



Financial Statements and Independent Auditor's  
Report

Converse Bank closed joint stock company

31 December 2008

# Contents

	<b>Page</b>
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

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To the Shareholders and Board of Directors of Closed Joint Stock Company Converse Bank:

We have audited the accompanying financial statements of Converse Bank CJSC (the “Bank”), which comprise the balance sheet as at December 31, 2008, 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, 2008, and of its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards.

Armand Pinarbasi, CA  
Managing partner



Aren Aghajanyan  
Audit Manager



Grant Thornton Amyot LLC  
5 March 2009  
Yerevan



## Income statement

In thousand Armenian drams	Notes	Year ended December 31, 2008 (audited)	Year ended December 31, 2007 (audited)
Interest and similar income	6	5,992,854	3,629,500
Interest and similar expense	6	(2,184,769)	(982,029)
<b>Net interest income</b>		<b>3,808,085</b>	2,647,471
Fee and commission income	7	1,312,720	1,041,104
Fee and commission expense	7	(300,699)	(246,607)
<b>Net fee and commission income</b>		<b>1,012,021</b>	794,497
Net trading income	8	1,500,548	879,670
Gains less losses on investments available for sale		177,935	36,848
Other income	9	284,069	222,020
Impairment charge for credit losses	10	(588,101)	(135,738)
Impairment losses on investments available-for sale		(2,363)	-
Staff costs	11	(1,802,392)	(1,108,433)
Depreciation of property and equipment	19	(488,576)	(441,125)
Amortization of intangible assets	20	(15,076)	(12,850)
Other expenses	12	(1,481,794)	(1,084,297)
<b>Profit before income tax</b>		<b>2,404,356</b>	1,798,063
Income tax expense	13	(560,305)	(390,622)
<b>Profit for the year</b>		<b>1,844,051</b>	1,407,441

The accompanying notes on pages 7 to 51 are an integral part of these financial statements.

## Balance sheet

In thousand Armenian drams	Notes	As of December 31, 2008 (audited)	As of December 31, 2007 (audited)
<b>ASSETS</b>			
Cash and balances with CBA	14	12,467,281	11,214,519
Trading securities	15	58,672	734,661
Amounts due from other financial institutions	16	5,171,616	5,280,880
Loans and advances to customers	17	42,658,156	30,177,025
Investments available for sale	18	671,931	4,514,691
Securities pledged under repurchase agreements	28	3,944,502	2,427,799
Property, plant and equipment	19	3,886,295	3,949,458
Intangible assets	20	103,340	59,523
Other assets	21	267,706	232,645
<b>TOTAL ASSETS</b>		<b>69,229,499</b>	<b>58,591,201</b>
<b>LIABILITIES AND EQUITY</b>			
<b>Liabilities</b>			
Amounts due to financial institutions	22	10,101,122	5,860,286
Amounts due to customers	23	42,660,322	40,670,420
Debt securities issued	24	301,280	-
Trading liabilities	25	2,139,090	-
Current income tax liabilities		265,486	51,924
Deferred income tax liabilities	13	472,991	484,508
Other liabilities	26	312,757	463,674
Other provisions	27	35,345	34,943
<b>Total liabilities</b>		<b>56,288,393</b>	<b>47,565,755</b>
<b>Equity</b>			
Share capital	29	1,233,133	1,233,133
Share premium		63,233	63,233
Statutory general reserve		648,183	648,183
Other reserves		1,862,068	1,926,290
Retained earnings		9,134,489	7,154,607
<b>Total equity</b>		<b>12,941,106</b>	<b>11,025,446</b>
<b>TOTAL LIABILITIES AND EQUITY</b>		<b>69,229,499</b>	<b>58,591,201</b>

The financial statements from pages 3 to 51 were approved by the Board of the Bank on 5 March 2009 and signed by the Bank's General Director and Chief Accountant. The accompanying notes on pages 7 to 51 are an integral part of these financial statements.

A. GHUKASYAN  
General Director



A. KARAKHANYAN  
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	Revaluation reserve of PPE	Retained earnings	Total
Balance as of January 1, 2007 (audited)	1,233,133	63,233	648,183	(4,254)	2,109,860	5,577,377	9,627,532
Adjustment to reserve on disposal of PPE	-	-	-	-	(169,789)	169,789	-
Net unrealized loss from changes in fair value	-	-	-	(532)	-	-	(532)
Net gains realized to net profit on disposal of available-for-sale instruments	-	-	-	(12,820)	-	-	(12,820)
Effect of deferred taxes	-	-	-	3,825	-	-	3,825
Total income and expense recognized directly in equity	-	-	-	(9,527)	(169,789)	169,789	(9,527)
Profit for the year	-	-	-	-	-	1,407,441	1,407,441
Total income and expense for the year	-	-	-	(9,527)	(169,789)	1,577,230	1,397,914
Balance as of December 31, 2007 (audited)	<u>1,233,133</u>	<u>63,233</u>	<u>648,183</u>	<u>(13,781)</u>	<u>1,940,071</u>	<u>7,154,607</u>	<u>11,025,446</u>
Adjustment to reserve on disposal of PPE	-	-	-	-	(135,831)	135,831	-
Net unrealized gains from changes in fair value	-	-	-	65,841	-	-	65,841
Net losses realized to net profit on disposal of available-for-sale instruments	-	-	-	23,412	-	-	23,412
Effect of deferred taxes	-	-	-	(17,644)	-	-	(17,644)
Total income and expense recognized directly in equity	-	-	-	71,609	(135,831)	135,831	71,609
Profit for the year	-	-	-	-	-	1,844,051	1,844,051
Total income and expense for the year	-	-	-	71,609	(135,831)	1,979,882	1,915,660
Balance as of December 31, 2008 (audited)	<u>1,233,133</u>	<u>63,233</u>	<u>648,183</u>	<u>57,828</u>	<u>1,804,240</u>	<u>9,134,489</u>	<u>12,941,106</u>

## Statement of cash flows

In thousand Armenian drams	Year ended December 31,2008 (audited)	Year ended December 31,2007 (audited)
<b>Cash flows from operating activities</b>		
Interest received	5,830,173	3,632,197
Interest paid	(1,807,447)	(1,013,438)
Fees and commissions received	1,312,720	945,258
Fees and commissions paid	(298,598)	(244,797)
Gains less losses from trading securities	(3,151)	106,962
Realised gains less losses from dealing in foreign currencies	1,506,614	922,424
Other income received	554,536	312,845
Recovery of previously written off loans	57,301	145,495
Salaries and benefits paid	(1,639,644)	(993,982)
Other operating expenses paid	(435,011)	(1,372,995)
<b>Cash flows from operating activities before changes in operating assets and liabilities</b>	<b>5,077,493</b>	<b>2,439,969</b>
<i>Net (increase)/decrease in operating assets</i>		
Deposited funds in the CBA	102,010	102,298
Amounts due from other financial institutions	(1,004,966)	89,232
Loans and advances to customers	(13,339,387)	(18,377,795)
Other assets	(1,838)	(5,066,896)
<i>Increase/(decrease) in operating liabilities</i>		
Amounts due to financial institutions	1,611,552	3,319,219
Amounts due to customers	5,477,697	20,761,982
Trading liabilities	2,139,090	-
Other liabilities	645,879	89,060
<b>Net cash flow from operating activities before income tax</b>	<b>707,530</b>	<b>3,357,069</b>
Income tax paid	(391,102)	(414,173)
<b>Net cash from operating activities</b>	<b>316,428</b>	<b>2,942,896</b>
<b>Cash flows from investing activities</b>		
Purchase of investment securities	(2,221,573)	(2,158,579)
Dividends received	504	782
Purchase of property and equipment	(380,757)	(432,691)
Proceeds from sale of property and equipment	4,977	115,106
<b>Net cash used in investing activities</b>	<b>(2,596,849)</b>	<b>(2,475,382)</b>
<b>Cash flow from financing activities</b>		
Loans received from financial institutions	1,363,929	152,335
Loans received from RA Government	750,000	-
Debt securities issued	300,000	-
<b>Net cash flow from financing activities</b>	<b>2,413,929</b>	<b>152,335</b>
<b>Net increase in cash and cash equivalents</b>	<b>133,508</b>	<b>619,849</b>
Cash and cash equivalents at the beginning of the year	14,755,899	14,845,723
Effect of exchange rate changes on cash and cash equivalents	(460,183)	(709,673)
<b>Cash and cash equivalents at the end of the year (Note 14)</b>	<b>14,429,224</b>	<b>14,755,899</b>

# Accompanying notes to the financial statements

## 1 Principal activities

Converse Bank CJSC (the “Bank”) is a closed joint-stock bank, which was incorporated in the Republic of Armenia in 1994. The Bank is regulated by the legislation of RA and conducts its business under license number 57, granted on November 28, 1994 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 25 branches in Yerevan and in different regions.

The registered office of the Bank is located at: Yerevan, Vazgen Sargsyan Str. 26/1.

## 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. In addition, economic conditions continue to limit the volume of activity in the financial markets, which may not be reflective of the values for financial instruments. The main obstacle to further economic development is a low level of economic and institutional development, along with a centralized economic base and regional instability.

The international rating agency Moody's Investors Service has assessed Armenia's sovereign rating Ba2 “Stable Outlook” in its annual report produced at the end of 2008. According to the report, the country's low government debt and minimal refinancing risks are allowing its rating to maintain a stable outlook in the current environment. A weak revenue base is the main fiscal risk, although it is ameliorated by the very comfortable debt service profile, its good relations with its official creditors, and the liquidity provided by the Diaspora.

Due to smaller extent of the involvement of foreign capital in the equities of Armenian businesses, as well as the comparably small foreign investments in the Armenian economy and the isolation of its relevant sectors from the rest of the world, the ongoing financial crisis observable in more developed and mature economies is not particularly severe and observable in Armenia as of the reporting date.

The Government of Armenia is in the process of researching the causes and consequences of the crisis with the purposes of developing a set of measures to fight against those consequences when the crisis becomes inevitable for Armenia.

However, in times of more severe market stress, the Armenian economy as well as the Bank may be subject to that crisis and the effects of the crisis may be significant. As far as the number of variables and assumptions involved in these uncertainties is big, management cannot make a reliable estimate of the amounts by which the carrying amounts of assets and liabilities of the Bank may be affected.

Accordingly, the financial statements of the Bank do not include the effects of adjustments, if any, which might have been considered necessary, had the effects of the current global crisis become observable and reliably measurable in Armenia.

### 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 Adoption of new and revised standards

In the current year the Bank has adopted all of the new and revised Standards and Interpretations issued by the International Accounting Standards Board (the “IASB”) and International Financial Reporting Interpretations Committee (the “IFRIC”) of the IASB that are relevant to its operations and effective for annual reporting periods beginning on January 1, 2008.

#### 3.6 Standards and Interpretations not yet applied by the Bank

At the date of authorization of these financial statements, certain new Standards, amendments and Interpretations to the existing Standards have been published but are not yet effective. The Bank has not early adopted any of these pronouncements.

Management anticipates that all of the pronouncements will be adopted in the Bank’s accounting policy for the first period beginning after the effect date of the pronouncement.

***The new Standards, amendments and Interpretations to the existing Standards that are not yet effective but are expected to be relevant to the Bank’s financial statements in the future.***

IAS 1 *Presentation of Financial Statements* (revised 2007)

New amendments in this standard affect the presentation of owner changes in equity and introduce a statement of comprehensive income. Preparers will have the option of presenting items of income

and expense and components of other comprehensive income either in a single statement of comprehensive income with subtotals, or in two separate statements (a separate income statement followed by a statement of other comprehensive income). This amendment does not affect the financial position or results of the Bank, but will give rise to additional disclosures. Management is currently assessing the detailed impact of this amendment on the Bank's financial statements.

#### IAS 23 *Borrowing Costs* (revised 2007)

Amendments in this standard require the capitalization of borrowing costs, to the extent they are directly attributable to the acquisition, production or construction of qualifying assets that need a period of time to get ready for their intended use or sale. The option of immediately expensing those borrowing costs, currently used by the Bank, will be removed. In accordance with the transitional provisions of the amended Standard, no changes will be made for borrowing costs incurred to this date that have been expensed. This amendment will decrease the Bank's reported interest expense and increase the capitalized cost of qualifying assets under construction in future periods.

#### IFRS 8 *Operating Segments*

This is a disclosure standard, which will result in a re-designation of the Bank's reportable segments but will not have any impact on the reported results or financial position.

***The new Standards, amendments and Interpretations to the existing Standards that are not yet effective and are not expected to be relevant to the Bank's financial statements.***

#### IFRIC 13 *Customer Loyalty Programmes*

This interpretation clarifies that when goods or services are sold together with a customer loyalty incentive (loyalty points or free products), the arrangement is a multiple-element arrangement and the consideration receivable from the customer is allocated between the components of the arrangement using fair values. The Bank currently is not running a similar programme. Accordingly, management believes that this interpretation is not relevant to the Bank's financial statements.

#### Amendment to IFRS 2 *Share-based Payment*

This amendment relates to vesting conditions and cancellations. The Bank currently is not running any share-based payment scheme. Accordingly, management believes that this amendment is not relevant to the Bank's financial statements.

### **Annual improvements 2008**

The IASB has issued Improvements for International Financial Reporting Standards 2008. Most of these amendments become effective in annual periods beginning on or after January 1, 2009. Management believes that these improvements will not have significant impact on the Bank's financial statements.

#### IAS 23 (Amendment) *Borrowing Costs* (effective from January 1, 2009).

The definition of borrowings costs has been amended so that interest expense is calculated using the effective interest rate method defined in IAS 39 Financial Instruments: Recognition and

Measurement (effective from January 1, 2009). The Bank will apply the IAS 23 (Amendment) prospectively to the capitalization of borrowing costs from January 1, 2009.

IAS 36 (Amendment) *Impairment of Assets* (effective from January 1, 2009)

Where fair value less costs to sell is calculated on the basis of discounted cash flows, disclosures equivalent to those for value-in-use calculation should be made. The Bank will apply the IAS 36 (Amendment) and provide the required disclosures where applicable for impairment tests from January 1, 2009.

IAS 38 (Amendment) *Intangible Assets* (effective from January 1, 2009)

A prepayment may only be recognized in the event that payment has been made in advance of obtaining right of access to goods or receipt of services.

Additionally, the amendment deletes the wording that states that there is “rarely if ever” support for use of a method that results in a lower rate of amortization than the straight-line method. The amendment will not have an impact on the Bank’s operations, since all intangible assets are amortized using the straight-line method.

IAS 40 (Amendment) *Investment Property (and consequential amendments to IAS 16)* (effective from January 1, 2009)

Property that is under construction or development for future use as investment property is within the scope of IAS 40. Where the fair value model is applied, such property is therefore measured at fair value. However, where fair value of investment property under construction is not reliably measurable, the property is measured at cost until the earlier of the date construction is completed and the date at which the fair value becomes reliably measurable. The Bank will apply the IAS 40 (Amendment) from January 1, 2009.

IAS 20 (Amendment) *Accounting for Government Grants and Disclosure of Government Assistance* (effective from January 1, 2009)

The benefit of a below-market rate government loan is measured as the difference between the carrying amount in accordance with IAS 39 and the proceeds received with the benefit to be accounted for in accordance with IAS 20. The Bank will apply the IAS 20 (Amendment) from 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.

*Dividend income*

Revenue is recognized when the Bank's right to receive the payment is established.

*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.

#### 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, 2008	December 31, 2007
AMD/1 US Dollar	306.73	304.22
AMD/1 Euro	435.00	446.96

#### 4.3 Taxation

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

Current tax is the expected tax payable on the taxable income for the period, 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 valuation techniques. Such techniques include using recent arm's length market transactions, reference to the current market value of another instrument, which is substantially the same, and 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*

On exceptional cases and depending on customer's position in the market and business, Bank seeks to restructure loans, provided client's long term creditworthiness is not under question, temporary financial difficulties are due to reasons beyond client's control and client's obligations towards bank are not past due at review time. Where possible, Bank takes additional collateral, guarantees to make its position stronger.

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

##### *Finance - Bank as lessee*

The Bank recognises finance leases as assets and liabilities in the balance sheet at the date of commencement of the lease term at amounts equal to the fair value of the leased property or, if lower, at the present value of the minimum lease payments. In calculating the present value of the minimum lease payments the discount factor used is the interest rate implicit in the lease, when it is practicable to determine; otherwise, the Bank’s incremental borrowing rate is used. Initial direct costs incurred are included as part of the asset. Lease payments are apportioned between the finance charge and the reduction of the outstanding liability. The finance charge is allocated to periods during the lease term so as to produce a constant periodic rate of interest on the remaining balance of the liability for each period.

##### *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
Equipment	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 on a straight-line basis over the useful economic lives of 1 to 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.

Costs associated with maintaining computer software programmes are recorded as an expense as incurred.

#### 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 Central Bank and 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. In addition, the Bank has no post-retirement benefits or significant other compensated benefits requiring accrual.

#### 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 and non-redeemable preference shares with discretionary dividends are both 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 these financial statements are presented below:

##### *Classification of investment securities*

Securities owned by the Bank comprise Armenian state and corporate bonds, securities issued by the Central Bank of Armenia 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 financials 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 30.

#### *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	Year ended 31.12.08	Year ended 31.12.07
Loans and advances to customers	5,127,894	2,874,309
Debt investment securities available-for-sale	344,447	371,302
Amounts due from other financial institutions	141,095	208,070
Reverse repurchase transactions	54,963	73,243
Interest accrued on impaired financial assets	238,866	56,813
Other interest income	85,589	45,763
<b>Total interest and similar income</b>	<b>5,992,854</b>	<b>3,629,500</b>

In thousand Armenian drams	Year ended 31.12.08	Year ended 31.12.07
Amounts due to customers	1,649,959	742,341
Amounts due to financial institutions	371,652	232,549
Debt securities issued	535	-
Repurchase transactions	157,869	5,246
Other interest expenses	4,754	1,893
<b>Total interest and similar expense</b>	<b>2,184,769</b>	<b>982,029</b>

## 7 Fee and commission income and expense

In thousand Armenian drams	Year ended 31.12.08	Year ended 31.12.07
Cash collection	307,629	174,423
Wire transfer fees	502,101	467,560
Plastic cards operations	374,026	303,274
Service fee for account maintenance of Municipal and State budgets	-	562
Guarantees and letters of credit	128,964	95,285
<b>Total fee and commission income</b>	<b>1,312,720</b>	<b>1,041,104</b>

In thousand Armenian drams	Year ended 31.12.08	Year ended 31.12.07
Wire transfer fees	58,015	44,746
Cash operations	120,423	100,776
Plastic cards operations	120,160	99,275
Other expenses	2,101	1,810
<b>Total fee and commission expense</b>	<b>300,699</b>	<b>246,607</b>

## 8 Net trading income

In thousand Armenian drams	Year ended 31.12.08	Year ended 31.12.07
Gains less losses from trading in foreign currencies transactions	1,506,614	922,424
Gains less losses from foreign exchange translation of trading assets	(2,915)	(111,083)
Gains less losses on trading of trading securities	(3,151)	68,329
<b>Total net trading income</b>	<b>1,500,548</b>	<b>879,670</b>

## 9 Other income

In thousand Armenian drams	Year ended 31.12.08	Year ended 31.12.07
Fines and penalties received	190,722	132,569
Dividend income	504	782
Income from grant	1,316	5,949
Other income	91,527	82,720
<b>Total other income</b>	<b>284,069</b>	<b>222,020</b>

## 10 Impairment charge for/(reversal of) credit losses

In thousand Armenian drams	Year ended 31.12.08	Year ended 31.12.07
Loans and advances to customers (Note 17)	589,643	108,130
Other assets (Note 21)	(1,944)	(7,335)
Guarantees (Note 27)	402	34,943
<b>Total impairment charge for credit losses</b>	<b>588,101</b>	<b>135,738</b>

## 11 Staff costs

In thousand Armenian drams	Year ended 31.12.08	Year ended 31.12.07
Wages and salaries	1,641,708	997,421
Social security contributions	160,684	111,012
<b>Total staff costs</b>	<b>1,802,392</b>	<b>1,108,433</b>

## 12 Other expenses

In thousand Armenian drams	Year ended 31.12.08	Year ended 31.12.07
Fixed and intangible assets maintenance	114,323	95,700
Advertising costs	158,060	127,645
Business trip expenses	29,238	10,218
Communications	94,777	95,022
Operating lease	163,781	61,246
Taxes, other than income tax, duties	131,515	97,489
Consulting and other services	82,620	34,834
Security	71,492	54,643
Loss on disposal of PPE	2,944	4,864
Office supplies	34,271	25,030
Penalties paid	8,130	22,512
Foreign currency translation net losses of non-trading assets	307,872	253,993
Cash collection expenses	63,228	54,281
Other expenses	219,543	146,820
<b>Total other expense</b>	<b>1,481,794</b>	<b>1,084,297</b>

## 13 Income tax expense

In thousand Armenian drams	Year ended 31.12.08	Year ended 31.12.07
Current tax expense	589,466	427,803
Adjustments of current income tax of previous years	-	12,324
Deferred tax	(29,161)	(49,505)
<b>Total income tax expense</b>	<b>560,305</b>	<b>390,622</b>

The corporate income tax within the Republic of Armenia is levied at the rate of 20% (2007: 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	Year ended 31.12.08	Effective rate (%)	Year ended 31.12.07	Effective rate (%)
<b>Profit before tax</b>	<b>2,404,356</b>		1,798,063	
Income tax at the rate of 20%	<b>480,871</b>	<b>20</b>	359,613	20
Non-taxable income	<b>(3,033)</b>	-	(41,524)	(2)
Non-deductible expenses	<b>20,893</b>	<b>1</b>	21,734	1
Foreign exchange loss	<b>61,574</b>	<b>2</b>	50,799	3
<b>Income tax expense</b>	<b>560,305</b>	<b>23</b>	<b>390,622</b>	<b>22</b>

Deferred tax calculation in respect of temporary differences:

In thousand Armenian drams	31.12.07	Recognized in income statement	Recognized in equity	31.12.08
Accrued expenses and other liabilities	<b>1,900</b>	<b>2,352</b>	-	<b>4,252</b>
Allowances for other provisions	<b>3,836</b>	<b>(2,428)</b>	-	<b>1,408</b>
Fair value measurement of securities available for sale	<b>4,889</b>	-	<b>9,755</b>	<b>14,644</b>
Fair value measurement of trading securities	<b>4,796</b>	<b>(4,796)</b>	-	-
Additional loan provision	<b>4,352</b>	<b>(4,352)</b>	-	-
<b>Total deferred tax assets</b>	<b>19,773</b>	<b>(9,224)</b>	<b>9,755</b>	<b>20,304</b>
Allowance for impairment on other assets	<b>(10,774)</b>	<b>4,426</b>	-	<b>(6,348)</b>
Fair value measurement of securities available for sale	-	-	<b>(27,399)</b>	<b>(27,399)</b>
Revaluation of the PPE	<b>(493,507)</b>	<b>33,959</b>	-	<b>(459,548)</b>
<b>Total deferred tax liability</b>	<b>(504,281)</b>	<b>38,385</b>	<b>(27,399)</b>	<b>(493,295)</b>
<b>Net deferred tax liability</b>	<b>(484,508)</b>	<b>29,161</b>	<b>(17,644)</b>	<b>(472,991)</b>

In thousand Armenian drams	31.12.06	Recognized in income statement	Recognized in equity	31.12.07
Accrued expenses and other liabilities	1,959	(59)	-	1,900
Allowances for other provisions	-	3,836	-	3,836
Fair value measurement of securities available for sale	1,064	-	3,825	4,889
Fair value measurement of trading securities	16,599	(11,803)	-	4,796
Additional loan provision	-	4,352	-	4,352
<b>Total deferred tax assets</b>	<b>19,622</b>	<b>(3,674)</b>	<b>3,825</b>	<b>19,773</b>
Allowance for impairment on other assets	-	(10,774)	-	(10,774)
Allowances for other provisions	(369)	369	-	-
Fair value measurement of trading securities	(29,625)	29,625	-	-
Revaluation of the PPE	(527,466)	33,959	-	(493,507)
<b>Total deferred tax liability</b>	<b>(557,460)</b>	<b>53,179</b>	-	<b>(504,281)</b>
<b>Net deferred tax liability</b>	<b>(537,838)</b>	<b>49,505</b>	<b>3,825</b>	<b>(484,508)</b>

According to RA tax legislation, the Bank has the right to set off the income tax prepayment with current year income tax liability after the end of the reporting year.

#### 14 Cash, cash equivalents and balances with CBA

In thousand Armenian drams	31.12.08	31.12.07
Cash on hand	3,977,346	3,774,239
Other money market placements	12,142	37,363
Correspondent account with the CBA	8,265,783	7,292,917
<b>Included in cash and cash equivalents</b>	<b>12,255,271</b>	<b>11,104,519</b>
Deposited funds with the CBA	212,010	110,000
<b>Total cash and balances with the CBA</b>	<b>12,467,281</b>	<b>11,214,519</b>
Cash and balances with the CBA, included in cash flow	12,255,271	11,104,519
Placements with other banks (note 16)	2,173,953	3,651,380
<b>Total cash and cash equivalents</b>	<b>14,429,224</b>	<b>14,755,899</b>

As at 31 December 2008 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 4,677,481 thousand (2007: AMD 4,148,269 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.

#### 15 Trading securities

In thousand Armenian drams	31.12.08	31.12.07
Securities issued by the Ministry of Finance – unquoted	58,672	267,121
Securities issued by the CBA – unquoted	-	388,680
Corporate shares - quoted	-	78,860
<b>Trading securities</b>	<b>58,672</b>	<b>734,661</b>

For 2007, corporate shares were pledged as guarantee for the Bank's operations with GunnAllen Inc.

Effective interest rates and maturities of interest trading securities are as follows:

In thousand Armenian drams		31.12.08		31.12.07
	%	Maturity	%	Maturity
Securities issued by the Ministry of Finance	0-10.53	2009-2028	6.61-6.74	2008-2012
Securities issued by the CBA	-	-	-	2008

As at 31 December 2008 included in assets held-for-trading is accrued interest income on debt securities amounting to AMD 1,625 thousand (2007: AMD 2,121 thousand).

## 16 Amounts due from other financial institutions

In thousand Armenian drams	31.12.08	31.12.07
Correspondent accounts with financial institutions	2,173,953	3,651,380
<b>Included in cash and cash equivalents</b>	<b>2,173,953</b>	<b>3,651,380</b>
Loans and deposits to financial institutions	1,468,497	546,391
Loans under repurchase agreements	1,210,014	-
Other amounts	319,152	1,083,109
<b>Total amounts due from other financial institutions</b>	<b>5,171,616</b>	<b>5,280,880</b>

As at 31 December 2008 the amounts due from other financial institutions in amounts of AMD 1,975,537 thousand (38%) (2007: AMD 2,926,246 thousand (55%)) were due from 3 banks.

As of 31 December 2008 included in amounts due from other financial institutions are guarantee deposits placed by the Bank for its operations in the amount of AMD 337,102 thousand (2007: AMD 478,587 thousand).

During 2008, 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 2008, the Bank placed AMD 92,545 thousand, including accrued interests, (2007: AMD 761,605 thousand) as deposits in drams with Armenian financial institution, which were related to deposits received from the same institution (See Note 22).

Fair value of assets pledged and carrying value of loans under reverse repurchase agreements as of 31 December 2008 are presented as follows:

In thousand Armenian drams	31.12.08		31.12.07	
	Fair value of collateral	Carrying value of loans	Fair value of collateral	Carrying value of loans
Securities issued by the Ministry of Finance of RA	1,232,356	1,210,014	-	-
<b>Total assets pledged and loans under reverse repurchase agreements</b>	<b>1,232,356</b>	<b>1,210,014</b>	<b>-</b>	<b>-</b>

As of 31 December 2008 out of total accepted securities AMD 938,371 thousand (2007: nil) were repledged to the third parties for periods not exceeding three months from the transfer (See Note 25).

## 17 Loans and advances to customers

In thousand Armenian drams	<b>31.12.08</b>	31.12.07
Loans to customers	<b>41,011,496</b>	28,540,468
Factoring	<b>866,636</b>	1,059,692
Overdrafts	<b>1,379,970</b>	686,812
Letters of credit	<b>312,381</b>	234,420
	<b>43,570,483</b>	30,521,392
Less allowance for loan impairment	<b>(912,327)</b>	(344,367)
<b>Total loans and advances to customers</b>	<b>42,658,156</b>	30,177,025

As of 31 December 2008, accrued interest income included in loans and advances to customers amounted to AMD 284,328 thousand (2007: AMD 202,841 thousand).

As of December 31, 2008, the Bank had a concentration of loans represented by AMD 10,645,899 thousand due from the ten largest third party entities and parties related with them (25% of gross loan portfolio) (2007: AMD 9,040,701 thousand or 30%). An allowance of AMD 448,741 thousand (2007: AMD 101,882 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					<b>31.12.08</b>
	<b>State owned enterprises</b>	<b>Privately held companies</b>	<b>Individuals</b>	<b>Sole proprietors</b>	<b>Total</b>
At 1 January 2008	4,527	192,092	126,346	21,402	344,367
Charge for the year	300	422,696	132,578	34,069	589,643
Amounts written off	-	(7,535)	(67,208)	(1,906)	(76,649)
Recoveries	-	17,575	35,819	1,572	54,966
At 31 December 2008	<u>4,827</u>	<u>624,828</u>	<u>227,535</u>	<u>55,137</u>	<u>912,327</u>
Individual impairment	-	570,256	-	-	570,256
Collective impairment	50	147,212	157,223	37,586	342,071
	<u>50</u>	<u>717,468</u>	<u>157,223</u>	<u>37,586</u>	<u>912,327</u>
Gross amount of loans individually determined to be impaired, before deducting any individually assessed impairment allowance	<u>-</u>	<u>2,476,893</u>	<u>-</u>	<u>-</u>	<u>2,476,893</u>

In thousand Armenian drams	31.12.07				
	State owned enterprises	Privately held companies	Individuals	Sole proprietors	Total
At 1 January 2007	1,895	211,091	50,444	13,603	277,033
Charge for the year	2,632	31,367	74,128	3	108,130
Amounts written off	-	(113,755)	(11,031)	(667)	(125,453)
Recoveries	-	63,389	12,805	8,463	84,657
At 31 December 2007	<u>4,527</u>	<u>192,092</u>	<u>126,346</u>	<u>21,402</u>	<u>344,367</u>
Individual impairment	-	44,215	-	-	44,215
Collective impairment	<u>4,527</u>	<u>147,877</u>	<u>126,346</u>	<u>21,402</u>	<u>300,152</u>
	<u>4,527</u>	<u>192,092</u>	<u>126,346</u>	<u>21,402</u>	<u>344,367</u>
Gross amount of loans individually determined to be impaired, before deducting any individually assessed impairment allowance	<u>-</u>	<u>1,117,898</u>	<u>-</u>	<u>-</u>	<u>1,117,898</u>

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

In thousand Armenian drams	31.12.08	31.12.07
State owned enterprises	4,953	452,709
Privately held companies	23,800,124	16,965,223
Individuals	15,722,365	11,081,552
Sole proprietors	3,758,564	1,819,067
Non-commercial institutions	149	-
Accrued interest	284,328	202,841
	<u>43,570,483</u>	<u>30,521,392</u>
Less allowance for loan impairment	(912,327)	(344,367)
<b>Total loans and advances to customers</b>	<u><b>42,658,156</b></u>	<u><b>30,177,025</b></u>

Loans to individuals comprise the following products:

In thousand Armenian drams	31.12.08	31.12.07
Mortgage loans	4,438,504	2,262,339
Consumer loans	6,763,032	4,821,713
Car loans	3,562,448	2,484,040
Other	958,381	1,513,460
<b>Total loans and advances to individuals (gross)</b>	<u><b>15,722,365</b></u>	<u><b>11,081,552</b></u>

At 31 December 2008 and 31 December 2007 the estimated fair value of loans and advances to customers approximates its carrying value. Refer to Note 32.

Credit, currency, liquidity and interest rate analyses of loans and advances to customers are disclosed in Note 34. The information on related party balances is disclosed in Note 31.

## 18 Investments available for sale

In thousand Armenian drams	31.12.08	31.12.07
<b>Unquoted investments</b>		
Corporate bonds	401,286	130,573
Securities issued by the Ministry of Finance of Armenia	52,924	2,755,046
Securities issued by the CBA	-	1,545,535
Corporate shares	217,721	83,537
<b>Total investments</b>	<b>671,931</b>	<b>4,514,691</b>

All debt securities have fixed coupons.

All unquoted available-for-sale equities are recorded at cost less allowance for impairment since its fair value cannot be reliably estimated. There is no market for these investments and the Bank intends to hold it for the long term.

The fair value of unquoted available-for-sale debt securities is measured using a valuation technique, which uses current market rates to discount future cash flows of the financial instruments.

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

In thousand Armenian drams	31.12.08		31.12.07	
	%	Maturity	%	Maturity
Securities issued the Ministry of Finance of Armenia	0-10.53%	2009-2028	6.61-8.14	2008-2022
Corporate bonds	9%	2009	9%	2008
Securities issued by the CBA	-	-	-	2008

As at 31 December 2008 debt securities available for sale at fair value of AMD 3,944,502 thousand were pledged to third parties in sale and repurchase agreements for periods not exceeding six months (2007: 2,427,799 thousand). See Note 28. These securities have been reclassified as securities pledged under repurchase agreements on the face of the balance sheet.

## 19 Property, plant and equipment

In thousand Armenian drams	Land and buildings	Equipment	Vehicles	Computers	Other fixed assets	Leasehold improvements	Total
<b>COST</b>							
Cost/Revalued amount at January 1, 2007	3,683,887	291,891	78,266	688,964	307,871	23,537	5,074,416
Additions	67,104	44,301	20,994	235,530	43,814	15,567	427,310
Disposals	-	(11,513)	(43,734)	(16,466)	(7,061)	-	(78,774)
At December 31, 2007	3,750,991	324,679	55,526	908,028	344,624	39,104	5,422,952
Additions	5,566	44,079	4,357	293,681	34,742	69,593	452,018
Disposals	-	(4,295)	(4,172)	(47,176)	(1,657)	(7,365)	(64,665)
Reclassification	(10,780)	89	-	-	(89)	-	(10,780)
At December 31, 2008	3,745,777	364,552	55,711	1,154,533	377,620	101,332	5,799,525
<b>DEPRECIATION</b>							
At January 1, 2007	222,899	203,012	36,660	487,340	122,284	8,777	1,080,972
Depreciation charge	223,071	37,158	11,183	107,450	55,305	6,958	441,125
Disposals	-	(10,422)	(21,387)	(13,188)	(3,606)	-	(48,603)
At December 31, 2007	445,970	229,748	26,456	581,602	173,983	15,735	1,473,494
Depreciation charge	223,510	42,730	10,087	137,715	61,953	12,581	488,576
Disposals	-	(4,295)	(2,991)	(34,545)	(1,192)	(5,817)	(48,840)
Reclassification	-	9	-	-	(9)	-	-
At December 31, 2008	669,480	268,192	33,552	684,772	234,735	22,499	1,913,230
<b>CARRYING VALUE</b>							
At December 31, 2008	3,076,297	96,360	22,159	469,761	142,885	78,833	3,886,295
At December 31, 2007	3,305,021	94,931	29,070	326,426	170,641	23,369	3,949,458

*Revaluation of assets*

The buildings owned by the Bank were evaluated by an independent appraiser Tigris LLC at 31 December 2005 using a combination of the market, income and cost methods resulting in a revaluation of AMD 1,540,084 thousand. Management have based their estimate of the fair value of the buildings on the results of the independent appraisal.

The net book value of buildings that would have been recognized under the historic cost method is 823,161 AMD thousand as at 31 December 2008 (2007: AMD 874,779 thousand).

Management believes that as of 31.12.08 the fair value of the buildings does not significantly differ from their carrying amount.

*Fully depreciated items*

As at 31 December 2008 fixed assets included fully depreciated assets in amount of AMD 690,658 thousand (2007: AMD 621,551 thousand).

*Fixed assets in the phase of installation*

As at 31 December 2008 fixed assets included assets in the phase of installation in amount of AMD 124,761 thousand (2007: AMD 66,951 thousand), which are not amortized and are classified in accordance with their type.

## 20 Intangible assets

In thousand Armenian drams	Licenses and patents	Acquired software licenses	Other	Total
<b>COST</b>				
At January 1, 2007	118,589	17,540	3,868	139,997
Additions	3,247	1,280	750	5,277
Disposals	(106)	(451)	(2,610)	(3,167)
At December 31, 2007	121,730	18,369	2,008	142,107
Additions	51,554	5,400	1,939	58,893
<b>At December 31, 2008</b>	<b>173,284</b>	<b>23,769</b>	<b>3,947</b>	<b>201,000</b>
<b>AMORTISATION</b>				
At January 1, 2007	60,995	8,660	1,437	71,092
Amortisation charge	10,585	1,705	560	12,850
Disposals	(55)	(49)	(1,254)	(1,358)
At December 31, 2007	71,525	10,316	743	82,584
Amortisation charge	12,523	2,352	201	15,076
<b>At December 31, 2008</b>	<b>84,048</b>	<b>12,668</b>	<b>944</b>	<b>97,660</b>
<b>CARRYING VALUE</b>				
<b>At December 31, 2008</b>	<b>89,236</b>	<b>11,101</b>	<b>3,003</b>	<b>103,340</b>
At December 31, 2007	50,205	8,053	1,265	59,523

*Fully amortized items*

As at 31 December 2008 intangible assets included fully amortized assets in amount of AMD 8,526 thousand (2007: nil).

## 21 Other assets

In thousand Armenian drams	31.12.08	31.12.07
Prepayments and other debtors	110,840	41,992
Prepayment to budget	26,193	1,647
Settlements with employees	80	-
Other assets	14,841	34,950
	151,954	78,589
Less allowance for impairment	(512)	(1,336)
	151,442	77,253
Accounts receivable	300	32,101
Accrued income	262	1,852
	562	33,953
Assets classified as held for sale	70,899	67,564
Other prepaid taxes	2,039	2,040
Materials	40,869	49,940
Other	1,895	1,895
<b>Total other assets</b>	<b>267,706</b>	<b>232,645</b>

As at December 31, 2008 assets classified as held for sale include AMD 61,419 thousand (2007: AMD 57,214 thousand) repossessed assets and AMD 9,480 thousand (2007: AMD 10,350 thousand) assets out of use and held for sale.

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

In thousand Armenian drams	<b>Total</b>
<b>At January 1, 2007</b>	3,432
Reversal	(7,335)
Amounts written off	(4,274)
Recoveries	9,513
<b>At December 31, 2007</b>	1,336
Reversal	(1,944)
Amounts written off	(2,152)
Recoveries	3,272
<b>At December 31, 2008</b>	512

## 22 Amounts due to financial institutions

In thousand Armenian drams	<b>31.12.08</b>	31.12.07
Obligations of the CBA	<b>6,702,199</b>	3,953,157
Correspondent accounts of other banks	<b>237,728</b>	211,702
Current accounts of other financial institutions	<b>724,867</b>	781,406
Loans and deposits from financial institutions	<b>2,183,878</b>	152,581
Other amounts	<b>252,450</b>	761,440
<b>Total amounts due to financial institutions</b>	<b>10,101,122</b>	5,860,286

Obligations of CBA include loans received within the scope of “Small and medium business loan project” of German-Armenian fund in the amount of AMD 2,745,050 thousand (2007: 1,525,710 thousand) and amounts under repurchase agreements in the amount of AMD 3,957,149 thousand (2007: 2,427,447 thousand). See note 28.

All deposits from banks have fixed interest rates. Loans from financial institutions have variable interest rates.

During 2008, 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 2008, the Bank received an equivalent of AMD 92,019 thousand, including interests accrued (2007: 761,440 thousand) as deposits in dollars of Armenian financial institution, which relate to deposits granted to the same institution (See Note 16).

The Bank has not had any defaults of principal, interest or other breaches with respect to its borrowings during the year (2007: nil).

## 23 Amounts due to customers

In thousand Armenian drams	31.12.08	31.12.07
<b>Government of the RA</b>		
Current/Settlement accounts	57,184	194,776
Time deposits	1,481,185	931,922
Loans received	753,390	-
	<u>2,291,759</u>	<u>1,126,698</u>
<b>Corporate customers</b>		
Current/Settlement accounts	12,478,568	19,485,036
Time deposits	9,816,724	8,052,438
	<u>22,295,292</u>	<u>27,537,474</u>
<b>Retail customers</b>		
Current/Demand accounts	4,018,332	3,920,708
Time deposits	14,054,939	8,085,540
	<u>18,073,271</u>	<u>12,006,248</u>
<b>Total amounts due to customers</b>	<u><u>42,660,322</u></u>	<u><u>40,670,420</u></u>

All customer deposits carry fixed rates.

As at 31 December 2008 included in the time deposit payable to Government is AMD 1,481,185 thousand (2007: AMD 931,922 thousand), which was attracted under the World Bank projects on “Enterprise Development” and “Agricultural Reform”.

Loans received from RA government include loans received within the scope of “Small and medium business loan project” of German-Armenian fund in the amount of AMD 753,390 thousand (2007: nil)

As at 31 December 2008 included in amounts due to customers are deposits amounting to AMD 48,633 thousand (2007: AMD 86,241 thousand) held as security against guarantees issued. The fair value of those deposits approximates the carrying amount.

At 31 December 2008 the aggregate balance of top ten customers of the Bank (including related parties, see Note 31) amounts to AMD 20,274,089 thousand (2007: AMD 17,930,945 thousand) or 48% of total customer accounts (2007: 44%). The amount of top ten customers does not include amounts due to RA Government.

The Bank has not had any defaults of principal, interest or other breaches with respect to its borrowings during the year (2007: nil).

## 24 Debt securities issued

In thousand Armenian drams	31.12.08	31.12.07
Bonds	301,280	-
<b>Total debt securities issued</b>	<u><u>301,280</u></u>	<u><u>-</u></u>

As of December 31, 2008, the Bank has issued coupon bonds with an aggregate value of AMD 300,000 thousand with annual interest rate of 10.64% and a maturity of 36 months.

The Bank has not had any defaults of interest or other breaches with respect to its borrowings during the year.

## 25 Trading liabilities

In thousand Armenian drams	31.12.08	31.12.07
Securities borrowed from third parties	1,200,719	-
Securities borrowed under repurchase agreements	938,371	-
<b>Total other liabilities</b>	<b>2,139,090</b>	<b>-</b>

Repurchase agreements represent the unquoted debt securities that the Bank intends to buy back in the short term (See Note 16).

Included in the securities borrowed from third parties, securities at the amount of AMD 1,079,762 thousand represent the securities borrowed from a related party and repledged to the third parties (see notes 31).

## 26 Other liabilities

In thousand Armenian drams	31.12.08	31.12.07
Accounts payables	91,040	103,140
Tax payable, other than income tax	5,121	59,405
Revenues of future periods	19,267	46,380
Grants related to assets	47,810	52,931
Due to personnel	52,675	50,610
Due to on payment checks	72,919	109,457
Other	23,925	41,751
<b>Total other liabilities</b>	<b>312,757</b>	<b>463,674</b>

### Grants related to assets

In thousand Armenian drams	2008	2007
At January 1	52,931	-
Increase/(decrease)	(3,805)	58,880
Recognition of income	(1,316)	(5,949)
<b>At December 31</b>	<b>47,810</b>	<b>52,931</b>

## 27 Other provisions

The movement in other provisions was as follows:

In thousand Armenian drams	31.12.08	31.12.07
<b>At January 1</b>	<b>34,943</b>	<b>-</b>
Arising during the year	402	34,943
<b>At December 31</b>	<b>35,345</b>	<b>34,943</b>

Provisions have been made in respect of costs arising from guarantees.

## 28 Securities pledged under repurchase agreements

In thousand Armenian drams	Asset	31.12.08 Liability
Investment securities (Note 18,22)	3,944,502	3,957,149
	<u>3,944,502</u>	<u>3,957,149</u>

In thousand Armenian drams	Asset	31.12.07 Liability
Investment securities (Note 18,22)	2,427,799	2,427,447
	<u>2,427,799</u>	<u>2,427,447</u>

## 29 Equity

As at 31 December 2008 the Bank's registered and paid-in share capital was AMD 1,233,133 thousand. In accordance with the Bank's statutes, the share capital consists of 12,331 ordinary shares, all of which have a par value of AMD 100,000 each and of 333 privileged shares, all of which have a par value of AMD 100 each.

The respective shareholdings as at 31 December 2008 and 31 December 2007 may be specified as follows:

In thousand Armenian drams	Paid-in share capital	% of total paid-in capital
Advanced Global Investments LLC	1,171,400	95
Advanced Global Investments LLC (preference shares)	33	-
Saint Apostolic Church of Armenia	61,700	5
	<u>1,233,133</u>	<u>100</u>

As at 31 December 2008, 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.

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.

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 more than 50% of the Bank's share capital reported in statutory books.

### 30 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.

Management also believes that the ultimate liability, if any, arising from legal actions and complaints taken against the Bank, will not have a material adverse impact on the financial condition or results of future operations of the Bank.

Therefore, the Bank has not made any respective provision related to such tax and legal matters.

#### *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	31.12.08	31.12.07
Undrawn loan commitments	1,963,972	2,357,897
Letters of credit	63,533	367,302
Guarantees	3,534,508	3,494,316
<b>Total commitments and contingent liabilities</b>	<b>5,562,013</b>	<b>6,219,515</b>

#### *Operating lease commitments – Bank as a lessee*

In the normal course of business the Bank enters into other lease agreements for buildings and premises.

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

In thousand Armenian drams	31.12.08	31.12.07
Not later than 1 year	190,735	126,518
Later than 1 year and not later than 5 years	533,367	391,962
Later than 5 years	41,069	101,391
<b>Total operating lease commitments</b>	<b>765,171</b>	<b>619,871</b>

#### *Insurance*

Some of the Bank's assets are insured. Bank has currently obtained Comprehensive Insurance Policy (BBB) to safeguard it from errors, omissions and losses.

Starting June 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.

### 31 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 ultimate controlling party to Advanced Global Investments LLC is Argentinean businessman E. Eurnekian.

A number of banking transactions are entered into with related parties. These include loans, deposits and other transactions.

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	31.12.08		31.12.07	
	Shareholders	Key management personnel	Shareholders	Key management personnel
<b>Loans and advances to customers</b>				
Loans outstanding at January 1, gross	29,859	60,252	1,067	25,811
Loans issued during the year	1,380,151	274,501	73,938	242,833
Loan repayments during the year	(873,471)	(144,301)	(45,146)	(208,392)
Loans outstanding at December 31, gross	536,539	190,452	29,859	60,252
Less: allowance for loan impairment	(5,365)	(1,905)	(322)	(680)
<b>Loans outstanding at December 31</b>	<b>531,174</b>	<b>188,547</b>	<b>29,537</b>	<b>59,572</b>
Impairment charge for credit losses	5,043	1,225	311	422
Interest income on loans	22,051	5,912	923	6,404
<b>Amounts due to customers</b>				
Deposits at January 1	3,174,840	358,529	101,396	39,726
Deposits received during the year	243,523,041	1,208,493	7,701,388	36,082,107
Deposits repaid during the year	(230,889,455)	(1,108,134)	(4,627,944)	(35,763,304)
<b>Deposits at December 31</b>	<b>15,808,426</b>	<b>458,888</b>	<b>3,174,840</b>	<b>358,529</b>
Interest expense on deposits	224,507	3,682	62,119	14,053
<b>Borrowed securities</b>				
Borrowed securities at January 1	-	-	-	-
Borrowings received during the year	1,079,762	-	-	-
Borrowings repaid during the year	-	-	-	-
<b>Borrowed securities at December 31</b>	<b>1,079,762</b>	<b>-</b>	<b>-</b>	<b>-</b>
Interest expense on borrowings	158	-	-	-
Guarantees received	-	-	-	44,986
<b>Income statement items</b>				
Fee and commission income	14,379	100	6,632	2,893
Other income	1,623	23,650	75,695	14,761
Other expenses	1,463	22,433	11,134	3,631

The loans issued to directors and other key management personnel (and close family members) have maturity from 3 months to 15 years and have interest rates of 7-24% (2007: 7-24%). The loans advanced to the directors are collateralised by gold, real estate, cash.

Compensation of key management personnel was comprised of the following:

In thousand Armenian drams	<b>31.12.08</b>	31.12.07
Salaries and other short-term benefits	<b>220,941</b>	65,147
Social security costs	<b>23,623</b>	4,092
<b>Total key management compensation</b>	<b>244,564</b>	69,239

### 32 Fair value of financial instruments

#### *Financial instruments not measured at fair value*

In thousand Armenian drams	2008		2007	
	Carrying value	Fair value	Carrying value	Fair value
<b>FINANCIAL ASSETS</b>				
Cash and balances with CBA	<b>12,467,281</b>	<b>12,467,281</b>	11,214,519	11,214,519
Amounts due from financial institutions	<b>5,171,616</b>	<b>5,171,616</b>	5,280,880	5,280,880
Loans and advances to customers	<b>42,658,156</b>	<b>42,658,156</b>	30,177,025	30,177,025
<b>FINANCIAL LIABILITIES</b>				
Amounts due to financial institutions	<b>10,101,122</b>	<b>10,101,122</b>	5,860,286	5,860,286
Amounts due to customers	<b>42,660,322</b>	<b>42,660,322</b>	40,670,420	40,670,420
Debt securities issued	<b>301,280</b>	<b>301,280</b>	-	-

#### *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. Fair value approximates carrying amounts as interest rates applicable reflect 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. Fair value approximates carrying amounts as current interest rates for new instruments reflect interest rate for instruments originated previously.

#### *Other borrowings*

The estimated fair value of fixed interest-bearing deposits is based on discounted cash flows using interest rates for new debts with similar remaining maturity. Fair value approximates carrying amounts as current interest rates for new instruments reflect interest rate for instruments originated previously.

### 33 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 34.3 for the Bank's contractual undiscounted repayment obligations.

In thousand Armenian drams								31.12.08
	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
<b>ASSETS</b>								
Cash and balances with CBA	12,255,271	-	-	12,255,271	212,010	-	212,010	12,467,281
Trading securities	-	7,558	-	7,558	51,114	-	51,114	58,672
Amounts due from other financial institutions	5,129,351	-	11,592	5,140,943	30,673	-	30,673	5,171,616
Loans and advances to customers	4,306,047	4,059,511	12,647,729	21,013,287	12,328,686	9,316,183	21,644,869	42,658,156
Investments available for sale	7,674	5,063	24,702	37,439	415,938	218,554	634,492	671,931
Securities pledged under repurchase agreements	3,944,502	-	-	3,944,502	-	-	-	3,944,502
	<u>25,642,845</u>	<u>4,072,132</u>	<u>12,684,023</u>	<u>42,399,000</u>	<u>13,038,421</u>	<u>9,534,737</u>	<u>22,573,158</u>	<u>64,972,158</u>
<b>LIABILITIES</b>								
Amounts due to financial institutions	5,203,408	333,718	3,015,723	8,552,849	1,548,273	-	1,548,273	10,101,122
Amounts due to customers	19,104,045	2,091,375	16,566,793	37,762,213	4,294,807	603,302	4,898,109	42,660,322
Debt securities issued	-	-	-	-	301,280	-	301,280	301,280
Trading liabilities	2,139,090	-	-	2,139,090	-	-	-	2,139,090
	<u>26,446,543</u>	<u>2,425,093</u>	<u>19,582,516</u>	<u>48,454,152</u>	<u>6,144,360</u>	<u>603,302</u>	<u>6,747,662</u>	<u>55,201,814</u>
<b>Net position</b>	<u>(803,698)</u>	<u>1,647,039</u>	<u>(6,898,493)</u>	<u>(6,055,152)</u>	<u>6,894,061</u>	<u>8,931,435</u>	<u>15,825,496</u>	<u>9,770,344</u>
<b>Accumulated gap</b>	<u>(803,698)</u>	<u>843,341</u>	<u>(6,055,152)</u>		<u>838,909</u>	<u>9,770,344</u>		

In thousand Armenian drams								31.12.07
	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
<b>ASSETS</b>								
Cash and balances with CBA	11,104,519	-	-	11,104,519	-	110,000	110,000	11,214,519
Trading securities	390,801	82,261	129,427	602,489	53,312	78,860	132,172	734,661
Amounts due from other financial institutions	5,116,255	-	134,203	5,250,458	30,422	-	30,422	5,280,880
Loans and advances to customers	1,293,909	2,665,821	10,842,333	14,802,063	13,526,709	1,848,253	15,374,962	30,177,025
Investments available for sale	134,604	1,575,497	345,629	2,055,730	2,110,496	348,465	2,458,961	4,514,691
Securities pledged under repurchase agreements	-	2,427,799	-	2,427,799	-	-	-	2,427,799
	<u>18,040,088</u>	<u>6,751,378</u>	<u>11,451,592</u>	<u>36,243,058</u>	<u>15,720,939</u>	<u>2,385,578</u>	<u>18,106,517</u>	<u>54,349,575</u>
<b>LIABILITIES</b>								
Amounts due to financial institutions	3,569,034	-	538,900	4,107,934	1,706,719	45,633	1,752,352	5,860,286
Amounts due to customers	29,339,489	2,244,754	5,888,762	37,473,005	3,189,233	8,182	3,197,415	40,670,420
	<u>32,908,523</u>	<u>2,244,754</u>	<u>6,427,662</u>	<u>41,580,939</u>	<u>4,895,952</u>	<u>53,815</u>	<u>4,949,767</u>	<u>46,530,706</u>
<b>Net position</b>	<u>(14,868,435)</u>	<u>4,506,624</u>	<u>5,023,930</u>	<u>(5,337,881)</u>	<u>10,824,987</u>	<u>2,331,763</u>	<u>13,156,750</u>	<u>7,818,869</u>
<b>Accumulated gap</b>	<u>(14,868,435)</u>	<u>(10,361,811)</u>	<u>(5,337,881)</u>		<u>5,487,106</u>	<u>7,818,869</u>		

### 34 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 Risk Management and Monitoring Department under policies approved by the Board of Directors. The Risk Management and Monitoring Department 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.

#### 34.1 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 Credit Committee and reported to the Board of Directors regularly.

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

The table below represents a worst case scenario of credit risk exposure to the Bank at 31 December 2008 and 31 December 2007, 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		Gross maximum exposure as of December 31, 2008	Gross maximum exposure as of December 31, 2007
	Notes		
Balances with CBA	14	8,489,935	7,440,280
Trading securities	15	58,672	734,661
Amounts due from other financial institutions	16	5,171,616	5,280,880
Loans and advances to customers	17	42,658,156	30,177,025
Investments available for sale	18	671,931	4,514,691
Securities pledged under repurchase agreements	28	3,944,502	2,427,799
<b>Total</b>		<b>60,994,812</b>	<b>50,575,336</b>
Commitments and contingent liabilities	30	5,562,013	6,219,515
<b>Total credit risk exposure</b>		<b>66,556,825</b>	<b>56,794,851</b>

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.

### 34.1.2 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 December 31 2008 and 31 December 2007.

In thousand Armenian drams	Armenia	OECD countries	Other non-OECD countries	Total
Balances with CBA	8,489,935	-	-	8,489,935
Trading securities	58,672	-	-	58,672
Amounts due from other financial institutions	2,786,462	2,288,851	96,303	5,171,616
Loans and advances to customers	42,530,309	17,454	110,393	42,658,156
Investments available for sale	525,780	146,151	-	671,931
Securities pledged under repurchase agreements	3,944,502	-	-	3,944,502
<b>As at 31 December 2008</b>	<b>58,335,660</b>	<b>2,452,456</b>	<b>206,696</b>	<b>60,994,812</b>
As of 31 December 2007	46,383,690	3,125,258	1,066,388	50,575,335

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 December 31 2008 and 31 December 2007.

In thousand Armenian drams	Financial institutions	Manufacturing	Trade	Construction	State sector	Consumer sector	Service	Other	Total
Balances with CBA	8,489,935	-	-	-	-	-	-	-	8,489,935
Trading securities	-	-	-	-	58,672	-	-	-	58,672
Amounts due from other financial institutions	5,171,616	-	-	-	-	-	-	-	5,171,616
Loans and advances to customers	-	6,453,304	13,326,330	4,489,218	4,904	14,788,642	738,555	2,857,203	42,658,156
Investments available for sale	171,864	51,804	322,543	21,876	50,781	-	53,063	-	671,931
Securities pledged under repurchase agreements	3,944,502	-	-	-	-	-	-	-	3,944,502
<b>As of December 31, 2008</b>	<b>17,777,917</b>	<b>6,505,108</b>	<b>13,648,873</b>	<b>4,511,094</b>	<b>114,357</b>	<b>14,788,642</b>	<b>791,618</b>	<b>2,857,203</b>	<b>60,994,812</b>
As of December 31, 2007	15,177,723	6,329,620	7,986,627	1,782,476	4,956,383	9,656,554	1,030,090	3,655,863	50,575,336

### 34.1.3 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 Credit Committee.

The exposure to any one borrower including banks and financial organizations is further restricted by sub-limits covering on- and off-balance sheet exposures.

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, equipment, inventory and vehicles.

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	31.12.08	31.12.07
Loans collateralized by real estate	32,528,024	18,231,796
Loans collateralized by vehicles	3,562,448	2,484,040
Loans collateralized by guarantees of enterprises	58,462	12,169
Loans collateralized by inventories	834,689	641,648
Loans collateralized by equipment	1,344,980	4,071,003
Loans collateralized by cash	185,723	239,229
Loans collateralized by shares of other companies	144,669	89,657
Other collateral	4,170,160	3,546,378
Unsecured loans	457,000	1,002,631
Accrued interest	284,328	202,841
<b>Total loans and advances to customers (gross)</b>	<b>43,570,483</b>	<b>30,521,392</b>

#### *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.

#### **34.1.4 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 or 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	31.12.08	31.12.07
Loans and advances to customers		
State owned enterprises	1.00%	1.00%
Privately held companies	1.72%	1.08%
Individuals	1.09%	1.13%
Sole proprietors	1.10%	1.15%

As of 31.12.08 and 31.12.07 the Bank has not had any losses on other financial assets bearing credit risk.

*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					31.12.08
	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	56,915	28,382	129,030	21,606	235,933
Individuals	24,727	22,421	9,254	18,368	74,770
Sole proprietors	4,329	4,779	1,636	779	11,523
<b>Total</b>	<b>85,971</b>	<b>55,582</b>	<b>139,920</b>	<b>40,753</b>	<b>322,226</b>

In thousand Armenian drams					31.12.07
	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	7,011	468	466	1,072	9,017
Individuals	123,718	2,103	480	8,586	134,887
Sole proprietors	34,646	-	-	1,867	36,513
<b>Total</b>	<b>165,375</b>	<b>2,571</b>	<b>946</b>	<b>11,525</b>	<b>180,417</b>

The fair value of collateral that the Bank holds relating to past due loans at 31 December 2008 amounts to AMD 7,771,416 thousand (2007: AMD 436,953 thousand). The collateral consists of real estate 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 2,476,893 thousand (2007: AMD 1,117,898 thousand). Refer to Note 17. The fair value of collateral that the Bank holds relating to loans individually determined to be impaired at 31 December 2008 amounts to AMD 3,228,041 thousand (2007: AMD 2,448,000 thousand). The collateral consists of real estate, inventory and properties.

### 34.2 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 methodology which reflects the interdependency between specific and general interest risk variables. Non-trading positions are managed and monitored using other sensitivity analyses.

### 34.2.1 Market risk – Trading

The Bank uses Basel II interest rate measurement methods and approaches to measure the risk of its securities held for trading. The method defines interest rate risk as the sum of specific and general interest rate risks.

To measure the interest rate risk the net positions in debt securities are calculated against the groups based on the following principles. To be included in the same group the securities must meet all of the following criteria:

- be issued by the same entity,
- expressed in the same currency,
- bear the same interest rate, or at maximum having a difference in interest rates of 0.2 interest points.

#### *Measurement of specific interest rate risk*

To measure the specific interest rate risk the positions of debt securities are calculated first. After which the gross position in debt securities is measured. In calculation of the gross position the debt securities are weighted according to the following classes:

- state debt securities
- reliable debt securities
- other debt securities

#### *Measurement of general interest rate risk*

To measure the general interest rate risk the positions in debt securities are calculated first as well. The gross net position in net securities is calculated as the difference between the sum of long positions in debt securities and sum of short positions in debt securities (in absolute terms). After the positions in debt securities are calculated the long or short positions debt securities are divided and weighted according to their remaining maturity. The minimal position in debt securities for each maturity band is defined as the minimal amount of the sum of all long and short positions (in absolute terms). Depending on the maturity all securities are divided into appropriate zones.

The general interest rate risk for a given day is the sum of the following:

- 10% of minimal position of each maturity band
- 40% of minimal position of the first zone
- 30% of minimal position of the second zone
- 30% of minimal position of the third zone
- 40% of minimal positions between the first and second zones
- 40% of minimal positions between the second and third zones
- 150% of minimal positions between the first and third zones
- 100% of the gross net position of debt securities.

On the days when there were no changes in the Bank's balance sheet (including non-working days) the daily data is based on the previous day's data.

The Banks' exposure to interest rate risk on its' trading portfolio is presented below:

In thousand Armenian drams	Specific risk	General risk	Total risk on trading portfolio
<b>As of December 31, 2008</b>	<b>1,173</b>	<b>2,499</b>	<b>3,672</b>
As of December 31, 2007	6,705	19,063	25,768

### 34.2.2 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.

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 2008. The sensitivity of equity is calculated by revaluating fixed rate available-for-sale financial assets at 31 December 2008 for the effects of the assumed changes in interest rates. The sensitivity of equity is analysed by maturity of the asset. The total sensitivity of equity is based on the assumption that there are parallel shifts in the yield curve.

In thousand Armenian drams		Sensitivity of equity					31.12.08
Currency	Change in basis points	Sensitivity of net interest income	Up to 6 months	6 months to 1 year	1 year to 5 years	More than 5 years	Total
AMD	+1%	-	2	4	40	-	46
USD	+1%	8	-	-	-	-	8
AMD	-1%	-	(2)	(4)	(40)	-	(46)
USD	-1%	(8)	-	-	-	-	(8)

In thousand Armenian drams		Sensitivity of equity					31.12.07
Currency	Change in basis points	Sensitivity of net interest income	Up to 6 months	6 months to 1 year	1 year to 5 years	More than 5 years	Total
AMD	+1%	-	108	12	46	18	184
USD	+1%	30	-	-	-	-	30
AMD	-1%	-	(108)	(12)	(46)	(18)	(184)
USD	-1%	(30)	-	-	-	-	(30)

#### *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.

The tables below indicate the currencies to which the Bank had significant exposure at 31 December 2008 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 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.

Currency	31.12.08		31.12.07	
	Change in currency rate in %	Effect on profit before tax	Change in currency rate in %	Effect on profit before tax
USD	+ 20	(105,028)	+ 5	29,487
USD	- 20	105,028	- 5	(29,487)
EUR	+ 32	(7,204)	+ 8	(6,393)
EUR	- 32	7,204	- 8	6,393

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

In thousand Armenian drams	Armenian Dram	Freely convertible currencies	Non-freely convertible currencies	Total
<b>ASSETS</b>				
Cash and balances with the CBA	7,037,243	5,094,564	335,474	12,467,281
Trading securities	58,672	-	-	58,672
Amounts due from other financial institutions	2,300,025	2,282,646	588,945	5,171,616
Loans and advances to customers	24,743,226	17,914,930	-	42,658,156
Investments available for sale	671,931	-	-	671,931
Securities pledged under repurchase agreements	3,944,502	-	-	3,944,502
	<b>38,755,599</b>	<b>25,292,140</b>	<b>924,419</b>	<b>64,972,158</b>
<b>LIABILITIES</b>				
Amounts due to financial institutions	7,559,322	2,455,154	86,646	10,101,122
Amounts due to customers	17,953,442	24,456,907	249,973	42,660,322
Debt securities issued	301,280	-	-	301,280
Trading liabilities	2,139,090	-	-	2,139,090
	<b>27,953,134</b>	<b>26,912,061</b>	<b>336,619</b>	<b>55,201,814</b>
<b>Net position as of 31 December 2008</b>	<b>10,802,465</b>	<b>(1,619,921)</b>	<b>587,800</b>	<b>9,770,344</b>
<b>Commitments and contingent liabilities as of 31 December 2008</b>	<b>4,403,145</b>	<b>1,129,526</b>	<b>29,342</b>	<b>5,562,013</b>
Total financial assets	34,807,185	18,416,960	1,125,430	54,349,575
Total financial liabilities	28,493,906	17,072,315	964,485	46,530,706
Net position as of 31 December 2007	6,313,279	1,344,645	160,945	7,818,869
Commitments and contingent liabilities as of 31 December 2007	4,368,375	1,851,140	-	6,219,515

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.

### 34.3 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. 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 14. 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 in accordance with the requirement of the Central Bank of Armenia.

The table below summarises the maturity profile of the Bank's financial liabilities at 31 December 2008 based on contractual undiscounted repayment obligations. See note 33 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

31.12.08

	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
<b>FINANCIAL LIABILITIES</b>						
Amounts due to financial institutions	5,203,408	333,718	3,015,723	1,548,273	-	10,101,122
Amounts due to customers	15,282,636	5,912,184	13,820,026	7,042,174	603,302	42,660,322
Debt securities issued	-	-	-	301,280	-	301,280
Trading liabilities	938,371	-	1,200,719	-	-	2,139,090
<b>Total undiscounted financial liabilities</b>	<b>21,424,415</b>	<b>6,245,902</b>	<b>18,036,468</b>	<b>8,891,727</b>	<b>603,302</b>	<b>55,201,814</b>
<b>Commitments and contingent liabilities</b>	<b>187,418</b>	<b>500,213</b>	<b>3,750,364</b>	<b>1,124,018</b>	<b>-</b>	<b>5,562,013</b>

In thousand Armenian drams							31.12.07
	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	
<b>FINANCIAL LIABILITIES</b>							
Amounts due to financial institutions	3,597,462	-	538,900	764,680	959,244	5,860,286	
Amounts due to customers	23,263,885	3,861,509	5,736,106	5,650,471	2,158,449	40,670,420	
<b>Total undiscounted financial liabilities</b>	<b>26,861,347</b>	<b>3,861,509</b>	<b>6,275,006</b>	<b>6,415,151</b>	<b>3,117,693</b>	<b>46,530,706</b>	
<b>Commitments and contingent liabilities</b>	<b>2,349,614</b>	<b>318,044</b>	<b>2,063,012</b>	<b>1,488,845</b>	<b>-</b>	<b>6,219,515</b>	

### 35 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.

The minimum ratio between total capital and risk weighted assets required by the Central Bank of Armenia is 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.

The risk-weighted assets are measured by means of a hierarchy of risk weights classified according to the nature of and reflecting an estimate of credit, market and operating risks.

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

The Central Bank of Armenia has set the minimal required total capital at AMD 5,000,000 thousand from January 1 2009.

### 36 Subsequent events

On March 3, 2009 the Central Bank of Armenia has decided to go to floating exchange rate of Armenian Dram against US dollar and other freely convertible currencies. This change has affected the exchange rate risk and financial position of the Bank in 2009 due to the fact that most of the debts of the Bank are denominated in those currencies. Refer to note 34.2.2 for the exchange rate risk of the Bank as of December 31, 2008.

On March 5, 2009 the following exchange rates were formed:

AMD/1USD	<b>366.38</b>
AMD/1EUR	<b>460.39</b>

### 37 Segment reporting

The Bank's primary format for reporting segment information is business segments and the secondary format is geographical segments.

#### *Business segments*

The Bank is organised on the basis of three main business segments:

Retail banking – representing provisioning of transactional banking services, accounts, deposits, debit and credit cards, overdrafts, consumer finance, mortgages, car and other loans to personal customers.

Corporate banking – representing provisioning of transactional banking services, accounts, deposits, corporate cards, overdrafts, guarantees, Letters of Credit, loans and other credit facilities to commercial entities and private entrepreneurs.

Financial Markets – representing investments and trading in securities, foreign exchange and money market transactions with banks and non-bank financial institutions, bond issuance and underwriting.

Transactions between the business segments are based on normal commercial terms and conditions. Funds are ordinarily reallocated between segments, resulting in funding cost transfers disclosed in operating income. Interest charged for these funds is based on the Bank's cost of funds).

There are no other material items of income or expense between the business segments. Segment assets and liabilities comprise operating assets and liabilities, being the majority of the balances sheet, but excluding items such as taxation and borrowings. Internal charges and transfer pricing adjustments have been reflected in the performance of each business. Revenue sharing agreements are used to allocate external customer revenues to a business segment on a reasonable basis.

Segment information about these businesses is presented below.

In thousand Armenian drams					<b>2008</b>
	<b>Retail banking</b>	<b>Corporate banking</b>	<b>Financial markets</b>	<b>Unallocated</b>	<b>Total</b>
Revenues	4,896,243	4,628,317	745,562	-	10,270,122
Costs and expenses	(3,180,801)	(2,965,605)	(1,215,709)	(503,651)	(7,865,766)
Profit before tax	1,715,442	1,662,712	(470,147)	(503,651)	2,404,356
Income tax expense				(560,305)	(560,305)
Profit for the year	1,715,442	1,662,712	(470,147)*	(1,063,956)	1,844,051
Total assets	20,026,902	23,267,175	20,936,308	4,999,114	69,229,499
Total liabilities	18,016,572	24,210,251	14,061,570	-	56,288,393
Capital expenditure	-	-	-	(173,684)	(173,684)
Depreciation expense	-	-	-	(503,652)	(503,652)
Impairment losses recognised during the year in the statement of income	(318,921)	(199,954)	(69,226)	-	(590,464)

\* Interest expense for funds attracted under specific projects are charged to Financial Markets, as a wholesale borrower, whilst interest income from allocation of these funds are contributed to Retail and Commercial banking, resulting in negative Profit before Tax for Financial Markets segment.

In thousand Armenian drams					2007
	Retail banking	Corporate banking	Financial markets	Unallocated	Total
Revenues	2,841,809	3,070,028	594,591	-	6,506,428
Costs and expenses	(1,900,207)	(1,685,325)	(668,858)	(453,974)	(4,708,365)
Profit before tax	941,602	1,384,703	(74,267)	(453,974)	1,798,063
Income tax expense	-	-	-	(390,622)	(390,622)
Profit for the year	941,602	1,384,703	(74,267)	(844,596)	1,407,441
Total assets	12,937,104	17,387,172	24,247,594	4,019,331	58,591,201
Total liabilities	12,166,396	29,256,204	6,143,155	-	47,565,755
Capital expenditure	-	-	-	(137,114)	(137,114)
Depreciation expense	-	-	-	(453,975)	(453,975)
Impairment losses recognised during the year in the statement of income	(68,870)	(46,412)	(20,456)	-	(135,738)

### Geographical segments

Segment information for the main geographical segments of the Bank is set out below:

In thousand Armenian drams				2008
	Armenia	OECD countries	Other non-OECD countries	Total
External revenues	9,474,397	705,552	90,173	10,270,122
Assets	66,312,068	2,634,195	283,236	69,229,499
Liabilities	33,848,243	3,595,487	18,844,663	56,288,393
Capital expenditure	173,684	-	-	173,684

In thousand Armenian drams				2007
	Armenia	OECD countries	Other non-OECD countries	Total
External revenues	5,939,126	501,199	66,103	6,506,428
Assets	54,413,297	3,167,860	1,010,044	58,591,201
Liabilities	38,878,231	4,004,180	4,683,344	47,565,755
Capital expenditure	137,114	-	-	137,114

External revenues, assets, liabilities and credit related commitments have generally been allocated based on domicile of the counterparty. Tangible assets (cash on hand, premises and equipment) have been allocated based on the country in which they are physically held.

