



Financial Statements and Independent Auditor's
Report

Aregak Universal Credit Organization closed joint
stock company

31 December 2008

Contents

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



Independent auditor's report

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To the Shareholder of Closed Joint Stock Company Aregak UCO:

We have audited the accompanying financial statements of Aregak UCO CJSC (the “Organization”), which comprise the balance sheet as at December 31, 2008, and the income statement, statement of changes in equity and cash flow statement for the year then ended, and a summary of significant accounting policies and other explanatory notes.

Management's responsibility for the financial statements

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

Auditor's responsibility

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

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the Organization'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 Organization's internal control.

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

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

Opinion

In our opinion, the financial statements give a true and fair view of the financial position of the Organization as of December 31, 2008, and of its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards.

Armand Pinarbasi, CA
Managing partner



Aren Aghajanyan
Head of Audit

Grant Thornton Amyot LLC
22 May 2009
Yerevan

Income statement

In thousand Armenian drams		Year ended December 31, 2008 (audited)	Year ended December 31, 2007 (audited)
	Notes		
Interest and similar income	6	2,020,750	1,442,603
Interest and similar expense	6	(506,276)	(232,056)
Net interest income		1,514,474	1,210,547
Fee and commission income	7	-	44,130
Fee and commission expense	7	(28,792)	(14,733)
Net fee and commission income		(28,792)	29,397
Gains less losses from transactions in foreign currencies		(961)	-
Other income	8	129,126	106,726
Impairment charge for credit losses	9	(63,889)	(30,087)
Staff costs	10	(723,293)	(641,448)
Depreciation of property and equipment	17	(45,932)	(19,999)
Amortization of intangible assets	18	(1,207)	(910)
Other expenses	11	(352,704)	(332,192)
Profit before income tax		426,822	322,034
Income tax expense	12	(131,525)	(98,041)
Profit for the year		295,297	223,993

The accompanying notes on pages 7 to 36 are an integral part of these financial statements.

Balance sheet

In thousand Armenian drams	Notes	As of December 31, 2008 (audited)	As of December 31, 2007 (audited)
ASSETS			
Cash on hand		6,804	9,544
Amounts due from other financial institutions	14	1,678,179	686,912
Loans held for sale	15	116,117	-
Loans and advances to customers	16	7,479,702	4,354,487
Property, plant and equipment	17	156,391	184,080
Intangible assets	18	9,939	11,146
Deferred income tax assets	12	413	109
Other assets	19	11,078	30,896
TOTAL ASSETS		9,458,623	5,277,174
LIABILITIES AND EQUITY			
Liabilities			
Amounts due to financial institutions	20	2,791,469	-
Borrowings	21	3,650,451	3,940,290
Current income tax liabilities		55,517	73,660
Other liabilities	22	43,350	17,244
Total liabilities		6,540,787	4,031,194
Equity			
Share capital	23	1,791,000	200,000
Statutory general reserve		22,127	3,892
Additional contribution		586,587	801,028
Retained earnings		518,122	241,060
Total equity		2,917,836	1,245,980
TOTAL LIABILITIES AND EQUITY		9,458,623	5,277,174

The financial statements from pages 3 to 36 were signed by the Organization's Executive Director and Finance Director on 22 May 2009. The accompanying notes on pages 7 to 36 are an integral part of these financial statements.



Signature of Armine Aghajanyan, Finance Director.

Statement of changes in equity

In thousand Armenian drams

	Share capital	Statutory general reserve	Additional contribution	Retained earnings	Total
Balance as of December 31, 2006 (audited)	<u>200,000</u>	<u>-</u>	<u>530,758</u>	<u>40,419</u>	<u>771,177</u>
Increase in capital as a result of borrowing received from the related party at below market interest rate (Note 21)	-	-	270,270	-	270,270
Total income and expense recognized directly in equity	-	-	270,270	-	270,270
Profit for the period	-	-	-	223,993	223,993
Total income and expense for the year	-	-	270,270	223,993	494,263
Distribution to reserve	-	3,892	-	(3,892)	-
Dividends to shareholders	-	-	-	(19,460)	(19,460)
Balance as of December 31, 2007 (audited)	<u>200,000</u>	<u>3,892</u>	<u>801,028</u>	<u>241,060</u>	<u>1,245,980</u>
Decrease in capital as a result of early repayment and change in interest rate of borrowing received from the related party at below market interest rate (Note 21)	-	-	(214,441)	-	(214,441)
Total income and expense recognized directly in equity	-	-	(214,441)	-	(214,441)
Profit for the year	-	-	-	295,297	295,297
Total income and expense for the year	-	-	(214,441)	295,297	80,856
Distribution to reserve	-	18,235	-	(18,235)	-
Increase in share capital	1,591,000	-	-	-	1,591,000
Balance as of December 31, 2008 (audited)	<u>1,791,000</u>	<u>22,127</u>	<u>586,587</u>	<u>518,122</u>	<u>2,917,836</u>

Statement of cash flows

In thousand Armenian drams	Year ended December 31, 2008 (audited)	Year ended December 31, 2007 (audited)
Cash flows from operating activities		
Interest received	1,986,069	1,415,460
Interest paid	(151,823)	(64,693)
Fees and commissions received	-	70,895
Fees and commissions paid	(36,607)	-
Salaries and benefits paid	(527,541)	(485,886)
Other taxes paid	(183,068)	(235,399)
Other income received	129,126	106,726
Other operating expenses paid	(311,263)	(287,480)
Cash flows from operating activities before changes in operating assets and liabilities	904,893	519,623
<i>Net (increase)/decrease in operating assets</i>		
Loans and advances to customers	(3,272,520)	(1,225,511)
Net cash flow used in operating activities before income tax	(2,367,627)	(705,888)
Income tax paid	(150,045)	(42,394)
Net cash used in operating activities	(2,517,672)	(748,282)
Cash flows from investing activities		
Long term deposits in banks	(1,453,210)	-
Purchase of property and equipment	(19,452)	(137,269)
Proceeds from the sale of property and equipment	292	-
Net cash used in investing activities	(1,472,370)	(137,269)
Cash flow from financing activities		
Proceeds from issue of share capital	1,591,000	-
Loans and borrowings received	1,933,826	1,360,000
Dividends paid to shareholders	-	(19,460)
Net cash flow from financing activities	3,524,826	1,340,540
Net increase(decrease) in cash and cash equivalents	(465,216)	454,989
Cash and cash equivalents at the beginning of the year	696,456	241,467
Effect of exchange rate changes on cash and cash equivalents	1,544	-
Cash and cash equivalents at the end of the year (Note 13)	232,784	696,456

Accompanying notes to the financial statements

1 Principal activities

Aregak Universal Credit Organization CJSC (the “Organization”) is a closed joint-stock company, which was incorporated in the Republic of Armenia in 2006. The Organization is regulated by the legislation of RA and conducts its business under license number 11, granted on 28 March 2006 by the Central Bank of Armenia (the “CBA”) and has started its activities on 1 May 2006.

The Organization is involved in microfinance and provides solidarity group-based micro credits, individual business and consumption loans and modified version of the group micro-loan, as well as other loans for the purchase of agricultural equipment in Armenia and Nagorno Karabakh. AREGAK UCO, headquarters in Yerevan, has 23 branches and 5 representative offices located throughout the twelve regions of Armenia and Nagorno Karabakh.

The registered office of the Organization is located at: 42/1 Arami str., Yerevan, Armenia, 0010.

2 Armenian business environment

Armenia continues to undergo political and economic changes. As an emerging market, Armenia does not possess a developed business and regulatory infrastructure that generally exists in a more mature free market economy. In addition, economic conditions continue to limit the volume of activity in the financial markets, which may not be reflective of the values for financial instruments. The main obstacle to further economic development is a low level of economic and institutional development, along with a centralized economic base and regional instability.

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

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

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

However, in times of more severe market stress, the Armenian economy as well as the Organization may be subject to that crisis and the effects of the crisis may be significant. 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 Organization may be affected.

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

3 Basis of preparation

3.1 Statement of compliance

The financial statements of the Organization 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.

3.3 Functional and presentation currency

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

3.4 Reclassifications

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

3.5 Adoption of new and revised standards

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

3.6 Standards and Interpretations not yet applied by the Organization

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 Organization has not early adopted any of these pronouncements.

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

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

IAS 1 Presentation of Financial Statements (revised 2007)

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

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

IAS 23 *Borrowing Costs* (revised 2007)

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

Based on Organization's current business model and accounting policies, management does not expect material impact on Organization's financial statements when these Standard, amendments and Interpretations to the existing Standards become effective.

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

IFRS 8 *Operating Segments*

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

IFRIC 13 *Customer Loyalty Programmes*

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

Amendment to IFRS 2 *Share-based Payment*

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

Annual improvements 2008

The IASB has issued *Improvements for International Financial Reporting Standards 2008*. Most of these amendments become effective in annual periods beginning on or after January 1, 2009. Management

believes that these improvements will not have significant impact on the Organization's financial statements.

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

The definition of borrowings costs has been amended so that interest expense is calculated using the effective interest rate method defined in IAS 39 *Financial Instruments: Recognition and Measurement* (effective from January 1, 2009). The Organization will apply the IAS 23 (Amendment) prospectively to the capitalization of borrowing costs from January 1, 2009.

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

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

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

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

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

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

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

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

The benefit of a below-market rate government loan is measured as the difference between the carrying amount in accordance with IAS 39 and the proceeds received with the benefit to be accounted for in accordance with IAS 20. The Organization will apply the IAS 20 (Amendment) from January 1, 2009.

4 Summary of significant accounting policies

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

4.1 Recognition of income and expenses

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

Interest income and expense

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

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

Fee and commission income and expense

Loan origination fees for loans issued to customers are deferred (together with related direct costs) and recognised as an adjustment to the effective yield of the loans. Fees, commissions and other income and expense items are generally recorded on an accrual basis when the service has been provided. Portfolio and other management advisory and service fees are recorded based on the applicable service contracts.

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.

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.

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 Organization in the preparation of the financial statements are as follows:

	December 31, 2008	December 31, 2007
AMD/1 US Dollar	306.73	304.22

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 Organization's activities. These taxes are included as a component of other expenses in the statement of income.

4.4 Cash and cash equivalents

Cash and cash equivalents comprise cash on hand and amounts due from 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 Financial instruments

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

Loans and receivables

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

Loans granted by the Organization 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.

4.6 Impairment of financial assets

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

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

under the contract. The Organization 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 Organization'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 Organization 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 Organization. If, in a subsequent year, the amount of the estimated impairment loss increases or decreases because of an event occurring after the impairment was recognized, the previously recognized impairment loss is increased or reduced by adjusting the allowance account. If future write-off is later recovered, the recovery is credited to the allowance account.

Renegotiated loans

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

4.7 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 Organization 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 Organization 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 Organization 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 Organization'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 Organization 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 Organization's continuing involvement is the amount of the transferred asset that the Organization 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 Organization's continuing involvement is limited to the lower of the fair value of the transferred asset and the option exercise price.

Financial liabilities

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

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

4.8 Leases

Operating - Organization as leasee

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

4.9 Property, plant and equipment

Property, plant and equipment ("PPE") are recorded at historical cost 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
Office equipment	5	20
Computers	3	33
Vehicles	5	20
Other fixed assets	5	20

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

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

4.10 Intangible assets

Intangible assets include computer software.

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 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.

4.11 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.

4.12 Borrowings

Borrowings, which include amounts due to shareholder and amounts received from financial and non financial institutions, 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.

4.13 Pensions

The Organization 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 Organization has no post-retirement benefits or significant other compensated benefits requiring accrual.

4.14 Provisions

Provisions are recognised when the Organization 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.

4.15 Share capital

Share capital

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

Dividends

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

4.16 Offsetting

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

5 Critical accounting estimates and judgements

The preparation of financial statements in conformity with IFRS requires management to make judgments, estimates and assumptions that affect the application of policies and the reported amounts of assets and liabilities, income and expense. The estimates and associated assumptions are based on historical experience and various other factors that are believed to be reasonable under the circumstances, the results of which form the basis of making the judgements about carrying values of assets and liabilities that are not readily apparent from other sources. Although these estimates are based on management's best knowledge of current events and actions, actual results ultimately may differ from these estimates.

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

Related party transactions

In the normal course of business the Organization 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 Organization 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 Organization 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 24.

6 Interest and similar income and expense

In thousand Armenian drams	2008	2007
Loans and advances to customers	1,904,006	1,435,984
Amounts due from other financial institutions	50,333	6,530
Loans held for sale	27,149	-
Interest accrued on impaired financial assets	39,262	89
Total interest and similar income	2,020,750	1,442,603

In thousand Armenian drams	2008	2007
Borrowings and loans	506,276	232,056
Total interest and similar expense	506,276	232,056

7 Fee and commission income and expense

In thousand Armenian drams	2008	2007
Portfolio service commission fees	-	44,130
Total fee and commission income	-	44,130

Portfolio service commission fees income represents income from managing loan portfolio of UMCOR, which did not exist during 2008.

In thousand Armenian drams	2008	2007
Bank service fees	28,792	14,733
Total fee and commission expense	28,792	14,733

8 Other income

In thousand Armenian drams	2008	2007
Fines and penalties received	128,684	104,851
Other income	442	1,875
Total other income	129,126	106,726

9 Impairment charge for credit losses

In thousand Armenian drams	2008	2007
Loans and advances to customers (Note 16)	63,889	30,087
Total impairment charge for credit losses	63,889	30,087

10 Staff costs

In thousand Armenian drams	2008	2007
Wages and salaries	653,827	577,954
Social security contributions	69,466	63,494
Total staff costs	723,293	641,448

11 Other expenses

In thousand Armenian drams	2008	2007
Fixed assets maintenance	76,210	83,580
Advertising costs and representative expenses	18,941	9,552
Business trip expenses	6,320	17,205
Communications	37,899	35,178
Operating lease	60,309	56,443
Taxes, other than income tax, duties	39,575	39,779
Consulting and other services	6,900	16,915
Security	47,656	42,705
Loss on disposal of PPE	184	-
Office supplies	10,390	13,207
Penalties paid	7,262	1,298
Foreign currency translation net losses of non-trading assets	577	-
Other expenses	40,481	16,330
Total other expense	352,704	332,192

12 Income tax expense

In thousand Armenian drams	2008	2007
Current tax expense	126,429	94,549
Adjustments of income tax of previous years	5,400	-
Deferred tax	(304)	3,492
Total income tax expense	131,525	98,041

The corporate income tax within the Republic of Armenia is levied at the rate of 20% (2007: 20%). Differences between IFRS and RA statutory tax regulations give rise to certain temporary differences between the carrying value of certain assets and liabilities for financial reporting purposes and for profit tax purposes. Deferred income tax is calculated using the principal tax rate of 20%.

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

In thousand Armenian drams	2008	Effective rate (%)	2007	Effective rate (%)
Profit before tax	426,822		322,034	
Income tax at the rate of 20%	85,364	20	64,407	20
Non-deductible expenses	40,646	10	33,634	10
Foreign currency translation net losses	115	-	-	-
Adjustments of income tax of previous years	5,400	-	-	-
Income tax expense	131,525	30	98,041	30

Deferred tax calculation in respect of temporary differences:

In thousand Armenian drams	2007	Recognized in income statement	2008
Accrued expenses and other liabilities	1,976	3,049	5,025
Total deferred tax assets	1,976	3,049	5,025
Allowances for impairment of other losses	(1,408)	(1,952)	(3,360)
Accrued interest on loans	(459)	(793)	(1,252)
Total deferred tax liability	(1,867)	(2,745)	(4,612)
Net deferred tax asset	109	304	413

In thousand Armenian drams	2006	Recognized in income statement	2007
Accrued expenses and other liabilities	4,138	(2,162)	1,976
Total deferred tax assets	4,138	(2,162)	1,976
Allowances for impairment of other losses	(537)	(871)	(1,408)
Accrued interest on loans	-	(459)	(459)
Total deferred tax liability	(537)	(1,330)	(1,867)
Net deferred tax asset	3,601	(3,492)	109

13 Cash and cash equivalents

In thousand Armenian drams	2008	2007
Cash on hand	6,804	9,544
Included in cash on hand	6,804	9,544
Placements with banks (Note 14)	225,980	686,912
Total cash and cash equivalents	232,784	696,456

14 Amounts due from other financial institutions

In thousand Armenian drams	2008	2007
Correspondent accounts with financial institutions	103,272	175,436
Deposits	122,708	511,476
Included in cash and cash equivalents	225,980	686,912
Deposits to financial institutions	1,452,199	-
Total amounts due from other financial institutions	1,678,179	686,912

During 2008, the Organization placed with and simultaneously received long-term funds from Armenian banks (these amounts are included in deposits to financial institutions). As of December 31, 2008, the Organization placed an equivalent of AMD 1,449,913 thousand (2007: nil) as deposits in USD with Armenian banks, which were related to loans received from the same banks (See Note 20).

15 Loans held for sale

On 07 October 2008 the Executive Administration of the Organization passed a resolution for selling part of its loan portfolio of Yerevan branch to Cascade Bank CJSC. Those loans are presented net of allowance for loan impairment amounting to AMD 2,460 thousand. The transaction was completed on 16 April 2009 (See Note 30).

16 Loans and advances to customers

In thousand Armenian drams	2008	2007
Loans to customers	7,604,537	4,417,893
Less allowance for loan impairment	(124,835)	(63,406)
Total loans and advances to customers	7,479,702	4,354,487

As of 31 December 2008 accrued interest income included in loans and advances to customers amounted to AMD 86,198 thousand (2007: AMD 43,216 thousand).

The loans to customers represent small loans to individuals involved in developing agriculture and in trade. The maximum limit of loans granted to an individual amounts to AMD 10,000 thousand.

Due to the small amount of individual loans there is no credit risk concentration.

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

In thousand Armenian drams	Industry	Trade	Construction	Consumer	Agriculture	Other	2008 Total
At 1 January 2008	795	24,950	508	-	29,129	8,024	63,406
Charge for the year	396	27,045	1,819	9,026	24,849	754	63,889
Transfer to loans held for sale	-	(1,865)	-	-	-	(595)	(2,460)
At 31 December 2008	<u>1,191</u>	<u>50,130</u>	<u>2,327</u>	<u>9,026</u>	<u>53,978</u>	<u>8,183</u>	<u>124,835</u>
Individual impairment	260	24,232	2,249	7,888	15,560	5,298	55,487
Collective impairment	931	25,898	78	1,138	38,418	2,885	69,348
	<u>1,191</u>	<u>50,130</u>	<u>2,327</u>	<u>9,026</u>	<u>53,978</u>	<u>8,183</u>	<u>124,835</u>
Gross amount of loans individually determined to be impaired, before deducting any individually assessed impairment allowance	<u>934</u>	<u>87,866</u>	<u>5,850</u>	<u>48,512</u>	<u>73,422</u>	<u>39,286</u>	<u>255,870</u>

In thousand Armenian drams	Industry	Trade	Construction	Consumer	Agriculture	Other	2007 Total
At 1 January 2007	96	3,258	102	-	23,227	6,636	33,319
Charge for the year	699	21,692	406	-	5,902	1,388	30,087
At 31 December 2007	<u>795</u>	<u>24,950</u>	<u>508</u>	<u>-</u>	<u>29,129</u>	<u>8,024</u>	<u>63,406</u>
Individual impairment	-	688	442	-	-	-	1,130
Collective impairment	795	24,262	66	-	29,128	8,024	62,276
	<u>795</u>	<u>24,950</u>	<u>508</u>	<u>-</u>	<u>29,128</u>	<u>8,024</u>	<u>63,406</u>
Gross amount of loans individually determined to be impaired, before deducting any individually assessed impairment allowance	<u>-</u>	<u>1,500</u>	<u>2,550</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>4,050</u>

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

In thousand Armenian drams	2008	2007
Privately held companies	44,825	61,644
Individuals	6,962,088	4,205,238
Sole proprietors	511,426	107,795
Accrued interest	86,198	43,216
	7,604,537	4,417,893
Less allowance for loan impairment	(124,835)	(63,406)
Total loans and advances to customers	7,479,702	4,354,487

At 31 December 2008 and 2007 the estimated fair value of loans and advances to customers approximates its carrying value. Refer to Note 26.

Credit, liquidity and interest rate analyses of loans and advances to customers are disclosed in Note 28. The information on related party balances is disclosed in Note 25.

17 Property, plant and equipment

In thousand Armenian drams	Buildings	Leasehold improvements	Communication devices & computers	Vehicles	Office equipment	Other PPE	Total
COST							
Cost at January 1, 2007	-	2,210	14,565	41,301	13,546	3,047	74,669
Additions	7,884	-	32,907	57,106	30,055	2,901	130,853
At December 31, 2007	7,884	2,210	47,472	98,407	43,601	5,948	205,522
Additions	1,163	140	16,106	-	1,431	612	19,452
Disposals	-	-	(852)	-	(306)	(405)	(1,563)
At December 31, 2008	9,047	2,350	62,726	98,407	44,726	6,155	223,411
DEPRECIATION							
At January 1, 2007	-	16	236	207	888	96	1,443
Depreciation charge	255	111	6,206	8,537	3,891	999	19,999
At December 31, 2007	255	127	6,442	8,744	4,779	1,095	21,442
Depreciation charge	422	116	16,313	19,694	8,200	1,187	45,932
Disposals	-	-	(156)	-	(63)	(135)	(354)
At December 31, 2008	677	243	22,599	28,438	12,916	2,147	67,020
CARRYING VALUE							
At December 31, 2008	8,370	2,107	40,127	69,969	31,810	4,008	156,391
At December 31, 2007	7,629	2,083	41,030	89,663	38,822	4,853	184,080

Fixed assets in the phase of installation

As at 31 December 2008 fixed assets included assets in the phase of installation in amount of AMD 5,448 thousand (2007: AMD 15,178 thousand), which are not amortized and are classified in accordance with their type.

As at 31 December 2008 fixed assets included fully depreciated and amortized assets in amount of AMD 115 thousand (2007: nil).

18 Intangible assets

In thousand Armenian drams	Acquired software
COST	
At January 1, 2007	5,648
Additions	6,416
At December 31, 2007	12,064
Additions	-
At December 31, 2008	12,064
AMORTISATION	
At January 1, 2007	8
Amortisation charge	910
At December 31, 2007	918
Amortisation charge	1,207
At December 31, 2008	2,125
CARRYING VALUE	
At December 31, 2008	9,939
At December 31, 2007	11,146

19 Other assets

In thousand Armenian drams	2008	2007
Prepayments and other debtors	3,387	812
Settlements with employees	27	192
Other assets	783	17,683
Other accounts receivable	-	565
	4,197	19,252
Materials	6,345	10,939
Other	536	705
Total other assets	11,078	30,896

20 Amounts due to financial institutions

In thousand Armenian drams	2008	2007
Loans from banks and financial institutions	2,791,469	-
Total amounts due to financial institutions	2,791,469	-

Loans from financial institutions include loans from HSBC Bank Armenia and Cascade Bank and from Oikocredit EDCS, U.A and Planet Finance NGO.

All loans from banks and financial institutions have fixed interest rates, except for the loan from Cascade Bank, which carries variable interest rate dependant upon change in exchange rate of USD to AMD .

During 2008, the Organization placed with and received long-term funds from Armenian banks in AMD (loans from financial institutions). As of December 31, 2008, the Organization received AMD 1,319,199 thousand (2007: nil) as loans from Armenian banks, which relate to deposits granted to the same banks (See Note 14)

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

21 Borrowings

In thousand Armenian drams	2008	2007
Loans	3,650,451	3,940,290
Total borrowings	3,650,451	3,940,290

Borrowings include a loan received during 2006 and 2007 from the sole shareholder of the Organization in the amount of AMD 4,510,000 thousand. The loan has been provided at below market rates, specifically at 2% p.a.

Since the beginning of 2008 the interest rate of the loan has been amended to 4.35 % p.a. There have also been early repayments of the loan during 2008 and 2009. Due to these substantial modifications of the terms of the loan agreement a new fair value of the loan as of 01.01.2008 has been calculated, equal to present value of future cash flows of the amended loan agreement discounted at 8% p.a.. This resulted in a decrease of additional contribution to equity of AMD 214,441 thousand presented in a statement of changes in equity. The unwinding of the gain in the year 2008 has resulted in interest expense of AMD 170,632 thousand (2007: 146,033).

Included in borrowing also a loan received from Oxfam-Novib Fonds in the amount of AMD 224,910 thousand.

Information on related party balances is disclosed in Note 25.

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

22 Other liabilities

In thousand Armenian drams	2008	2007
Accounts payables	8,815	9,852
Tax payable, other than income tax	12,215	798
Due to personnel	22,125	6,459
Other	195	135
Total other liabilities	43,350	17,244

23 Equity

As at 31 December 2008 the Organization's registered and paid-in share capital was AMD 1,791,000 thousand. In accordance with the Organization's statutes, the share capital consists of 8,955 ordinary shares, all of which have a par value of AMD 200 thousand each.

The sole shareholder of the Organization is the United Methodologist Committee on Relief.

As at 31 December 2008, the Organization did not possess any of its own shares.

In 2008 the shareholder of the Organization increased its share capital by AMD 1,591,000 thousand (2007: nil).

The share capital of the Organization 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 risks, including future losses and other unforeseen risks or contingencies. The reserve has been created in accordance with the Organization's statutes that provide for the creation of a reserve for these purposes of 15% of the Organization's share capital reported in statutory books.

24 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 Organization has complied with all regulations and has completely settled all its tax liabilities.

As of 31 December 2008 there were no legal actions and complaints taken against the Organization.

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

Operating lease commitments – Organization as a lessee

In the normal course of business the Organization enters into commercial lease agreements for office buildings and premises.

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

In thousand Armenian drams	2008	2007
Not later than 1 year	49,559	50,481
Later than 1 year and not later than 5 years	47,226	36,921
Total operating lease commitments	96,785	87,402

25 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 Organization's Management as well as other persons and enterprises related with and controlled by them respectively.

The Organization's only shareholder and its ultimate controlling party is United Methodologist Committee on Relief.

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

	2008	2007
Borrowings		
At the beginning of the period	3,940,290	2,683,197
Borrowings received during the year	115,800	1,257,093
Borrowings repaid during the year	(636,996)	-
At December 31	3,419,094	3,940,290
Interest expense on loans	363,311	232,056
Income statement items		
Fee and commission income	-	44,130

Borrowings represent the loan received from the sole shareholder. See Note 21 for more details. Fee and commission income represents income from managing loan portfolio of UMCOR.

Compensation of key management personnel was comprised of the following:

In thousand Armenian drams	2008	2007
Salaries and other short-term benefits	72,547	71,562
Social security costs	4,901	4,750
Total key management compensation	77,448	76,312

26 Fair value of financial instruments

Financial instruments not measured at fair value

The fair value of financial assets and liabilities, not presented on the Organization's balance sheet at their fair value, does not differ significantly from their carrying values.

In thousand Armenian drams	2008		2007	
	Carrying value	Fair value	Carrying value	Fair value
FINANCIAL ASSETS				
Cash	6,804	6,804	9,544	9,544
Amounts due from financial institutions	1,678,179	1,678,179	686,912	686,912
Loans held for sale	116,117	116,117	-	-
Loans and advances to customers	7,479,702	7,479,702	4,354,487	4,354,487
FINANCIAL LIABILITIES				
Amounts due to financial institutions	2,791,469	2,791,469	-	-
Borrowings	3,650,451	3,650,451	3,940,290	3,940,290

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 mainly are the same as rates in force..

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. The carrying amount of loans approximates their fair value.

Borrowings

The estimated fair value of borrowings not quoted in an active market is based on discounted cash flows using interest rates for new debts with similar remaining maturity. The carrying amount of borrowings approximates their fair value.

27 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 28.3 for the Organization's contractual undiscounted repayment obligations.

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
ASSETS								
Cash on hand	6,804	-	-	6,804	-	-	-	6,804
Amounts due from other financial institutions	228,266	-	-	228,266	1,449,913	-	1,449,913	1,678,179
Loans held for sale	-	-	116,117	116,117	-	-	-	116,117
Loans and advances to customers	760,648	1,335,673	4,150,849	6,247,170	1,231,477	1,055	1,232,532	7,479,702
	995,718	1,335,673	4,266,966	6,598,357	2,681,390	1,055	2,682,445	9,280,802
LIABILITIES								
Amounts due to financial institutions	15,650	-	14,989	30,639	2,760,830	-	2,760,830	2,791,469
Borrowings	6,447	1,339,468	265,293	1,611,208	2,039,243	-	2,039,243	3,650,451
	22,097	1,339,468	280,282	1,641,847	4,800,073	-	4,800,073	6,441,920
Net position	973,621	(3,795)	3,986,684	4,956,510	(2,118,683)	1,055	(2,117,628)	2,838,882
Accumulated gap	973,621	969,826	4,956,510		2,837,827	2,838,882		

In thousand Armenian drams									2007
	Demand and less than 1 month	From 1 to 3 months	From 3 to 12 months	Subtotal less than 12 months	From 1 to 5 years	More than 5 years	Subtotal over 12 months	Total	
ASSETS									
Cash on hand	9,544	-	-	9,544	-	-	-	9,544	
Amounts due from other financial institutions	686,912	-	-	686,912	-	-	-	686,912	
Loans and advances to customers	11,983	286,751	3,628,427	3,927,161	427,326	-	427,326	4,354,487	
	<u>708,439</u>	<u>286,751</u>	<u>3,628,427</u>	<u>4,623,617</u>	<u>427,326</u>	<u>-</u>	<u>427,326</u>	<u>5,050,943</u>	
LIABILITIES									
Borrowings	-	-	-	-	3,940,290	-	3,940,290	3,940,290	
	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>3,940,290</u>	<u>-</u>	<u>3,940,290</u>	<u>3,940,290</u>	
Net position	<u>708,439</u>	<u>286,751</u>	<u>3,628,427</u>	<u>4,623,617</u>	<u>(3,512,964)</u>	<u>-</u>	<u>(3,512,964)</u>	<u>1,110,563</u>	
Accumulated gap	<u>708,439</u>	<u>995,190</u>	<u>4,623,617</u>		<u>1,110,653</u>	<u>1,110,653</u>			

28 Risk management

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

The Organization'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 Organization regularly reviews its risk management policies and systems to reflect changes in markets, products and emerging best practice.

Risk management is carried out by a Risk Management and Financial Analysis Unit under policies approved by the Shareholder. The Risk Management Financial Analysis Unit identifies, evaluates and hedges financial risks in close co-operation with the Organization's operating units. The Shareholder approves written principles for overall risk management, as well as written policies covering specific areas. 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.

28.1 Credit risk

The Organization takes on exposure to credit risk, which is the risk that a counterparty will cause a financial loss for the Organization by failing to discharge an obligation. Credit risk is the most important risk for the Organization'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 Organization's asset portfolio. The credit risk management and control are centralised in credit risk management team of Organization's Credit Unit and reported to the Executive Administration of the Organization and head of each business unit regularly.

28.1.1 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 Organization at 31 December 2008 and 2007, without taking account of any collateral held or other credit enhancements attached. For on-balance-sheet assets, the exposures set out above are based on net carrying amounts as reported in the balance sheet.

In thousand Armenian drams	Notes	Gross maximum exposure as of December 31, 2008	Gross maximum exposure as of December 31, 2007
Amounts due from other financial institutions	14	1,678,179	686,912
Loans held for sale	15	116,117	-
Loans and advances to customers	16	7,479,702	4,354,487
Total credit risk exposure		9,273,998	5,041,399

28.1.2 Risk concentrations of the maximum exposure to credit risk

Geographical sectors

All of the Organization's assets are located in Armenia.

Industry sectors

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

In thousand Armenian drams	Financial institutions	Manuf acturing	Agriculture	Constru ction	Trade	Other	Total
Amounts due from other financial institutions	1,678,179	-	-	-	-	-	1,678,179
Loans held for sale	-	-	-	-	90,892	25,225	116,117
Loans and advances to customers	-	93,967	3,896,669	13,130	2,751,668	724,268	7,479,702
As at 31 December 2008	1,678,179	93,967	3,896,669	13,130	2,842,560	749,493	9,273,998
As at 31 December 2007	686,912	79,041	1,894,694	9,185	1,799,275	572,292	5,041,399

28.1.3 Risk limit control and mitigation policies

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

The Organization 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. 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 borrower and product are approved by the Credit Committee or Executive Body.

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 Organization 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 Organization implements guidelines on the acceptability of specific classes of collateral or credit risk mitigation.

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

In thousand Armenian drams	2008	2007
Loans collateralized by real estate	1,555,161	416,648
Loans collateralized by movable property	144,788	4,510
Vehicles	122,226	-
Loans collateralized by group guarantees	5,770,968	3,996,735
Other	11,394	-
Total loans and advances to customers (gross)	7,604,537	4,417,893

28.1.4 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 Organization addresses impairment assessment into areas: individually assessed allowances and collectively assessed allowances.

Individually assessed allowances

The Organization 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 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.

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	2008	2007
Loans and advances to customers		
Manufacturing	0.1%	-
Trade	0.3%	0.4%
Agriculture	0.2%	0.2%
Other	0.3%	0.1%

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					2008
	Less than 30 days	31 to 60 days	61 to 90 days	More than 91 days	Total
Loans and advances to customers					
Privately held companies	9,209	-	-	7,366	16,575
Individuals	122,573	26,845	7,102	49,460	205,980
Sole proprietors	17,125	752	-	11,271	29,148
Total	148,907	27,597	7,102	68,097	251,703

In thousand Armenian drams					2007
	Less than 30 days	31 to 60 days	61 to 90 days	More than 91 days	Total
Loans and advances to customers					
Privately held companies	-	-	-	2,407	2,407
Individuals	35,147	7,088	1,743	17,634	61,612
Total	35,147	7,088	1,743	20,041	64,019

The fair value of collateral that the Organization holds relating to past due loans at 31 December 2008 amounts to AMD 808,384 thousand (2007: AMD 345,077 thousand). The collateral consists of group guarantees and real estate.

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 255,870 thousand (2007: AMD 4,050 thousand) . Refer to Note 16. The fair value of collateral that the Organization holds relating to loans individually determined to be impaired at 31 December 2008 amounts to AMD 739,678 thousand (2007: AMD 2,238 thousand). The collateral consists of equipment and furniture.

28.2 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 Organization classifies exposures to market risk into non-trading portfolios. Non-trading positions are managed and monitored using sensitivity analyses. Except for the concentrations within foreign currency, the Organization has no significant concentration of market risk.

28.2.1 Market risk – Non-trading

Interest rate risk

Interest rate risk arises from the possibility that changes in interest rates will affect future cash flows or the fair values of financial instruments. The Organization's loan products do not have floating interest rates, therefore the greatest interest rate risk will occur if the external funding rates go up faster than the Organization can adjust its lending rates while considering local market rates. The Organization is mitigating this risk with external funding terms of 24-36 months and average terms of client loans of around 14 months.

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

The sensitivity of the income statement is the effect of the assumed changes in interest rates on the net interest income for one year, based on the floating rate non-trading financial assets and financial liabilities held at 31 December 2008, including the effect of hedging instruments.

In thousand Armenian drams		2008	
Currency	Change in basis points	Sensitivity of net interest income	
AMD	+0.8	(1,634)	
AMD	-0.9	3,547	

There is no interest rate risk as of 31 December 2007:

Currency risk

Currency risk is the risk that the value of a financial instrument will fluctuate due to changes in foreign exchange rates. Currently the Organization has a policy of fully covering the foreign exchange exposure. The outside funding in foreign currency is fully hedged by back to back transactions or through lending in foreign currency, matching foreign exchange denominated assets equal to foreign exchange liability exposure. As funding sources grow the Organization will identify specific limits of risk tolerance, like limiting the ratio of foreign exchange assets to foreign exchange liabilities for any particular time period to between 0.9-1.1, minimizing the mismatch of foreign exchange assets and liabilities risk exposure to 10%.

The tables below indicate the currencies to which the Organization had significant exposure at 31 December 2008 on its non-trading monetary assets and liabilities and its forecast cash flows. The analysis calculated the effect of a reasonably possible movement of the currency rate against the Armenian dram, with all other variables held constant on the income statement (due to the fair value of currency sensitive non-trading monetary assets and liabilities). 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	2008		2007		
	Currency	Change in currency rate in %	Effect on profit before tax	Change in currency rate in %	Effect on profit before tax
USD		22	20,080	-	-
USD		(22)	(20,080)	-	-

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

In thousand Armenian drams	Armenian Dram	Freely convertible currencies	Total
ASSETS			
Cash	6,804	-	6,804
Amounts due from other financial institutions	99,503	1,578,676	1,678,179
Loans held for sale	116,117	-	116,117
Loans and advances to customers	7,264,923	214,779	7,479,702
	<u>7,487,347</u>	<u>1,793,455</u>	<u>9,280,802</u>
LIABILITIES			
Amounts due to financial institutions	1,321,384	1,470,085	2,791,469
Borrowings	3,419,094	231,357	3,650,451
	<u>4,740,478</u>	<u>1,701,442</u>	<u>6,441,920</u>
Net position as at 31 December 2008	<u>2,746,869</u>	<u>92,013</u>	<u>2,838,882</u>
Total financial assets	-	-	-
Total financial liabilities	-	-	-
Net position as at 31 December 2007	-	-	-

There are no foreign currency assets and liabilities as of 31 December 2007.

Freely convertible currencies represent mainly US dollar amounts.

28.3 Liquidity risk

Liquidity risk is the risk that the Organization 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, manages assets with liquidity in mind, and monitors future cash flows and liquidity on a daily bases.

The liquidity management of the Organization 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.

The table below summarises the maturity profile of the Organization's financial liabilities at 31 December 2008 based on contractual undiscounted repayment obligations. See note 27 for the expected maturities of these liabilities.

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	Total
FINANCIAL LIABILITIES					
Amounts due to financial institutions	15,650	-	14,989	2,760,830	2,791,469
Borrowings	6,447	115,800	265,293	3,262,911	3,650,451
Total undiscounted financial liabilities	22,097	115,800	280,282	6,023,741	6,441,920
<hr/>					
In thousand Armenian drams					2007
	Demand and less than 1 month	From 1 to 3 months	From 3 to 12 months	From 1 to 5 years	Total
FINANCIAL LIABILITIES					
Borrowings	-	-	-	3,940,290	3,940,290
Total undiscounted financial liabilities	-	-	-	3,940,290	3,940,290

The Organization has received significant funds from its shareholder and financial and non-financial institutions. Any significant withdrawal of these funds would have an adverse impact on the operations of the Organization. Management believes that this level of funding will remain with the Organization for the foreseeable future and that in the event of withdrawal of funds, the Organization would be given sufficient notice so as to realise its liquid assets to enable repayment.

29 Capital adequacy

The Organization maintains an actively managed capital base to cover risks inherent in the business. The adequacy of the Organization'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 Organization.

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

The Organization 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 Organization may adjust the amount of dividend payment to shareholder, return capital to shareholder or issue capital securities. No changes were made in the objectives, policies and processes from the previous years.

Central Bank of Armenia requires minimal total capital of AMD 150,000 thousand.

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

30 Subsequent events

30.1 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 Organization in 2009 due to the fact that part of the debts of the Organization are denominated in USD. Refer to note 28.2.1 for the exchange rate risk of the Organization as of December 31, 2008.

On May 22, 2009 the following exchange rate was established:

AMD/1USD	372.37
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30.2 On 03 March 2009 and 14 April 2009 the Organization has increased its share capital by AMD 952,000 thousand and AMD 357,000 thousand respectively.

30.3 On 16 April 2009 the Organization sold part of its loan portfolio of Yerevan branch classified as held for sale for AMD 112,129 thousand to Cascade Bank CJSC. Gain on disposal amounting to AMD 1,216 thousand was recognized (See Note 15).



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