

Financial Statements and Independent Auditor's  
Report

Converse Bank closed joint stock company

31 December 2009

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Grant Thornton

## 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 statement of financial position as at December 31, 2009, and the statement of comprehensive income, statement of changes in equity and statement of cash flows 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.



## Statement of comprehensive income

In thousand Armenian drams	Notes	Year ended December 31, 2009	Year ended December 31, 2008
Interest and similar income	6	6,902,601	5,992,854
Interest and similar expense	6	(3,211,028)	(2,184,769)
<b>Net interest income</b>		<b>3,691,573</b>	<b>3,808,085</b>
Fee and commission income	7	1,184,586	1,312,720
Fee and commission expense	7	(320,496)	(300,699)
<b>Net fee and commission income</b>		<b>864,090</b>	<b>1,012,021</b>
Net trading income	8	1,094,993	1,500,548
Gains less losses on investments available for sale		101,935	177,935
Other income	9	158,602	284,069
Impairment charge for credit losses	10	(2,363,961)	(588,101)
Impairment losses on investments available-for sale		-	(2,363)
Foreign currency translation net loss of non-trading assets and liabilities	11	(711,085)	(307,872)
Staff costs	12	(1,813,606)	(1,802,392)
Depreciation of property and equipment	20	(576,469)	(488,576)
Amortization of intangible assets	21	(31,953)	(15,076)
Other expenses	13	(1,539,764)	(1,173,922)
<b>Profit/(loss) before income tax</b>		<b>(1,125,645)</b>	<b>2,404,356</b>
Income tax (expense)/benefit	14	99,416	(560,305)
<b>Profit/(loss) for the year</b>		<b>(1,026,229)</b>	<b>1,844,051</b>
<b>Other comprehensive income:</b>			
Net unrealized gains/(loss) from changes in fair value		(136,156)	65,841
Net losses realized to net profit/(loss) on disposal of available-for-sale instruments		11,005	23,412
Income tax relating to components of other comprehensive income		483,216	(17,644)
<b>Other comprehensive income for the year, net of tax</b>		<b>358,065</b>	<b>71,609</b>
<b>Total comprehensive income/(expense) for the year</b>		<b>(668,164)</b>	<b>1,915,660</b>

The accompanying notes on pages 7 to 53 are an integral part of these financial statements.

# Statement of financial position

In thousand Armenian drams	Notes	As of December 31, 2009	As of December 31, 2008
<b>ASSETS</b>			
Cash and balances with CBA	15	17,361,232	12,467,281
Financial assets at fair value through profit or loss	16	275,915	58,672
Amounts due from other financial institutions	17	10,586,270	5,171,616
Loans and advances to customers	18	41,127,384	42,658,156
Investments available for sale	19	2,258,481	671,931
Securities pledged under repurchase agreements	29	2,323,985	3,944,502
Property, plant and equipment	20	3,711,424	3,886,295
Intangible assets	21	281,394	103,340
Deferred income tax assets	14	109,641	-
Prepaid income taxes		278,106	-
Other assets	22	341,924	267,706
<b>TOTAL ASSETS</b>		<b>78,655,756</b>	<b>69,229,499</b>
<b>LIABILITIES AND EQUITY</b>			
<b>Liabilities</b>			
Amounts due to financial institutions	23	9,314,811	10,101,122
Amounts due to customers	24	56,440,073	42,660,322
Debt securities issued	25	301,312	301,280
Trading liabilities	26	-	2,139,090
Current income tax liabilities		-	265,486
Deferred income tax liabilities	14	-	472,991
Other liabilities	27	308,317	312,757
Other provisions	28	18,301	35,345
<b>Total liabilities</b>		<b>66,382,814</b>	<b>56,288,393</b>
<b>Equity</b>			
Share capital	30	1,233,133	1,233,133
Share premium		63,233	63,233
Statutory general reserve		648,183	648,183
Other reserves		2,050,344	1,862,068
Retained earnings		8,278,049	9,134,489
<b>Total equity</b>		<b>12,272,942</b>	<b>12,941,106</b>
<b>TOTAL LIABILITIES AND EQUITY</b>		<b>78,655,756</b>	<b>69,229,499</b>

The financial statements from pages 3 to 53 were signed by the Bank's Executive Director and Chief Accountant on 05 March 2010. The accompanying notes on pages 7 to 53 are an integral part of these financial statements.

T. DAVTYAN  
Executive 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
<b>Balance as of January 1, 2008</b>	1,233,133	63,233	648,183	(13,781)	1,940,071	7,154,607	11,025,446
Profit for the year	-	-	-	-	-	1,844,051	1,844,051
<b>Other comprehensive income:</b>							
Adjustment to revaluation reserve on depreciation 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
Income tax relating to components of other comprehensive income	-	-	-	(17,644)	-	-	(17,644)
Total comprehensive income for the year	-	-	-	71,609	(135,831)	1,979,882	1,915,660
<b>Balance as of December 31, 2008</b>	<b>1,233,133</b>	<b>63,233</b>	<b>648,183</b>	<b>57,828</b>	<b>1,804,240</b>	<b>9,134,489</b>	<b>12,941,106</b>
Loss for the year	-	-	-	-	-	(1,026,229)	(1,026,229)
<b>Other comprehensive income:</b>							
Adjustment to revaluation reserve on depreciation of PPE	-	-	-	-	(169,789)	169,789	-
Net unrealized loss from changes in fair value	-	-	-	(136,156)	-	-	(136,156)
Net losses realized to net loss on disposal of available-for-sale instruments	-	-	-	11,005	-	-	11,005
Income tax relating to components of other comprehensive income	-	-	-	23,668	459,548	-	483,216
Total comprehensive income/(expense) for the year	-	-	-	(101,483)	289,759	(856,440)	(668,164)
<b>Balance as of December 31, 2009</b>	<b>1,233,133</b>	<b>63,233</b>	<b>648,183</b>	<b>(43,655)</b>	<b>2,093,999</b>	<b>8,278,049</b>	<b>12,272,942</b>

## Statement of cash flows

In thousand Armenian drams	Year ended December 31,2009	Year ended December 31,2008
<b>Cash flows from operating activities</b>		
Interest received	6,982,349	5,982,209
Interest paid	(2,849,548)	(1,625,070)
Fees and commissions received	1,184,586	1,312,720
Fees and commissions paid	(317,813)	(298,598)
Gains less losses from trading securities	(46,809)	(3,151)
Realised gains less losses from dealing in foreign currencies	1,158,856	1,506,614
Other income received	151,507	134,876
Recovery of previously written off loans	50,696	57,301
Salaries and benefits paid	(1,808,065)	(1,805,232)
Other operating expenses paid	(1,681,897)	(1,162,285)
<b>Cash flows from operating activities before changes in operating assets and liabilities</b>	<b>2,823,862</b>	<b>4,099,384</b>
<i>Net (increase)/decrease in operating assets</i>		
Deposited funds in the CBA	(309,059)	(102,010)
Amounts due from other financial institutions	(2,159,828)	(1,960,621)
Loans and advances to customers	3,140,283	(12,961,492)
Other assets	(185,531)	(27,432)
<i>Increase/(decrease) in operating liabilities</i>		
Amounts due to financial institutions	(87,979)	871,170
Amounts due to customers	6,790,550	1,799,772
Trading liabilities	(2,138,932)	2,139,090
Other liabilities	(272,492)	(102,915)
<b>Net cash flow from operating activities before income tax</b>	<b>7,600,874</b>	<b>(6,245,054)</b>
Income tax paid	(433,952)	(375,904)
<b>Net cash from operating activities</b>	<b>7,166,922</b>	<b>(6,620,958)</b>
<b>Cash flows from investing activities</b>		
(Purchase)/sale of investment securities	(1,656,614)	3,886,595
Dividends received	7,095	504
Purchase of property, equipment and intangible assets	(617,910)	(500,131)
Proceeds from sale of property, equipment and intangible assets	6,156	12,881
<b>Net cash used in investing activities</b>	<b>(2,261,273)</b>	<b>3,399,849</b>
<b>Cash flow from financing activities</b>		
Loans received/(redeemed) from financial institutions	(1,239,640)	3,055,339
Debt securities issued	-	300,000
<b>Net cash flow from financing activities</b>	<b>(1,239,640)</b>	<b>3,355,339</b>
<b>Net increase in cash and cash equivalents</b>	<b>3,666,009</b>	<b>134,230</b>
Cash and cash equivalents at the beginning of the year	14,429,224	14,755,899
Effect of exchange rate changes on cash and cash equivalents	2,771,683	(460,905)
<b>Cash and cash equivalents at the end of the year (Note 15)</b>	<b>20,866,916</b>	<b>14,429,224</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, regional instability and international economic crisis.

The international economic crisis led to shortage of RA GDP, as well as the cash flow transfers from abroad upon which the economy of Armenia is significantly dependant. Though the RA Government and the CBA have undertaken a number of preventing procedures, still there are uncertainties on the capital availability and acquisition cost both for the Bank and for its customers, and in times of more severe market stress the effects of the crisis may be significant both for the Armenian economy and for the Bank. However, 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, which might have been considered necessary.

## **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 of the Republic of Armenia and 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 Changes in accounting policies**

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, 2009. The standards and interpretations which have had effect on the financial statements are presented below:

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

The Bank applies revised IAS 1 Presentation of Financial Statements (2007), which became effective as of 1 January 2009. The amendment has introduced terminology changes (including revised titles for the financial statements) and changes in the format and content of the financial statements. This standard affects the presentation of owner changes in equity and introduces a statement of comprehensive income. The Bank chooses the present income and expense and components of other comprehensive income in a single statement of comprehensive income with subtotals. The adoption of the standard does not affect the financial position or profits of the Bank, but gives rise to additional disclosures.

Comparative information has been re-presented so that it also is in conformity with the revised standard. Since the change in accounting policy only impacts presentation aspects, there is no impact on earnings per share.

#### *IFRS 7 (Amendment) 7 Financial Instruments: Disclosures* (effective from January 1, 2009)

The Bank has implemented the improvements made to IFRS 7 in March 2009. The effective date of the amendments is 1 January 2009. The amendments extend and specify the disclosures for the fair value of financial instruments and liquidity risk (see note 33.1). The Bank selected not to provide comparative information for these expanded disclosures in the current year, in accordance with transitional relieves offered in these amendments.

### IFRS 8 *Operating Segments*

This year the Bank adopted IFRS 8 Operating Segments, which replaces IAS 14 Segment Reporting. The standard is applied retrospectively. The accounting policy for identifying segments is now based on internal management reporting information that is regularly reviewed by the chief operating decision maker. In contrast, IAS 14 required the Bank to identify two sets of segments (primary and secondary) based on risks and rewards of the operating segments. However the adoption IFRS 8 has not changed significantly the disclosures being made under IAS 14. It resulted in the disclosures for geographic areas being made only for revenues from external customers and non-current assets other than financial instruments, deferred tax assets, post-employment benefit assets, and rights arising under insurance contracts. Refer to note 37 for the new format of disclosures.

### **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. At the moment in management's estimation their possible effect on the Bank's financial statements can not be material.

### IFRS 2(Amendment) *Share-based payment-Group Cash-settled Share-based Payment Transactions*

The main purpose of the Amendments to IFRS 2 is to specify the accounting, in the financial statements of an entity that receives goods or services from its suppliers (including employees), for similar arrangements that are share-based and cash-settled when the entity itself does not have any obligation to make the required payments to its suppliers. IFRS 2 (Amendment) will be applied retrospectively for annual periods beginning on or after 1 January 2010.

### IFRS 3 *Business Combinations* (revised 2008)

This standard is applicable for business combinations occurring in reporting periods beginning on or after July 1, 2009 and will be applied prospectively. The new standard introduces changes to the accounting requirements for business combinations, but still requires the use of the purchase method, and will have a significant effect on business combinations occurring in reporting periods beginning on or after July 1, 2009.

### IAS 27 *Consolidated and Separate Financial Statements* (revised 2008)

The revised standard introduces changes to the accounting requirements for the loss of control of a subsidiary and for changes in the entity's interest in subsidiaries.

### IAS 32 (Amendment) *Financial instruments: Presentation-Classification of Right Issues*

The Amendment alters IAS 32 *Financial Instruments: Presentation* so that rights, options or warrants to acquire a fixed number of the entity's own equity instruments for a fixed amount of any currency are equity instruments if the entity offers the rights, options or warrants pro rata to all of its existing owners of the same class of its own (non-derivative) equity instruments. Prior to the Amendment, rights issues denominated in a foreign currency 'failed' equity classification and were required to be accounted for as derivative liabilities. IAS 32 (Amendment) will be applied retrospectively for annual periods beginning on or after 1 February 2010.

*IAS 39(Amendment) Financial Instruments: Recognition and Measurement-Eligible hedged items*

The final amendments addressed only the designation of a one-sided risk in a hedged item, and the designation of inflation as a hedged risk or portion in particular situation. The amendment clarifies that an entity is permitted to designate a portion of the fair value changes or cash flow variability of a financial instrument as a hedged item. (effective from July 1, 2009).

Amendments to IFRIC 9 and IAS 39-*Embedded derivatives*. (effective from July 1, 2009).

The Amendment is consequential upon the changes made to IAS 39 in October and November 2008 permitting the reclassification of non-derivative financial assets out of the fair value through profit or loss category in some circumstances. The Amendment clarifies that:

- If an entity transfers a financial asset out of the fair value through profit or loss category in accordance with the previous IAS 39 amendments, it must assess whether the financial asset contains an embedded derivative that is required to be separated from the host contract.
- This assessment is based on circumstances that existed when the entity first became party to the contract (not the date of the reclassification).
- If the financial asset contains an embedded derivative that is required to be separated, but the entity is unable to measure the derivative reliably, it is prohibited from reclassifying the asset.

*IFRIC 17 Distributions of Non-cash Assets to Owners*

This Interpretation provides guidance on the appropriate accounting treatment when an entity distributes assets other than cash as dividends to shareholders. This Interpretation will be effective for annual periods beginning on or after July 1, 2009.

*IFRIC 18 Transfers of Assets from Customers*

Applies to agreements in which an entity receives an item of property, plant and equipment from a customer that the entity must then use to connect the customer to a network, or to provide the customer with ongoing access to a supply of goods or services, or both. It also applies to agreements in which an entity receives cash that must be used only to construct or acquire property, plant and equipment that must be used for those purposes. IFRIC 18 will be applied prospectively to transfers of assets received on or after 1 July 2009.

**Annual improvements 2009**

In April 2009 the IASB has published *Improvements to IFRSs* ('2009 Improvements') which makes minor amendments to a number of International Financial Reporting Standards (IFRSs). This publication completes the IASB's second round of annual improvements. Most of these improvements become effective in annual periods beginning on January 1, 2010.

*IFRS 5 (Amendment) Non-current Assets Held for Sale and Discontinued Operations*

Clarifies that IFRS 5 and other IFRSs that specifically refer to non-current assets (or disposal groups) classified as held for sale or discontinued operations set out all the disclosures required in respect of those assets or operations. IFRS 5 (Amendment) will be applied prospectively for annual periods beginning on or after 1 January 2010.

*IFRS 8 (Amendment) Operating Segments*

Clarifies that a measure of segment assets should be disclosed, only if that amount is regularly provided to the chief operating decision maker. IFRS 8 (Amendment) will be applied retrospectively for annual periods beginning on or after 1 January 2010.

*IAS 1 (Amendment) Presentation of Financial Statements*

Amendment to clarify the classification of a liability that can, at the option of the counterparty, be settled by the issue of the entity's equity instruments. IAS 1 (Amendment) will be applied retrospectively for annual periods beginning on or after 1 January 2010.

*IAS 7 (Amendment) Statement of Cash Flows*

Amends IAS 7 to state explicitly that only an expenditure that results in a recognized asset can be classified as a cash flow from investing activities. IAS 7 (Amendment) will be applied retrospectively for annual periods beginning on or after 1 January 2010.

*IAS 17 (Amendment) Leases*

Amendment to IAS 17 clarifying that when a lease includes both land and buildings elements, an entity assesses the classification of each element as a finance or an operating lease separately in accordance with the general guidance on lease classification in paragraphs 7-13 of IAS 17. IAS 17 (Amendment) will be applied retrospectively for annual periods beginning on or after 1 January 2010.

*IAS 36 (Amendment) Impairment of Assets*

Clarifies that the largest unit permitted by IAS 36 for the purpose of allocating goodwill to cash-generating units is the operating segment level defined in IFRS 8 before aggregation as permitted in that Standard. IAS 36 (Amendment) will be applied prospectively for annual periods beginning on or after 1 January 2010.

*IAS 38 (Amendment) Intangible Assets*

Clarifies the description of valuation techniques commonly used by entities when measuring the fair value of intangible assets acquired in a business combination that are not traded in active markets. IAS 38 (Amendment) will be applied prospectively for annual periods beginning on or after 1 July 2009.

*IAS 39 (Amendment) Financial Instruments: Recognition and Measurement*

- Aims to clarify whether embedded prepayment options, in which the exercise price represented a penalty for early repayment of the loan, are considered closely related to the host debt contract.
- Aims to clarify that the scope exemption in IAS 39.2(g) applies only to binding (forward) contracts between an acquirer and a selling shareholder to buy or sell an acquiree that will result in a business combination at a future acquisition date.
- Clarifies when gains and losses on hedging instruments should be reclassified from equity to profit and loss account as a reclassification adjustment.

IAS 39 (Amendment) will be applied prospectively for annual periods beginning on or after 1 January 2010.

## **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*

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

#### *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 as 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:

	<b>December 31, 2009</b>	December 31, 2008
AMD/1 US Dollar	<b>377.89</b>	306.73
AMD/1 Euro	<b>542.23</b>	435.00

### **4.3 Taxation**

Income tax on the profit for the year 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 year, using tax rates enacted or substantially enacted at the balance sheet date, and any adjustment to tax payable in respect of previous years.

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

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

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

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

#### *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 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.

As part of its operational activities, the Bank securitises financial assets, generally through the sale of these assets to special purposes entities which issue securities to investors. The transferred assets

may qualify for derecognition in full or in part. Reference should be made to the accounting policy on “Derecognition of financial assets and financial liabilities”. Interests in the securitised financial assets may be retained by the Bank and are primarily classified as financial assets recorded at fair value through profit or loss, and gains and losses are reported in “Net trading income”. Gains or losses on securitizations are based on the carrying amount of the financial assets derecognized and the retained interest, based on their relative fair values at the date of the transfer.

#### ***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 leasee***

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.

#### 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.

The Bank transfers increase of fixed asset’s unit revaluation to retained earnings in line with the calculation of depreciation during the useful life of the asset and at disposal of the fixed asset.

#### 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.

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

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, debt securities issued and subordinated debt 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.

#### **4.22 Segment reporting**

An operating segment is a component of the Bank that engages in business activities from which it may earn revenues and incur expenses, including revenues and expenses that relate to transactions with any of the Bank's other components. In identifying its operating segments, management generally distinguishes components of the Bank that is engaged in providing products or services (business segment). All operating segments' operating results are reviewed regularly by the Bank's CEO to make decisions about resources to be allocated to the segment and assess its performance, and for which discrete financial information is available. Geographical segments of the Bank have been reported separately within these financial statements based on the ultimate domicile of the counterparty, e.g. based on economic risk rather than legal risk of the counterparty.

### **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 state and corporate bonds, securities issued by the Central Bank of Armenia and corporate shares. Upon initial recognition, the Bank designates securities as

trading securities and 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 31.

During 2009 the State Revenue Committee adjacent to RA Government has provided new interpretation on application of some articles of the RA Law on Profit tax to the fixed assets revaluated by banks. The Management of the Bank has reviewed its previous estimations, according to which economic profits receivable from compensation of carrying value of revaluated fixed assets are non taxable; therefore, the taxation base for these assets approximates their carrying value which supposes that in the future taxable amounts will not occur. The affect of the change in revaluation is disclosed in Note 14.

#### ***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	2009	2008
Loans and advances to customers	<b>5,832,436</b>	5,127,894
Debt investment securities available-for-sale	<b>395,958</b>	344,447
Amounts due from other financial institutions	<b>47,429</b>	141,095
Reverse repurchase transactions	<b>106,546</b>	54,963
Interest accrued on impaired financial assets	<b>509,879</b>	238,866
Other interest income	<b>10,353</b>	85,589
<b>Total interest and similar income</b>	<b>6,902,601</b>	5,992,854

In thousand Armenian drams	2009	2008
Amounts due to customers	2,354,122	1,649,959
Amounts due to financial institutions	606,031	371,652
Debt securities issued	31,953	535
Repurchase transactions	206,649	157,869
Other interest expenses	12,273	4,754
<b>Total interest and similar expense</b>	<b>3,211,028</b>	<b>2,184,769</b>

## 7 Fee and commission income and expense

In thousand Armenian drams	2009	2008
Cash collection	286,064	307,629
Wire transfer fees	474,071	502,101
Plastic cards operations	310,793	374,026
Guarantees and letters of credit	113,658	128,964
<b>Total fee and commission income</b>	<b>1,184,586</b>	<b>1,312,720</b>

In thousand Armenian drams	2009	2008
Wire transfer fees	46,300	58,015
Cash operations	145,954	120,423
Plastic cards operations	120,754	120,160
Other expenses	7,488	2,101
<b>Total fee and commission expense</b>	<b>320,496</b>	<b>300,699</b>

## 8 Net trading income

In thousand Armenian drams	2009	2008
Gains less losses from foreign currency transactions	1,158,856	1,506,614
Net loss from changes in fair value of trading assets and liabilities	(17,054)	(2,915)
Gains less losses on trading of trading assets	(46,809)	(3,151)
<b>Total net trading income</b>	<b>1,094,993</b>	<b>1,500,548</b>

## 9 Other income

In thousand Armenian drams	2009	2008
Fines and penalties received	51,551	190,722
Dividend income	7,095	504
Income from grants	2,422	1,316
Other income	97,534	91,527
<b>Total other income</b>	<b>158,602</b>	<b>284,069</b>

**10 Impairment charge/(reversal of impairment) for credit losses**

In thousand Armenian drams	2009	2008
Loans and advances to customers (Note 18)	2,373,456	589,643
Other assets (Note 22)	7,549	(1,944)
Other provisions (Note 28)	(17,044)	402
<b>Total impairment charge for credit losses</b>	<b>2,363,961</b>	<b>588,101</b>

**11 Foreign currency translation net loss of non-trading assets and liabilities**

On March 3, 2009 the Central Bank of Armenia has decided to go to floating exchange rate of 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. As of the mentioned date the net loss from foreign currency translations of non-trading assets and liabilities of the Bank comprises AMD 777,021 thousand.

**12 Staff costs**

In thousand Armenian drams	2009	2008
Wages and other benefits	1,639,544	1,641,708
Social security contributions	174,062	160,684
<b>Total staff costs</b>	<b>1,813,606</b>	<b>1,802,392</b>

**13 Other expenses**

In thousand Armenian drams	2009	2008
Fixed assets maintenance	129,580	114,323
Advertising costs	139,567	158,060
Business trip expenses	136,000	29,238
Communications	118,120	94,777
Operating lease	189,341	163,781
Taxes, other than income tax, duties	164,418	131,515
Consulting and other services	132,356	82,620
Security	89,736	71,492
Loss on disposal of PPE	140	2,944
Office supplies	32,205	34,271
Penalties paid	2,068	8,130
Cash collection expenses	67,929	63,228
Other expenses	338,304	219,543
<b>Total other expense</b>	<b>1,539,764</b>	<b>1,173,922</b>

**14 Income tax expense/(benefit)**

In thousand Armenian drams	2009	2008
Current tax expense	-	589,466
Deferred tax	(99,416)	(29,161)
<b>Total income tax expense/(benefit)</b>	<b>(99,416)</b>	<b>560,305</b>

The corporate income tax within the Republic of Armenia is levied at the rate of 20% (2008: 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/(benefit) and accounting profit/(loss) is provided below:

In thousand Armenian drams	2009	Effective rate (%)	2008	Effective rate (%)
<b>Profit/(loss) before tax</b>	<b>(1,125,645)</b>		2,404,356	
Income tax at the rate of 20%	(225,129)	(20)	480,871	20
Non-taxable income	(40,533)	(4)	(3,033)	-
Non-deductible expenses	24,029	2	20,893	1
Foreign exchange losses	142,217	13	61,574	2
<b>Income tax expense/(benefit)</b>	<b>(99,416)</b>	<b>(9)</b>	<b>560,305</b>	<b>23</b>

Deferred tax calculation in respect of temporary differences:

In thousand Armenian drams	2008	Recognized in comprehensive income statement	Recognized in equity	2009
Accrued expenses and other liabilities	4,252	(916)	-	3,336
Allowances for other provisions	1,408	(1,408)	-	-
Securities available for sale	14,644	-	15,713	30,357
Tax losses carried forward	-	157,367	-	157,367
<b>Total deferred tax assets</b>	<b>20,304</b>	<b>155,043</b>	<b>15,713</b>	<b>191,060</b>
Other assets	(6,348)	(55,627)	-	(61,975)
Securities available for sale	(27,399)	-	7,955	(19,444)
Fixed assets	(459,548)	-	459,548	-
<b>Total deferred tax liability</b>	<b>(493,295)</b>	<b>(55,627)</b>	<b>467,503</b>	<b>(81,419)</b>
<b>Net deferred tax asset/(liability)</b>	<b>(472,991)</b>	<b>99,416</b>	<b>483,216</b>	<b>109,641</b>

In thousand Armenian drams	2007	Recognized in comprehensive income statement	Recognized in equity	2008
Accrued expenses and other liabilities	1,900	2,352	-	4,252
Allowances for other provisions	3,836	(2,428)	-	1,408
Securities available for sale	4,889	-	9,755	14,644
Trading securities	4,796	(4,796)	-	-
Loans and advances to customers	4,352	(4,352)	-	-
<b>Total deferred tax assets</b>	<u>19,773</u>	<u>(9,224)</u>	<u>9,755</u>	<u>20,304</u>
Other assets	(10,774)	4,426	-	(6,348)
Securities available for sale	-	-	(27,399)	(27,399)
Fixed assets	(493,507)	33,959	-	(459,548)
<b>Total deferred tax liability</b>	<u>(504,281)</u>	<u>38,385</u>	<u>(27,399)</u>	<u>(493,295)</u>
<b>Net deferred tax asset/(liability)</b>	<u>(484,508)</u>	<u>29,161</u>	<u>(17,644)</u>	<u>(472,991)</u>

As of the reporting date the Bank possesses deferred income tax assets which occur from calculated tax loss and which can be used for the purpose of reducing the taxable income of the future reporting period. Consistent with its scope of operations, the Bank has recognized these assets in the financial statements as the management believes that the Bank will have taxable income in the future for the coverage of which the Bank will be able to use the assets related to income tax.

As at 31 December 2009 the Bank has available AMD 786,835 thousand in tax losses carried forward.

During 2009 the Bank has derecognised deferred tax liability in the amount of AMD 459,548 thousand which was previously recognised on revaluated fixed assets. See Note 5.

## 15 Cash, cash equivalents and balances with CBA

In thousand Armenian drams	2009	2008
Cash on hand	<b>5,086,790</b>	3,977,346
Other money market placements	<b>1,398</b>	12,142
Correspondent account with the CBA	<b>11,751,975</b>	8,265,783
<b>Included in cash and cash equivalents</b>	<u><b>16,840,163</b></u>	<u>12,255,271</u>
Deposits with the CBA	<b>521,069</b>	212,010
<b>Total cash and balances with the CBA</b>	<u><b>17,361,232</b></u>	<u>12,467,281</u>
Cash and balances with the CBA, included in cash flow	<b>16,840,163</b>	12,255,271
Placements with other banks (note 17)	<b>4,026,753</b>	2,173,953
<b>Total cash and cash equivalents</b>	<u><b>20,866,916</b></u>	<u>14,429,224</u>

As at 31 December 2009 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 12,273,044 thousand (2008: AMD 4,677,481 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.

## 16 Financial assets at fair value through profit or loss

In thousand Armenian drams	2009	2008
Trading securities issued by the Ministry of Finance of RA	275,915	58,672
<b>Trading securities</b>	<b>275,915</b>	<b>58,672</b>

Nominal interest rates and maturities of these securities are as follows:

In thousand Armenian drams	2009		2008	
	%	Maturity	%	Maturity
Securities issued by the Ministry of Finance of RA	0-12.5	2009-2028	0-10.53	2009-2028

## 17 Amounts due from other financial institutions

In thousand Armenian drams	2009	2008
Correspondent accounts with financial institutions	4,026,753	2,173,953
<b>Included in cash and cash equivalents</b>	<b>4,026,753</b>	<b>2,173,953</b>
Loans and deposits to financial institutions	2,926,504	1,468,497
Reverse repurchase agreements	1,684,519	1,210,014
Other amounts	1,948,494	319,152
<b>Total amounts due from other financial institutions</b>	<b>10,586,270</b>	<b>5,171,616</b>

As at 31 December 2009 the amounts due from other financial institutions in amounts of AMD 3,676,870 thousand (35%) (2008: AMD 1,975,537 thousand (39%)) were due from 3 banks.

As of 31 December 2009 included in amounts due from other financial institutions are guarantee deposits placed by the Bank for its operations in the amount of AMD 338,169 thousand (2008: AMD 337,102 thousand).

During 2009, 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 2009, the Bank placed deposits in foreign currency equivalent to AMD 1,679,779 thousand (2008: AMD 92,545 thousand), which were related to deposits in drams received from the same Armenian banks (See Note 23).

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

In thousand Armenian drams	2009		2008	
	Fair value of collateral	Carrying value of loans	Fair value of collateral	Carrying value of loans
Securities pledged under repurchase agreements	1,676,686	1,684,519	1,232,356	1,210,014
<b>Total assets pledged under repurchase agreements</b>	<b>1,676,686</b>	<b>1,684,519</b>	<b>1,232,356</b>	<b>1,210,014</b>

As of 31 December 2008 out of total accepted securities AMD 938,371 thousand were re-pledged to the third parties for periods not exceeding three months from the transfer (See Note 26).

## 18 Loans and advances to customers

In thousand Armenian drams	2009	2008
Loans to customers	40,984,414	41,011,496
Factoring	81,341	866,636
Overdrafts	2,532,539	1,379,970
Letter of credit	-	312,381
	<b>43,598,294</b>	<b>43,570,483</b>
Less allowance for loan impairment	(2,470,910)	(912,327)
<b>Total loans and advances to customers</b>	<b>41,127,384</b>	<b>42,658,156</b>

As of 31 December 2009, accrued interest income included in loans and advances to customers amounted to AMD 274,244 thousand (2008: AMD 284,328 thousand).

As of December 31, 2009, the Bank had a concentration of loans represented by AMD 13,380,596 thousand due from the ten largest third party entities and parties related with them (30.7% of gross loan portfolio) (2008: AMD 10,645,899 thousand or 25%). An allowance of AMD 1,970,275 thousand (2008: AMD 448,741 thousand) was made against these loans.

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

In thousand Armenian drams	2009	2008
Manufacture	6,276,681	5,865,292
Agriculture	1,435,326	829,542
Construction	4,835,091	4,538,358
Trading	8,425,545	13,690,362
Transport	208,010	748,434
Services	798,978	785,819
Consumer	12,340,944	10,545,233
Mortgage	7,368,216	4,468,647
Other sectors	1,909,503	2,098,796
	<b>43,598,294</b>	<b>43,570,483</b>
Less allowance for loan impairment	(2,470,910)	(912,327)
<b>Total loans and advances to customers</b>	<b>41,127,384</b>	<b>42,658,156</b>

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

2009										
In thousand Armenian drams	Manufacture	Agriculture	Construction	Trading	Transport	Services	Consumer	Mortgage	Other	Total
At 1 January 2009	300,816	4,400	326,954	100,741	6,975	8,046	95,639	31,836	36,920	912,327
Charge for the year	353,207	66,164	897,277	377,013	4,407	18,578	221,641	68,479	366,690	2,373,456
Amounts written off	(25,133)	(12,144)	(65,361)	(336,252)	(8,536)	(18,907)	(230,876)	(27,097)	(141,263)	(865,569)
Recoveries	3,859	67	7,327	9,518	-	210	29,050	-	665	50,696
At 31 December 2009	<u>632,749</u>	<u>58,487</u>	<u>1,166,197</u>	<u>151,020</u>	<u>2,846</u>	<u>7,927</u>	<u>115,454</u>	<u>73,218</u>	<u>263,012</u>	<u>2,470,910</u>
Individual impairment	588,500	46,656	1,137,717	43,366	-	-	-	-	244,060	2,060,299
Collective impairment	44,249	11,831	28,480	107,654	2,846	7,927	115,454	73,218	18,952	410,611
	<u>632,749</u>	<u>58,487</u>	<u>1,166,197</u>	<u>151,020</u>	<u>2,846</u>	<u>7,927</u>	<u>115,454</u>	<u>73,218</u>	<u>263,012</u>	<u>2,470,910</u>
Gross amount of loans individually determined to be impaired, before deducting any individually assessed impairment allowance	<u>1,929,479</u>	<u>266,015</u>	<u>2,059,142</u>	<u>257,757</u>	-	-	-	-	<u>1,204,209</u>	<u>5,716,602</u>

2008										
In thousand Armenian drams	Manufacture	Agriculture	Construction	Trading	Transport	Services	Consumer	Mortgage	Other	Total
At 1 January 2008	112,772	3,505	13,907	98,744	6,644	10,882	73,009	14,971	9,933	344,367
Charge/(recovery) for the year	192,404	(5,114)	313,047	6,227	331	(13,253)	52,149	16,865	26,987	589,643
Amounts written off	(7,535)	-	-	(4,230)	-	(210)	(64,674)	-	-	(76,649)
Recoveries	3,175	6,009	-	-	-	10,627	35,155	-	-	54,966
At 31 December 2008	<u>300,816</u>	<u>4,400</u>	<u>326,954</u>	<u>100,741</u>	<u>6,975</u>	<u>8,046</u>	<u>95,639</u>	<u>31,836</u>	<u>36,920</u>	<u>912,327</u>
Individual impairment	247,920	-	307,408	-	-	-	-	-	14,928	570,256
Collective impairment	52,896	4,400	19,546	100,741	6,975	8,046	95,639	31,836	21,992	342,071
	<u>300,816</u>	<u>4,400</u>	<u>326,954</u>	<u>100,741</u>	<u>6,975</u>	<u>8,046</u>	<u>95,639</u>	<u>31,836</u>	<u>36,920</u>	<u>912,327</u>
Gross amount of loans individually determined to be impaired, before deducting any individually assessed impairment allowance	<u>1,452,485</u>	-	<u>73,310</u>	-	-	-	-	-	<u>951,098</u>	<u>2,476,893</u>

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

In thousand Armenian drams	2009	2008
State owned enterprises	46,451	4,953
Privately held companies	20,861,172	23,800,124
Individuals	19,584,623	15,722,365
Sole proprietors	2,831,747	3,758,564
Non-commercial institutions	57	149
Accrued interest	274,244	284,328
	<u>43,598,294</u>	<u>43,570,483</u>
Less allowance for loan impairment	(2,470,910)	(912,327)
<b>Total loans and advances to customers</b>	<b><u>41,127,384</u></b>	<b><u>42,658,156</u></b>

Loans to individuals comprise the following products:

In thousand Armenian drams	2009	2008
Mortgage loans	7,321,828	4,438,504
Consumer loans	7,467,781	6,763,032
Car loans	3,929,219	3,562,448
Other	865,795	958,381
<b>Total loans and advances to individuals (gross)</b>	<b><u>19,584,623</u></b>	<b><u>15,722,365</u></b>

At 31 December 2009 and 31 December 2008 the estimated fair value of loans and advances to customers approximates its carrying value. Refer to Note 33.

Credit, currency, liquidity and interest rate analyses of loans and advances to customers are disclosed in Note 35. The information on related party balances is disclosed in Note 32.

## 19 Investments available for sale

In thousand Armenian drams	2009	2008
<b>Unquoted investments</b>		
RA corporate bonds	74,092	401,286
Securities issued by the Ministry of Finance of Armenia	2,005,945	52,924
RA equity shares	72,381	71,570
Equity shares of OECD countries	106,063	146,151
<b>Total investments</b>	<b><u>2,258,481</u></b>	<b><u>671,931</u></b>

All debt securities have fixed coupons.

All unquoted RA 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 interest rates and maturity date comprise:

In thousand Armenian drams	2009		2008	
	%	Maturity	%	Maturity
Securities issued the Ministry of Finance of Armenia	0-12.5%	2009-2028	0-10.53%	2009-2028
RA corporate bonds	9.5-10.5%	2010-2011	9%	2009

As at 31 December 2009 debt securities available for sale at fair value of AMD 2,323,985 thousand were pledged to third parties in sale and repurchase agreements for periods not exceeding six months (2008: 3,944,502 thousand). See Note 29. These securities have been reclassified as securities pledged under repurchase agreements on the face of the balance sheet.

## 20 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, 2008	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)
At December 31, 2008	(10,780)	89	-	-	(89)	-	(10,780)
	<b>3,745,777</b>	<b>364,552</b>	<b>55,711</b>	<b>1,154,533</b>	<b>377,620</b>	<b>101,332</b>	<b>5,799,525</b>
Additions	104,468	58,488	6,092	184,889	49,386	4,569	407,892
Disposals	-	(1,148)	-	(101,470)	(2,843)	-	(105,461)
Reclassifications	-	(29)	-	-	29	-	-
Adjustments	-	-	-	-	3,600	-	3,600
<b>At December 31, 2009</b>	<b>3,850,245</b>	<b>421,863</b>	<b>61,803</b>	<b>1,237,952</b>	<b>427,792</b>	<b>105,901</b>	<b>6,105,556</b>
<b>DEPRECIATION</b>							
At January 1, 2008	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)
Reclassifications	-	9	-	-	(9)	-	-
At December 31, 2008	<b>669,480</b>	<b>268,192</b>	<b>33,552</b>	<b>684,772</b>	<b>234,735</b>	<b>22,499</b>	<b>1,913,230</b>
Depreciation charge	230,830	43,538	8,277	208,161	65,290	20,373	576,469
Disposals	-	(645)	-	(96,350)	(2,172)	-	(99,167)
Adjustments	-	-	-	-	3,600	-	3,600
<b>At December 31, 2009</b>	<b>900,310</b>	<b>311,085</b>	<b>41,829</b>	<b>796,583</b>	<b>301,453</b>	<b>42,872</b>	<b>2,394,132</b>
<b>CARRYING VALUE</b>							
<b>At December 31, 2009</b>	<b>2,949,935</b>	<b>110,778</b>	<b>19,974</b>	<b>441,369</b>	<b>126,339</b>	<b>63,029</b>	<b>3,711,424</b>
At December 31, 2008	3,076,297	96,360	22,159	469,761	142,885	78,833	3,886,295

### Revaluation of assets

The buildings owned by the Bank were evaluated by an independent appraiser 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 has 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 863,875 AMD thousand as at 31 December 2009 (2008: AMD 823,161 thousand).

Management believes that as of 31.12.09 the fair value of the buildings does not significantly differ from their carrying amount.

#### *Fully depreciated items*

As at 31 December 2009 fixed assets included fully depreciated assets in amount of AMD 855,246 thousand (2008: AMD 690,658 thousand).

#### *Fixed assets in the phase of installation*

As at 31 December 2009 fixed assets included assets in the phase of installation in amount of AMD 109,286 thousand (2008: AMD 124,761 thousand), which are not amortized and are classified in accordance with their type.

## **21 Intangible assets**

In thousand Armenian drams	<b>Licenses</b>	<b>Computer software</b>	<b>Other</b>	<b>Total</b>
<b>COST</b>				
At January 1, 2008	121,730	18,369	2,008	142,107
Additions	51,554	5,400	1,939	58,893
At December 31, 2008	<b>173,284</b>	<b>23,769</b>	<b>3,947</b>	<b>201,000</b>
Additions	<b>199,641</b>	<b>362</b>	<b>10,015</b>	<b>210,018</b>
Disposals	(71)	-	-	(71)
<b>At December 31, 2009</b>	<b>372,854</b>	<b>24,131</b>	<b>13,962</b>	<b>410,947</b>
<b>AMORTISATION</b>				
At January 1, 2008	71,525	10,316	743	82,584
Amortisation charge	12,523	2,352	201	15,076
At December 31, 2008	<b>84,048</b>	<b>12,668</b>	<b>944</b>	<b>97,660</b>
Amortisation charge	<b>27,664</b>	<b>4,025</b>	<b>264</b>	<b>31,953</b>
Disposals	(60)	-	-	(60)
<b>At December 31, 2009</b>	<b>111,652</b>	<b>16,693</b>	<b>1,208</b>	<b>129,553</b>
<b>CARRYING VALUE</b>				
<b>At December 31, 2009</b>	<b>261,202</b>	<b>7,438</b>	<b>12,754</b>	<b>281,394</b>
At December 31, 2008	89,236	11,101	3,003	103,340

#### *Fully amortized items*

As at 31 December 2009 intangible assets included fully amortized assets in amount of AMD 8,762 thousand (2008: AMD 8,526 thousand).

## 22 Other assets

In thousand Armenian drams	2009	2008
Prepayments and other debtors	136,807	110,840
Prepayment to budget	30,999	26,193
Settlements with employees	452	80
Other assets	93,364	14,841
	<b>261,622</b>	151,954
Less allowance for impairment	(2,504)	(512)
	<b>259,118</b>	151,442
Accounts receivable	300	300
Accrued income	345	262
	<b>645</b>	562
Assets classified as held for sale	26,430	70,899
Other prepaid taxes	2,308	2,039
Materials	45,528	40,869
Other	7,895	1,895
<b>Total other assets</b>	<b>341,924</b>	267,706

As at December 31, 2009 assets classified as held for sale include AMD 15,965 thousand (2008: AMD 61,419 thousand) repossessed assets and AMD 10,465 thousand (2008: AMD 9,480 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	Total
<b>At January 1, 2008</b>	1,336
Reversal for the year	(1,944)
Amounts written off	(2,152)
Recoveries	3,272
<b>At December 31, 2008</b>	<b>512</b>
Charge for the year	7,549
Amounts written off	(9,358)
Recoveries	3,801
<b>At December 31, 2009</b>	<b>2,504</b>

## 23 Amounts due to financial institutions

In thousand Armenian drams	2009	2008
Obligations of the CBA	5,950,957	6,702,199
Correspondent accounts of other banks	96,590	237,728
Current accounts of other financial institutions	1,589,182	724,867
Loans and deposits from financial institutions	-	2,183,878
Other amounts	1,678,082	252,450
<b>Total amounts due to financial institutions</b>	<b>9,314,811</b>	10,101,122

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 3,632,489 thousand (2008: 2,745,050 thousand) and amounts under repurchase agreements in the amount of AMD 2,318,468 thousand (2008: 3,957,149 thousand). See note 29.

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

During 2009, 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 2009, the Bank received an equivalent of AMD 1,678,082 thousand (2008: 92,019 thousand) as deposits in foreign currency from the same Armenian banks, which relate to deposits in foreign currency granted to the same banks (See Note 17).

The Bank has not had any defaults of principal, interest or other breaches with respect to its borrowings during the year (2008: nil).

## 24 Amounts due to customers

In thousand Armenian drams	2009	2008
<b>Government of the RA</b>		
Current/Settlement accounts	264,216	57,184
Time deposits	3,246,907	2,234,575
	<b>3,511,123</b>	2,291,759
<b>Corporate customers</b>		
Current/Settlement accounts	19,978,221	12,478,568
Time deposits	11,652,454	9,816,724
	<b>31,630,675</b>	22,295,292
<b>Retail customers</b>		
Current/Demand accounts	7,763,518	4,018,332
Time deposits	13,534,757	14,054,939
	<b>21,298,275</b>	18,073,271
<b>Total amounts due to customers</b>	<b>56,440,073</b>	42,660,322

All customer deposits carry fixed rates.

As at 31 December 2009 included in the time deposit payable to Government is AMD 1,370,840 thousand (2008: AMD 1,481,185 thousand), which was attracted under the World Bank projects on “Enterprise Development” and “Agricultural Reform”, the amount of AMD 141,246 thousand attracted from “Millennium Challenges Foundation-Armenia” SNCO (2008: AMD 153,190 thousand), as well as the loans received within the scope of “Small and medium business loan project” of German-Armenian fund in the amount of AMD 1,734,821 thousand (2008: AMD 753,390 thousand)

As at 31 December 2009 included in amounts due to customers are deposits amounting to AMD 515,562 thousand (2008: AMD 48,633 thousand) held as security against guarantees issued. The fair value of those deposits approximates the carrying amount.

At 31 December 2009 the aggregate balance of top ten customers of the Bank (including related parties, see Note 32) amounts to AMD 24,516,869 thousand (2008: AMD 20,274,089 thousand) or 46% of total customer accounts (2008: 50%). 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 (2008: nil).

## 25 Debt securities issued

In thousand Armenian drams	2009	2008
Bonds	301,312	301,280
	<u>301,312</u>	<u>301,280</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 (2008: same).

## 26 Trading liabilities

In thousand Armenian drams	2009	2008
Securities borrowed from third parties	-	1,200,719
Securities borrowed under repurchase agreements	-	938,371
<b>Total trading liabilities</b>	<u>-</u>	<u>2,139,090</u>

As of 31.12.2008 the repurchase agreements represent the unquoted debt securities that the Bank intends to buy back in the short term (See Note 17).

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 re-pledged to the third parties (see notes 32).

## 27 Other liabilities

In thousand Armenian drams	2009	2008
Accounts payables	63,253	91,040
Tax payable, other than income tax	72,434	5,121
Revenues of future periods	21,350	19,267
Grants related to assets	45,388	47,810
Due to personnel	26,420	52,675
Due to on payment checks	63,009	72,919
Other	16,463	23,925
<b>Total other liabilities</b>	<u>308,317</u>	<u>312,757</u>

## 27.1 Grants related to assets

In thousand Armenian drams	2009	2008
At January 1	47,810	52,931
Increase/(decrease)	-	(3,805)
Recognition of income	(2,422)	(1,316)
<b>At December 31</b>	<b>45,388</b>	<b>47,810</b>

## 28 Other provisions

The movement in other provisions was as follows:

In thousand Armenian drams	2009	2008
<b>At January 1</b>	<b>35,345</b>	34,943
Arising during the year/(reversal)	(17,044)	402
<b>At December 31</b>	<b>18,301</b>	<b>35,345</b>

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

## 29 Securities pledged under repurchase agreements

In thousand Armenian drams	Asset		Liability	
	2009	2008	2009	2008
Securities pledged under repurchase agreements (Note 19, 23)	2,323,985	3,944,502	2,318,468	3,957,149
	<b>2,323,985</b>	<b>3,944,502</b>	<b>2,318,468</b>	<b>3,957,149</b>

## 30 Equity

As at 31 December 2009 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 2009 and 31 December 2008 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
	<b>1,233,133</b>	<b>100</b>

As at 31 December 2009, 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.

### 31 Contingent liabilities and commitments

#### *Tax and legal matters*

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

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

As of 31 December 2009 there were no legal actions and complaints taken against 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	2009	2008
Undrawn loan commitments	4,143,181	1,963,972
Letters of credit	-	63,533
Guarantees	1,830,141	3,534,508
<b>Total commitments and contingent liabilities</b>	<b>5,973,322</b>	<b>5,562,013</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	2009	2008
Not later than 1 year	185,038	190,735
Later than 1 year and not later than 5 years	493,440	533,367
Later than 5 years	38,986	41,069
<b>Total operating lease commitments</b>	<b>717,464</b>	<b>765,171</b>

### Insurance

The insurance industry in Armenia is in a developing state and many forms of insurance protection common in other parts of the world are not yet generally available. The Bank does not have full coverage for business interruption, or for third party liability in respect of property or environmental damage arising from accidents on Bank property or relating to Bank operations. Until the Bank obtains adequate insurance coverage, there is a risk that the loss or destruction of certain assets could have a material adverse effect on the Bank's operations and financial position.

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.

### 32 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 Bank 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	2009		2008	
	Shareholders	Key management personnel	Shareholders	Key management personnel
<b>Loans and advances to customers</b>				
Loans outstanding at January 1, gross	536,539	190,452	29,859	60,252
Loans issued during the year	634,950	77,853	1,380,151	274,501
Loan repayments during the year	(919,035)	(249,180)	(873,471)	(144,301)
Loans outstanding at December 31, gross	252,454	19,125	536,539	190,452
Less: allowance for loan impairment	(2,525)	(191)	(5,365)	(1,905)
<b>Loans outstanding at December 31</b>	<b>249,929</b>	<b>18,934</b>	<b>531,174</b>	<b>188,547</b>
Impairment charge/(reversal of impairment) for credit losses	(2,840)	(1,714)	5,043	1,225
Interest income on loans	59,847	7,178	22,051	5,912
<b>Amounts due to customers</b>				
Deposits at January 1	15,808,426	458,888	3,174,840	358,529
Deposits received during the year	234,880,605	926,414	243,523,041	1,208,493
Deposits repaid during the year	(229,166,274)	(1,376,213)	(230,889,455)	(1,108,134)
<b>Deposits at December 31</b>	<b>21,522,757</b>	<b>9,089</b>	<b>15,808,426</b>	<b>458,888</b>
Interest expense on deposits	937,880	19,986	224,507	3,682
<b>Borrowed securities</b>				
Borrowed securities at January 1	1,079,762	-	-	-
Borrowings received during the year	-	-	1,079,762	-
Borrowings repaid during the year	(1,079,762)	-	-	-
<b>Borrowed securities at December 31</b>	<b>-</b>	<b>-</b>	<b>1,079,762</b>	<b>-</b>
Interest expense on borrowings	-	-	158	-

In thousand Armenian drams	2009		2008	
	Shareholders	Key management personnel	Shareholders	Key management personnel
<b>Items of comprehensive statement of Income</b>				
Fee and commission income	41,125	22	14,379	100
Other income	1,535	8,513	1,623	23,650
Advisory expenses	41,795	55,131	34,147	60,127
Other expenses	751	1,001	1,463	22,433

The loans issued to directors and other key management personnel (and close family members) have maturity from 3 months to 20 years and have interest rates of 5-24% (2008: 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	2009	2008
Salaries and other short-term benefits	221,157	220,941
Social security costs	22,735	23,623
<b>Total key management compensation</b>	<b>243,892</b>	<b>244,564</b>

### 33 Fair value of financial instruments

*Financial instruments not measured at fair value*

In thousand Armenian drams	2009		2008	
	Carrying value	Fair value	Carrying value	Fair value
<b>FINANCIAL ASSETS</b>				
Cash and balances with CBA	17,361,232	17,361,232	12,467,281	12,467,281
Amounts due from financial institutions	10,586,270	10,586,270	5,171,616	5,171,616
Loans and advances to customers	41,127,384	41,127,384	42,658,156	42,658,156
<b>FINANCIAL LIABILITIES</b>				
Amounts due to financial institutions	9,314,811	9,314,811	10,101,122	10,101,122
Amounts due to customers	56,440,073	56,440,073	42,660,322	42,660,322
Issued debt securities	301,312	301,312	301,280	301,280

#### *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, which are mainly the same as current interest 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.

**33.1 Fair Value Hierarchy**

The fair value hierarchy has the following levels:

- Level 1: quoted prices (unadjusted) in active markets for identical assets or liabilities
- Level 2: inputs other than quoted prices included within Level 1 that are observable for the asset and liability, either directly (i.e. as prices) or indirectly (i.e. derived from prices)
- Level 3: inputs for the asset or liability that are not based on observable market data (unobservable inputs).

In thousand Armenian drams				2009
	Level 1	Level 2	Level 3	Total
<b>FINANCIAL ASSETS</b>				
Trading securities	-	275,915	-	275,915
Investments available for sale	-	2,080,037	-	2,080,037
Unquoted equity investments	-	106,063	-	106,063
Securities pledged under repurchase agreements	-	2,323,985	-	2,323,985
<b>Total</b>	-	<b>4,786,000</b>	-	<b>4,786,000</b>

The methods and valuation techniques used for the purpose of measuring fair value are unchanged compared to the previous reporting period.

*Unquoted RA equity investments*

The fair value of Bank's investment in unquoted RA equity investments cannot be reliably measured and is therefore excluded from this disclosure. Refer to note 19 for further information about this equity investment.

**34 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 35.3 for the Bank's contractual undiscounted repayment obligations.

In thousand Armenian drams								2009
	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	16,840,163	-	-	16,840,163	-	521,069	521,069	17,361,232
Trading securities	-	2,547	15,115	17,662	201,372	56,881	258,253	275,915
Amounts due from other financial institutions	9,662,076	206,935	379,090	10,248,101	-	338,169	338,169	10,586,270
Loans and advances to customers	2,557,313	2,403,689	11,166,254	16,127,256	20,506,051	4,494,077	25,000,128	41,127,384
Investments available for sale	-	57,472	520,028	577,500	986,371	694,610	1,680,981	2,258,481
Securities pledged under repurchase agreements	2,323,985	-	-	2,323,985	-	-	-	2,323,985
	<b>31,383,537</b>	<b>2,670,643</b>	<b>12,080,487</b>	<b>46,134,667</b>	<b>21,693,794</b>	<b>6,104,806</b>	<b>27,798,600</b>	<b>73,933,267</b>

In thousand Armenian drams								2009
	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>LIABILITIES</b>								
Amounts due to financial institutions	4,417,085	377,583	787,149	5,581,817	3,732,994	-	3,732,994	9,314,811
Amounts due to customers	30,726,433	6,682,933	14,072,129	51,481,495	4,626,818	331,760	4,958,578	56,440,073
Debt securities issued	-	1,312	-	1,312	300,000	-	300,000	301,312
	<u>35,143,518</u>	<u>7,061,828</u>	<u>14,859,278</u>	<u>57,064,624</u>	<u>8,659,812</u>	<u>331,760</u>	<u>8,991,572</u>	<u>66,056,196</u>
<b>Net position</b>	<u>(3,759,981)</u>	<u>(4,391,185)</u>	<u>(2,778,791)</u>	<u>(10,929,957)</u>	<u>13,033,982</u>	<u>5,773,046</u>	<u>18,807,028</u>	<u>7,877,071</u>
<b>Accumulated gap</b>	<u>(3,759,981)</u>	<u>(8,151,166)</u>	<u>(10,929,957)</u>		<u>2,104,025</u>	<u>7,877,071</u>		

In thousand Armenian drams								2008
	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>		

### 35 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 Department under policies approved by the Board of Directors. The Risk Management 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.

### 35.1 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.

#### 35.1.1 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 2009 and 2008, without taking account of any collateral held or other credit enhancements attached. For on-balance-sheet assets, the exposures set out above are based on net carrying amounts as reported in the balance sheet.

In thousand Armenian drams	Notes	Gross maximum exposure as of December 31, 2009	Gross maximum exposure as of December 31, 2008
Balances with CBA	15	12,274,442	8,489,935
Trading securities	16	275,915	58,672
Amounts due from other financial institutions	17	10,586,270	5,171,616
Loans and advances to customers	18	41,127,384	42,658,156
Investments available for sale	19	2,258,481	671,931
Securities pledged under repurchase agreements	29	2,323,985	3,944,502
<b>Total</b>		<b>68,846,477</b>	<b>60,994,812</b>
Commitments and contingent liabilities	31	5,973,322	5,562,013
<b>Total credit risk exposure</b>		<b>74,819,799</b>	<b>66,556,825</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.

#### 35.1.2 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 2009 and 31 December 2008.

In thousand Armenian drams	Other non-OECD countries			Total
	Armenia	OECD countries		
Balances with CBA	12,274,442	-	-	12,274,442
Trading securities	275,915	-	-	275,915
Amounts due from other financial institutions	5,141,719	4,248,873	1,195,678	10,586,270
Loans and advances to customers	41,052,171	7,865	67,348	41,127,384
Investments available for sale	2,152,418	106,063	-	2,258,481
Securities pledged under repurchase agreements	2,323,985	-	-	2,323,985
<b>As at 31 December 2009</b>	<b>63,220,650</b>	<b>4,362,801</b>	<b>1,263,026</b>	<b>68,846,477</b>
As at 31 December 2008	58,335,660	2,452,456	206,696	60,994,812

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 2009 and 31 December 2008.

In thousand Armenian drams	Financial institutions	Manufacturing	Agriculture	Trading	Construction	Consumer sector (mortgage)				Other	Total
						State sector	Services				
Balances with CBA	12,274,442	-	-	-	-	-	-	-	-	-	12,274,442
Trading securities	-	-	-	-	-	275,915	-	-	-	-	275,915
Amounts due from other financial institutions	10,586,270	-	-	-	-	-	-	-	-	-	10,586,270
Loans and advances to customers	-	5,643,933	1,376,839	8,274,525	3,668,894	46,272	19,520,488	996,216	1,600,217	-	41,127,384
Investments available for sale	115,719	-	-	-	21,824	2,005,945	-	52,268	62,725	-	2,258,481
Securities pledged under repurchase agreements	2,323,985	-	-	-	-	-	-	-	-	-	2,323,985
<b>As at 31 December 2009</b>	<b>25,300,416</b>	<b>5,643,933</b>	<b>1,376,839</b>	<b>8,274,525</b>	<b>3,690,718</b>	<b>2,328,132</b>	<b>19,520,488</b>	<b>1,048,484</b>	<b>1,662,942</b>	<b>-</b>	<b>68,846,477</b>
As at 31 December 2008	17,777,917	6,505,108	815,979	13,648,873	4,511,094	114,357	14,788,642	791,618	2,041,224	-	60,994,812

### 35.1.3 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	2009	2008
Loans collateralized by real estate	30,323,545	32,741,686
Loans collateralized by vehicles	3,929,219	3,585,848
Loans collateralized by guarantees of enterprises	797,405	58,846
Loans collateralized by inventories	675,210	840,172
Loans collateralized by equipment	3,347,640	1,353,815
Loans collateralized by cash	165,283	186,943
Loans collateralized by shares of other companies	-	145,619
Other collateral	3,520,641	4,197,552
Unsecured loans	839,351	460,002
<b>Total loans and advances to customers (gross)</b>	<b>43,598,294</b>	<b>43,570,483</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.

#### **35.1.4 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 estimates impairment for loans based on an analysis of the future cash flows for impaired loans and based on its past loss experience for portfolios of loans for which no indications of impairment have been identified approaching conservatively. 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	2009	2008
	%	%
Loans and advances to customers		
Manufacture	1.0	1.0
Agriculture	1.0	1.0
Construction	1.0	1.0
Transport	1.4	1.0
Trading	1.3	1.0
Public food and services	1.0	1.0
Consumer	1.0	1.0
Mortgage	1.0	1.0
Other sectors	1.3	1.0

As of 31.12.09 and 31.12.08 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					2009
	Less than 30 days	31 to 60 days	61 to 90 days	More than 91 days	Total
Loans and advances to customers					
Manufacture	19,538	505	99	194,831	214,973
Agriculture	40,951	111,821	-	2,588	155,360
Construction	1,114	0	-	41,881	42,995
Trading	19,081	68,426	3,437	130,852	221,796
Consumer	67,436	44,309	7,791	150,226	269,762
Mortgage	38,954	39,477	46,799	112,527	237,757
Services	29,698	1,336	36	52,934	84,004
Other sectors	9,019	2,919	-	23,285	35,223
<b>Total</b>	<b>225,791</b>	<b>268,793</b>	<b>58,162</b>	<b>709,124</b>	<b>1,261,870</b>

In thousand Armenian drams					2008
	Less than 30 days	31 to 60 days	61 to 90 days	More than 91 days	Total
Loans and advances to customers					
Manufacture	797,584	-	85,843	3,782	887,209
Agriculture	-	-	-	9,868	9,868
Construction	1,923	-	104,269	-	106,192
Trading	100,773	108,191	41,852	39,883	290,699
Consumer	101,948	44,640	19,494	79,838	245,920
Mortgage	18,868	23,841	-	-	42,709
Services	28,872	5,050	2,973	4,084	40,979
Other sectors	118,813	10,103	2,995	-	131,911
<b>Total</b>	<b>1,168,781</b>	<b>191,825</b>	<b>257,426</b>	<b>137,455</b>	<b>1,755,487</b>

The fair value of collateral that the Bank holds relating to past due loans at 31 December 2009 amounts to AMD 3,333,334 thousand (2008: AMD 7,771,416 thousand). The collateral consists of cash, securities 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 5,716,602 thousand (2008: AMD 2,476,893 thousand). Refer to Note 18. The fair value of collateral that the Bank holds relating to individually impaired loans at 31 December 2009 amounts to AMD 4,708,918 thousand (2008: AMD 3,228,041 thousand). The collateral consists of real estate, inventory and properties.

#### *Renegotiated loans*

The carrying amount for renegotiated financial assets by class is presented below:

In thousand Armenian drams	2009	2008
Manufacture	1,795,341	-
Agriculture	7,317	-
Construction	131,688	-
Trading	73,628	-
Consumer	6,926	-
Mortgage	54,057	-
Other	1,394,562	-
<b>Total renegotiated loans</b>	<b>3,463,519</b>	-

## 35.2 Market risk

Market risk is the risk that the fair value or future cash flows of financial instruments will fluctuate due to changes in market variables such as interest rates and foreign exchange rates. The Bank classifies exposures to market risk into either trading or non-trading portfolios. The market risk for the trading portfolio is managed and monitored based on a VaR methodology which reflects the interdependency between risk variables. Non-trading positions are managed and monitored using other sensitivity analyses.

### 35.2.1 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.



In thousand Armenian drams								2008
Currency	Change in basis points	Sensitivity of net interest income	Sensitivity of equity				Total	
			Up to 6 months	6 months to 1 year	1 year to 5 years	More than 5 years		
AMD	+1%	-	2	4	40	-	46	
USD	+1%	8	-	-	-	-	8	
AMD	-1%	-	(2)	(4)	(40)	-	(46)	
USD	-1%	(8)	-	-	-	-	(8)	

### 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 2009 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.

In thousand Armenian drams						
Currency	Change in currency rate in %	Effect on profit before tax	2009	Change in currency rate in %	Effect on profit before tax	2008
			Effect on equity			Effect on equity
USD	+5	(17,902)	(14,322)	+ 20	(105,028)	(84,024)
USD	-5	17,902	14,322	- 20	105,028	84,024
EUR	+8	(957)	(766)	+ 32	(7,204)	(5,764)
EUR	-8	957	766	- 32	7,204	5,764

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	5,705,408	11,419,701	236,123	17,361,232
Trading securities	275,915	-	-	275,915
Amounts due from other financial institutions	1,370,182	8,473,970	742,118	10,586,270
Loans and advances to customers	19,285,400	21,841,984	-	41,127,384
Investments available for sale	2,258,481	-	-	2,258,481
Securities pledged under repurchase agreements	2,323,985	-	-	2,323,985
	<u>31,219,371</u>	<u>41,735,655</u>	<u>978,241</u>	<u>73,933,267</u>
<b>LIABILITIES</b>				
Amounts due to financial institutions	8,053,326	1,261,370	115	9,314,811
Amounts due to customers	15,394,024	40,836,865	209,184	56,440,073
Debt securities issued	301,312	-	-	301,312
	<u>23,748,662</u>	<u>42,098,235</u>	<u>209,299</u>	<u>66,056,196</u>
<b>Net position as at 31 December 2009</b>	<u>7,470,709</u>	<u>(362,580)</u>	<u>768,942</u>	<u>7,877,071</u>
<b>Commitments and contingent liabilities as at 31 December 2009</b>	<u>2,360,792</u>	<u>3,612,530</u>	<u>-</u>	<u>5,973,322</u>

Total financial assets	38,755,599	25,292,140	924,419	64,972,158
Total financial liabilities	27,953,134	26,912,061	336,619	55,201,814
Net position as at 31 December 2008	10,802,465	(1,619,921)	587,800	9,770,344
Commitments and contingent liabilities as at 31 December 2008	4,403,145	1,129,526	29,342	5,562,013

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.

### 35.3 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 15. 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 2009 based on contractual undiscounted repayment obligations. See note 34 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	2009					Total
	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	
<b>FINANCIAL LIABILITIES</b>						
Amounts due to financial institutions	4,417,390	380,600	833,398	3,753,299	-	9,384,687
Amounts due to customers	30,733,808	6,749,620	14,719,888	5,020,171	348,545	57,572,032
Debt securities issued	-	7,783	23,610	331,480	-	362,873
<b>Total undiscounted financial liabilities</b>	<b>35,151,198</b>	<b>7,138,003</b>	<b>15,576,896</b>	<b>9,104,950</b>	<b>348,545</b>	<b>67,319,592</b>
<b>Commitments and contingent liabilities</b>	<b>8,459</b>	<b>558,972</b>	<b>2,976,570</b>	<b>2,429,321</b>	<b>-</b>	<b>5,973,322</b>

In thousand Armenian drams						2008
	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	5,203,435	333,897	3,141,375	1,553,352	-	10,232,059
Amounts due to customers	19,109,874	2,112,726	17,311,350	4,892,547	613,403	44,039,900
Debt securities issued	-	7,577	23,610	362,960	-	394,147
Trading liabilities	2,139,090	-	-	-	-	2,139,090
Total undiscounted financial liabilities	<u>26,452,399</u>	<u>2,454,200</u>	<u>20,476,335</u>	<u>6,808,859</u>	<u>613,403</u>	<u>56,805,196</u>
Commitments and contingent liabilities	<u>187,418</u>	<u>500,213</u>	<u>3,750,364</u>	<u>1,124,018</u>	<u>-</u>	<u>5,562,013</u>

### 36 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.

### 37 Segment reporting

#### *Operating segments*

The Bank is organised on the basis of three main operating segments. These operating segments are monitored and strategic decisions are made on the basis of segment operating results.

Retail banking – representing private banking services, private customer current accounts, savings, deposits, investment savings products, custody, credit and debit cards, consumer loans and mortgages.

Corporate banking – representing direct debit facilities, current accounts, deposits, overdrafts, loan and other credit facilities, foreign currency and derivative products.

Investment banking – representing financial instruments trading, structured financing, corporate leasing, and merger and acquisitions advice.

Transactions between the business segments are 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 capital. 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				2009
	Retail banking	Corporate banking	Investment banking	Total
Segment revenues	5,901,204	5,608,235	193,256	11,702,695
Segment costs and expenses	(3,921,673)	(4,721,544)	(1,212,741)	(9,855,958)
Profit/(loss) from operations	1,979,531	886,691	(1,019,485)	1,846,737
Impairment losses recognized in the statement of comprehensive income	(457,633)	(1,906,328)	-	(2,363,961)
Segment profit/(loss) before tax	1,521,898	(1,019,637)	(1,019,485)	(517,224)
Segment assets	25,641,667	20,597,736	28,075,173	74,314,576
Segment liabilities	22,023,302	33,342,321	10,914,610	66,280,233
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In thousand Armenian drams				2008
	Retail banking	Corporate banking	Investment banking	Total
Segment revenues	4,896,243	4,628,317	745,562	10,270,122
Segment costs and expenses	(2,861,880)	(2,765,651)	(1,144,120)	(6,771,651)
Profit/(loss) from operations	2,034,363	1,862,666	(398,558)	3,498,471
Impairment losses recognized in the statement of comprehensive income	(318,921)	(199,954)	(71,589)	(590,464)
Segment profit/(loss) before tax	1,715,442	1,662,712	(470,147)	2,908,007
Segment assets	20,026,902	23,267,175	20,936,308	64,230,385
Segment liabilities	18,016,572	24,210,251	14,061,570	56,288,393

*Reconciliations of operating segments revenues, profit or loss, assets and liabilities*

In thousand Armenian drams	2009	2008
<b>Revenues</b>		
Total segment revenues	11,702,695	10,270,122
Other unallocated revenues	-	-
<b>Total Bank's revenues</b>	<b>11,702,695</b>	<b>10,270,122</b>
<b>Profit(loss)</b>		
Total segment profit or loss before tax	(517,224)	2,908,007
Other income not allocated	-	-
Other expenses not allocated	(608,421)	(503,651)
<b>Bank's profit/(loss) before income tax</b>	<b>(1,125,645)</b>	<b>2,404,356</b>
<b>Assets</b>		
Total segment assets	74,314,576	64,230,385
Property, plant and equipment	3,711,424	3,886,295
Intangible assets	281,394	103,339
Other unallocated assets	348,362	1,009,480
<b>Bank's total assets</b>	<b>78,655,756</b>	<b>69,299,499</b>
<b>Liabilities</b>		
Total segment liabilities	66,280,233	56,288,393
Other unallocated assets	102,581	-
<b>Bank's total liabilities</b>	<b>66,382,814</b>	<b>56,288,393</b>

*Geographical information*

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

In thousand Armenian drams	2009			
	Armenia	Other non-OECD countries	OECD countries	Total
Revenues	10,742,450	424,195	536,050	11,702,695
Assets	73,029,929	1,263,026	4,362,801	78,655,756
Liabilities	47,237,599	5,091,348	14,053,867	66,382,814
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In thousand Armenian drams	2008			
	Armenia	Other non-OECD countries	OECD countries	Total
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

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



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