have been incurred and the time it will be identified as requiring an individually assessed impairment allowance, and expected receipts and recoveries once impaired.

Financial guarantees and letters of credit are assessed and provision made in a similar manner as for loans.

Loans and advances neither past due nor impaired

The table below shows the credit quality by class of asset for loans and advances neither past due or impaired, based on the historical counterparty default rates.

In thousand Armenian drams	2007	2006
Loans and advances to customers		
State owned enterprises	-	-
Privately held companies	-	-
Individuals	0.6 %	1.6 %
Sole proprietors	-	-
Non-commercial institutions	-	-

Past due but not impaired loans

Past due loans and advances include those that are only past due by a few days. The majority of the past due loans are not considered to be impaired.

Analysis of past due loans by age and by class is provided below.

In thousand Armenian drams					2007
	Less than 30 days	31 to 60 days	61 to 90 days	More than 91 days	Total
Loans and advances to customers					
Privately held companies	7,988	5,125	20,185	24,957	58,255
Individuals	30,262	14,251	8,746	21,195	74,454
Sole proprietors	196	283	-	665	1,144
Total	38,446	19,659	28,931	46,817	133,853

In thousand Armenian drams					2006
	Less than 30 days	31 to 60 days	61 to 90 days	More than 91 days	Total
Loans and advances to customers					
Privately held companies	5,555	4,955	973	9,509	20,992
Individuals	24,759	12,992	12,543	95,696	145,990
Sole proprietors	3,565	1,195	821	1,642	7,223
Total	33,879	19,142	14,337	106,847	174,205

The fair value of collateral that the Bank holds relating to past due loans at 31 December 2007 amounts to AMD 1,125,605 thousand. (2006: AMD 1,254,257 thousand). The collateral consists of cash, securities, letters of guarantees and properties.

Loans and advances individually impaired

The total gross amount of individually impaired loans and advances to customers before taking into consideration the cash flows from collateral held is AMD 3,109,047 thousand (2006: AMD 1,955,734 thousand). The fair value of collateral that the Bank holds relating to loans individually determined to be impaired at 31 December 2007 amounts to AMD 4,494,367 thousand. (2006: AMD 3,288,254 thousand). The collateral consists of cash, securities, letters of guarantees and properties.

29.2 Market risk

Market risk is the risk that the fair value or future cash flows of financial instruments will fluctuate due to changes in market variables such as interest rates and foreign exchange rates. The Bank classifies exposures to market risk into either trading or non-trading portfolios. The market risk for the trading portfolio is managed and monitored based on a VaR methodology which reflects the interdependency between risk variables. Non-trading positions are managed and monitored using other sensitivity analyses. The Bank has no significant concentration of market risk.

29.2.1 Market risk – Non-trading

Interest rate risk

Interest rate risk arises from the possibility that changes in interest rates will affect future cash flows or the fair values of financial instruments. The Board of Directors has established limits on the interest rate gaps for stipulated periods. Positions are monitored on a daily basis and hedging strategies are used to ensure positions are maintained within the established limits.

The following table demonstrates the sensitivity to a reasonable possible change in interest rates, with all other variables held constant, of the Bank's income statement.

The sensitivity of the income statement is the effect of the assumed changes in interest rates on the net interest income for one year, based on the floating rate non-trading financial assets and financial liabilities held at 31 December 2007, including the effect of hedging instruments. The sensitivity of equity is calculated by revaluing fixed rate available-for-sale financial assets, including the effect of any associated hedges, and swaps designated as cash flow hedges, at 31 December 2007 for the effects of the assumed changes in interest rates. The sensitivity of equity is analysed by maturity of the asset or swap. The total sensitivity of equity is based on the assumption that there are parallel shifts in the yield curve, while the analysis by maturity band displays the sensitivity to non-parallel changes.

In thousand Armenian drams

2007

Currency	Change in basis points	Sensitivity of net interest income	Sensitivity of equity				Total
			Up to 6 months	6 months to 1 year	1 year to 5 years	More than 5 years	
AMD	+2	-	(111,771)	(232)	(124,396)	(122,886)	(258,685)
USD	+2	(114,500)	-	-	-	-	-
AMD	-2	-	13,842	252	134,706	150,388	299,188
USD	-2	114,500	-	-	-	-	-

In thousand Armenian drams

2006

Currency	Change in basis points	Sensitivity of net interest income	Sensitivity of equity				Total
			Up to 6 months	6 months to 1 year	1 year to 5 years	More than 5 years	
AMD	+2	-	(28,565)	(29,784)	(83,400)	(132,371)	(274,120)
USD	+2	25,284	-	-	-	-	-
AMD	-2	-	36,165	31,945	92,601	149,433	310,143
USD	-2	(25,284)	-	-	-	-	-

Currency risk

Currency risk is the risk that the value of a financial instrument will fluctuate due to changes in foreign exchange rates. The Board of Directors has set limits on positions by currency. Positions are monitored on a daily basis and hedging strategies are used to ensure positions are maintained within established limits.

The tables below indicate the currencies to which the Bank had significant exposure at 31 December 2007 on its non-trading monetary assets and liabilities and its forecast cash flows. The analysis calculated the effect of a reasonably possible movement of the currency rate against the Armenian dram, with all other variables held constant on the income statement (due to the fair value of currency sensitive non-trading monetary assets and liabilities) and equity (due to the change in fair value of currency swaps and forward foreign exchange contracts used as cash flow hedges, and equity instruments). A negative amount in the table reflects a potential net reduction in income statement or equity, while a positive amount reflects a net potential increase.

In thousand Armenian drams

Currency	Change in currency rate in %	2007		2006	
		Effect on profit before tax	Currency	Effect on profit before tax	Change in currency rate in %
USD	20	36,821	20	85,149	
EUR	20	(15,521)	20	(1,254)	
RUR	20	545	20	23,273	
USD	(20)	(36,821)	(20)	(85,149)	
EUR	(20)	15,521	(20)	1,254	
RUR	(20)	(545)	(20)	(23,273)	

The Bank's exposure to foreign currency exchange risk is as follow:

In thousand Armenian drams	Armenian Dram	Freely convertible currencies	Non-freely convertible currencies	Total
ASSETS				
Cash and balances with the CBA	8,360,498	5,561,440	112,563	14,034,501
Amounts due from other financial institutions	516,484	9,164,229	367,793	10,048,506
Loans and advances to customers	38,717,736	15,778,882	-	54,496,618
Investments available for sale	7,347,420	-	-	7,347,420
	54,942,138	30,504,551	480,356	85,927,045
LIABILITIES				
Amounts due to financial institutions	6,559,243	5,732,982	2	12,292,227
Amounts due to customers	36,487,996	24,334,292	260,604	61,082,892
	43,047,239	30,067,274	260,606	73,375,119
Net position as at 31 December 2007	11,894,899	437,277	219,750	12,551,926
Credit related commitments as at 31 December 2007	5,185,594	6,185,284	-	11,370,878
Total financial assets	31,496,854	31,525,465	213,648	63,235,967
Total financial liabilities	25,817,193	31,471,898	97,380	57,386,471
Net position as at 31 December 2006	5,679,661	53,567	116,268	5,849,496
Credit related commitments as at 31 December 2006	4,477,232	2,787,523	40,020	7,304,775

Freely convertible currencies represent mainly US dollar amounts, but also include currencies from other OECD countries. Non-freely convertible amounts relate to currencies of CIS countries, excluding Republic of Armenia.

29.3 Liquidity risk

Liquidity risk is the risk that the Bank will be unable to meet its payment obligations when they fall due under normal and stress circumstances. To limit this risk, management has arranged diversified funding sources in addition to its core deposit base, manages assets with liquidity in mind, and monitors future cash flows and liquidity on a daily bases. This incorporates an assessment of expected cash flows and the availability of high grade collateral which could be used to secure additional funding if required.

The Bank maintains a portfolio of highly marketable and diverse assets that can be easily liquidated in the event of an unforeseen interruption of cash flow. The Bank also has committed lines of credit that it can access to meet liquidity needs. In addition, the Bank maintains an obligatory minimum reserve deposits with the Central Bank of Armenia equal to 8% of certain obligations of the Bank denominated in Armenian drams and 12% on certain obligations of the Bank denominated in foreign currency. See note 13. The liquidity position is assessed and managed under a variety of scenarios, giving due consideration to stress factors relating to both the market in general and specifically to the Bank.

The liquidity management of the Bank requires considering the level of liquid assets necessary to settle obligations as they fall due; maintaining access to a range of funding sources; maintaining funding contingency plans and monitoring balance sheet liquidity ratios against regulatory

requirements. The Bank calculates liquidity ratios on a daily basis in accordance with the requirement of the Central Bank of Armenia. These ratios are:

- General liquidity ratio (N_2^1), which is calculated as the ratio of highly-liquid assets to total assets; the ratio was 29.30 at 31 December 2007 (2006: 48.74).
- Current liquidity ratio (N_2^2), which is calculated as the ratio of highly-liquid assets to on-demand liabilities; the ratio was 76.94 at 31 December 2007 (2006: 90.62).

The table below summarises the maturity profile of the Bank's financial liabilities at 31 December 2007 based on contractual undiscounted repayment obligations. See note 28 for the expected maturities of these liabilities. Repayments which are subject to notice are treated as if notice were to be given immediately. However, the Bank expects that many customers will not request repayment on the earliest date the Bank could be required to pay and the table does not reflect the expected cash flows indicated by the Bank's deposit retention history.

In thousand Armenian drams						2007
	Demand and less than 1 month	From 1 to 3 months	From 3 to 12 months	From 1 to 5 years	More than 5 years	Total
FINANCIAL LIABILITIES						
Amounts due to financial institutions	1,506,041	5,359,887	311,611	3,213,314	1,901,374	12,292,227
Amounts due to customers	41,887,972	6,116,883	11,219,691	1,573,060	285,286	61,082,892
Total undiscounted financial liabilities	43,394,013	11,476,770	11,531,302	4,786,374	2,186,660	73,375,119
Credit related commitments	5,283,996	1,142,616	1,221,080	2,738,585	984,601	11,370,878

In thousand Armenian drams						2006
	Demand and less than 1 month	From 1 to 3 months	From 3 to 12 months	From 1 to 5 years	More than 5 years	Total
FINANCIAL LIABILITIES						
Amounts due to financial institutions	1,402,714	70,617	30,528		-	1,503,859
Amounts due to customers	40,674,418	4,098,489	8,492,006	2,617,565	134	55,882,612
Total undiscounted financial liabilities	42,077,132	4,169,106	8,522,534	2,617,565	134	57,386,471
Credit related commitments	5,126,747	1,112,577	724,762	340,689	-	7,304,775

30 Capital adequacy

The Bank maintains an actively managed capital base to cover risks inherent in the business. The adequacy of the Bank's capital is monitored using, among other measures, the rules and ratios

established by the Basel Committee on Banking Supervision (“BIS rules/ratios”) and adopted by the Central Bank of Armenia in supervising the Bank.

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

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

In thousand Armenian drams	2007		2006	
	Actual	Required	Actual	Required
Tier 1 capital	13,269,818	-	7,033,132	-
Tier 2 capital	803,365	-	1,209,691	-
Total capital	14,073,183	2,400,000	8,242,823	2,400,000
Risk weighted assets	67,158,310	-	34,516,298	-
Tier 1 capital ratio	19.8%	8%	20.4%	8%
Total capital ratio	21.0%	12%	23.9%	12%

Regulatory capital consists of Tier 1 capital, which comprises share capital, share premium, retained earnings including current year profit, and general reserve. Regulatory capital is calculated in accordance with the requirements of the Central Bank of Armenia and accounting standards of the Republic of Armenia. The other component of regulatory capital is Tier 2 capital, which includes revaluation reserves and other reserves.

The risk-weighted assets are measured by risk weights classified according to assessment of credit, market and other operational risks.

The Bank has complied with all externally imposed capital requirements through the period.

From 1 January 2009 minimum required capital becomes AMD 5,000,000 thousand.



Grant Thornton

www.gta.am