

FINCA AZERBAIJAN

Independent Auditor's Report

Financial Statements for the year ended 31 December 2008
Prepared under IFRS

Contents

Independent Auditor's Report	3
Financial Statements	
Balance Sheet	4
Income Statement	5
Statement of Cash Flows	6
Statement of Changes in Equity	7
Notes to Financial Statements	8 - 28

RSM Top-Audit

RSM Top-Audit

Bldg. 2, 54 Bolshaya Ordynka St.

Moscow 119017, Russia

Tel./fax: 7 (495) 363 2848 / 981 4121

www.top-audit.ru

Email: mail@top-audit.ru

27.10.2009 № 21-953

Independent Auditor's Report

To the Founders of FINCA Azerbaijan and the Board of Directors FINCA International, Inc. USA:

Report on the Financial Statements

We have audited the accompanying financial statements of FINCA Azerbaijan (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 include: designing, implementing and maintaining internal control relevant to the preparation and fair presentation of the 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 entity'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 entity'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 present fairly, in all material respects, the financial position of Organization as of December 31, 2008, and of its performance and cash flows for the year then ended in accordance with International Financial Reporting Standards.



PSM Top-Audit is an independent member firm of RSM International, an affiliation of independent accounting and consulting firms.

PSM Top-Audit is a member of the Association of Accountants - Auditors of the Commonwealth.

FINCA Azerbaijan
Balance Sheet as at December 31, 2008
(in US Dollars)

	Notes	December 31, 2008	December 31, 2007
ASSETS			
Non-current assets			
Intangible assets	2	2,185,144	61,348
Property and equipment	3	731,954	648,975
Loans to customers	4	12,914,015	7,962,988
Other receivables	5	279,283	384,342
Deferred tax assets	11	1,424,235	611,308
		17,534,631	9,668,961
Current assets			
Loans to customers	4	53,227,348	35,811,131
Other receivables	5	1,272,307	865,572
Prepaid and other assets		465,631	253,906
Cash and cash equivalents	6	3,383,055	3,042,317
		58,348,341	39,972,926
TOTAL ASSETS		75,882,972	49,641,887
EQUITY AND LIABILITIES			
EQUITY			
Share capital		5,000	5,000
Retained Earnings	15	12,051,608	8,603,357
TOTAL EQUITY		12,056,608	8,608,357
LIABILITIES			
Non-current liabilities			
Long-term borrowings	7	42,709,789	31,892,432
Deferred tax liabilities	11	455,232	130,349
		43,165,021	32,022,781
Current Liabilities			
Short-term borrowings	7	14,755,614	6,644,148
Trade and other payables	8	4,865,886	1,704,317
Taxes payable	9	179,250	109,411
Interest payable	10	860,593	552,873
		20,661,343	9,010,749
TOTAL LIABILITIES		63,826,364	41,033,530
TOTAL EQUITY AND LIABILITIES		75,882,972	49,641,887

On behalf of the Management

Jeffrey A Flowers
Country Director
See Notes to Financial Statements.

Manish Sane
Chief Financial Officer

FINCA Azerbaijan

Income Statement

For the year ended December 31, 2008

(in US Dollars)

	Notes	Year ended December 31, 2008	Year ended December 31, 2007
OPERATING REVENUE			
Income from portfolio		21,025,228	10,695,594
Commission fees	20	2,996,598	1,723,725
Penalty fees		75,420	224,857
Other income		64,275	29,625
		24,161,521	12,673,801
OPERATING EXPENSES			
Net impairment loss on financial assets	4	(179,675)	(398,525)
Financial costs	12	(5,164,854)	(2,389,873)
Foreign exchange gain		298,450	72,184
Personnel expenses	13	(10,334,047)	(4,384,052)
Operating expenses	14	(4,973,671)	(3,666,024)
Depreciation and amortization	3	(226,220)	(113,090)
		(20,580,017)	(10,879,380)
PROFIT BEFORE INCOME TAX		3,581,504	1,794,421
Income tax expense	11	(555,889)	(212,090)
PROFIT FOR THE PERIOD		3,025,615	1,582,331

On behalf of the Management

Jeffrey A Flowers

Country Director

See Notes to Financial Statements.

Manish Sane

Chief Financial Officer

FINCA Azerbaijan
Statement of Cash Flows
For the year ended December 31, 2008
(in US Dollars)

	Year ended December 31, 2008	Year ended December 31, 2007
CASH FLOWS FROM OPERATING ACTIVITIES		
Profit before tax	3,581,504	1,794,421
Adjustments to reconcile change in net assets to net cash provided by operating activities:		
Depreciation and amortization	226,220	113,090
Impairment on financial assets	179,675	398,525
Interest expenses	5,164,854	2,389,873
Profit of disposal assets	(105)	(98)
CHANGES IN WORKING CAPITAL:		
Increase in loans to customers	(22,546,921)	(26,049,752)
Increase in other receivables, prepaid and other assets	(513,401)	(535,170)
Increase in trade and other payables	3,161,569	738,191
Increase in taxes payable	109,275	(20,813)
Income tax paid	(1,083,366)	(661,782)
CASH USED IN OPERATING ACTIVITIES	(11,720,696)	(21,833,515)
CASH FLOWS FROM INVESTING ACTIVITIES		
Purchase of property and equipment:	(2,432,996)	(610,856)
Proceeds from sale of property and equipment	105	151
CASH USED IN INVESTING ACTIVITIES	(2,432,891)	(610,705)
CASH FLOWS FROM FINANCING ACTIVITIES		
Proceeds from equity contributed	422,636	-
Proceeds from borrowings	32,882,308	25,688,153
Interest paid	(18,810,619)	(2,110,516)
CASH FROM FINANCING ACTIVITIES	14,494,325	23,577,637
INCREASE IN CASH AND CASH EQUIVALENTS	340,738	1,133,417
Cash and Cash Equivalents		
Beginning	3,042,317	1,908,900
Ending	3,383,055	3,042,317

On behalf of the Management

Jeffrey A Flowers
Country Director

See Notes to Financial Statements.

Manish Sane
Chief Financial Officer

FINCA Azerbaijan

Statement of Changes in Equity

For the year ended December 31, 2008

(in US Dollars)

	Share capital	Retained earnings	Equity Contributed	Total equity
<i>Note</i>				
Balance at 31 December 2006	5,000	7,385,185	-	7,390,185
Prior period adjustments	20	(364,159)	-	(364,159)
Balance at 1 January 2007	5,000	7,021,026	-	7,026,026
Profit for the period	-	1,582,331	-	1,582,331
Balance at 31 December 2007	5,000	8,603,357	-	8,608,357
Balance at 1 January 2008	5,000	8,603,357	-	8,608,357
Equity contributed	15	-	422,636	422,636
Profit for the period	-	3,025,615	-	3,025,615
Balance at 31 December 2008	5,000	11,628,972	422,636	12,056,608

On behalf of the Management

Jeffrey A Flowers

Country Director

See Notes to Financial Statements.

Manish Sane

Chief Financial Officer

FINCA Azerbaijan

Notes to the Financial Statements for the year ended December 31, 2007

(in US Dollars)

Note 1. Nature of Activities and Significant Accounting Policies

Nature of Activities:

FINCA International, Inc. ("FINCA"), a not-for-profit organization, is incorporated in the USA. FINCA provides self-help opportunity by providing small loans to entrepreneurs and enterprises. Services are provided through affiliated organizations ("affiliates"). The affiliates are typically separate legal entities operating under affiliation agreements with FINCA International.

FINCA Azerbaijan Limited Liability Non-Bank Credit Organization ("the Organization") is the affiliate of FINCA in Azerbaijan. Under the management of its regional hub headquartered in Kiev, Ukraine ("FINCA HUB"), the Organization carries out its operations.

The Organization's mission is to provide financial services to Azerbaijan's lowest-income entrepreneurs so they can create jobs, build assets and improve their standard of living. Loans are provided to individual clients, often members of self-organized 'solidarity groups' organized to provide a mechanism to secure loans through joint-and-several liability.

The Organization was established in April 1998 and started its lending operations in June 1998. Until 19 November 1999 it was registered as a representative office of FINCA in Azerbaijan ("the representative office"). On 19 November, 1999, the Organization was registered with the Azerbaijan Ministry of Justice and obtained the status of a legal entity. The Organization was reregistered to comply with the regulations of the National Bank of Azerbaijan, in accordance with which only legal entities can perform lending activities on the territory of Azerbaijan. The new entity obtained a license for lending activities from the National Bank of Azerbaijan on 29 February, 2000.

Operating Environment - Over recent years, Azerbaijan has undergone substantial political and economic changes. As an emerging market, Azerbaijan does not possess a well-developed commercial infrastructure, which generally exists in more mature business markets. Laws and regulations affecting businesses operating within the country, as well as throughout the Commonwealth of Independent States ("CIS"), are subject to rapid change. In addition, continued economic stability is dependent to a large extent on the effectiveness of fiscal measures taken by the government, decisions of international lending organizations, and other actions beyond the Organization's control.

Although recently there have been positive economic signs in Azerbaijan, the long-term prospects for the Azeri economy remain uncertain. As a result, the Organization's assets and operations could be at risk if there are any adverse changes in the political and business environment.

Taxation and Other Statutory Regulations - In accordance with the Agreement between the Government of the United States of America and Government of the Republic of Azerbaijan Regarding Cooperation to Facilitate the Provision of Assistance signed on 11 May 2000, for the period from April 1998 to 31 December, 2005, the Organization was defined as an operator responsible for the implementation of U.S. Government assistance programs and as such was not liable for income tax, value added tax, social and pension contributions or any other taxes derived from any activities related to grants received from the U.S. Government. The Organization became a normal taxpayer as the agreement with USAID ended on 31 December 2005, but continued to enjoy relief from social and pension contributions as a participant in the State Program for Internally Displaced Persons. The State Program is a government initiative, based on a Presidential Decree issued in 2004. The State Program is administered by the Republic of Azerbaijan, Cabinet of Ministers, Office of the Deputy Prime Minister, which is empowered to define the organizations participating in the program, and which qualify for exemptions from social fund contributions. The Office of the Deputy Prime Minister has defined the Organization as a participant in the program, and has provided the relevant documentation confirming the Organization's exemption from social security contributions. The exemption has been confirmed in writing by the Social Protection Fund.

Based on an inspection conducted in December, 2008, the Social Protection Fund has challenged the Organization's exemption from social fund contributions for the period from 1 January, 2007 to 31 December, 2008. The Organization has formally disputed the findings of the audit. The matter is currently under discussion between the parties. (See Note 19 below.) The Azerbaijan tax authorities are increasingly directing their attention to the business community as a result of the overall economic environment. In respect of this, the local and national tax environments in Azerbaijan are constantly changing and subject to inconsistent application, interpretation and enforcement. Non-compliance with Azerbaijan laws and regulations can lead to the imposition of severe penalties and interest. Future tax examinations could assess additional taxes, penalties and interest, and these amounts could be material. The Organization believes it has complied with all applicable regulations and requirements. However, since the regulations are not always clearly written, it is difficult to predict future interpretations by regulatory authorities, and outcomes of such interpretations.

FINCA Azerbaijan
Notes to the Financial Statements for the year ended December 31, 2007
(in US Dollars)

Note 1. Nature of Activities and Significant Accounting Policies (Continued)

A summary of FINCA's significant accounting policies follows:

Basis of accounting: The financial statements have been prepared in accordance with International Financial Reporting Standards ("IFRS"), including International Accounting Standards and Interpretations issued by the International Accounting Standards Board and the International Financial Reporting Interpretations Committee.

Cash and cash equivalents: FINCA considers all highly liquid investments with an original maturity of three months or less to be cash equivalents.

Loans and advances receivables: Loans and advances to customers are stated at the unpaid principal balance less provisions for loan losses. FINCA estimates amounts of possible losses on loans and advances at the statement of financial position date to determine the provisions, and believes they are reasonable, having regard to the risks in lending in its market. FINCA recognizes that economic and regulatory conditions may have an impact on the debtors' ability to repay loans.

All delinquent loans are provided for by specific provisions using prescribed percentages depending on overdue days. In determining its specific provision FINCA classifies loans and advances into categories based on aging analysis and applies the following minimum rates:

Overdue days	Prescribed percentages for creation specific provisions
1 - 7 days past due	1 %
8 - 30 days past due	10 %
31 - 60 days past due	25 %
61-90 days past due	50 %
91-180 days past due	75 %
181 or more days past due	100 %

FINCA also maintains a minimum general provision of 1 % against the current loan portfolio at the end of each month.

Loans are considered overdue if any payment has fallen due and remained unpaid. Loan payments are applied first to any penalty fines due, then to interest due, and then to any installment of principal that is due but unpaid, beginning with the earliest such installment. The number of days of lateness is based on the due date of the earliest loan installment that has not been fully paid.

The amount of interest accrued as of December 31, 2008 is \$ 998,537 (as of December 31, 2007: \$ 608,128).

At the time a loan is deemed doubtful, or management believes the contractual interest or principal due will not be collected, the loan is classified as non-performing and any interest accrued is reversed. As at December 31, 2008 the allowance for doubtful accounts was \$ 708,230 (As at December 31, 2007: \$ 510,992).

Loans overdue for more than 180 days are written-off as unrecoverable. Loans are written-off before reaching 180 days overdue if it is determined that they are unrecoverable.

The Organization does not accrue interest on loans with payments more than 30 days overdue.

Property and equipment:

Until end of 2005, the Organization capitalized all assets with purchase price of \$5000 or more. Since January 1, 2006 the policy of recognizing and recording Fixed Assets has been aligned with the statutory accounting which mandates a capitalization threshold of AZN 110 (approximately \$138).

Property and equipment is stated at cost and depreciated on a straight-line basis over the estimated useful life of the assets.

FINCA Azerbaijan
Notes to the Financial Statements for the year ended December 31, 2007
(in US Dollars)

Note 1. Nature of Activities and Significant Accounting Policies (Continued)

Revenue and support: Interest income and upfront commission fee (*collected on the day of disbursement of loan to customers*) is amortized over the period of loan using a method close to effective interest rate method as suggested by IAS 18 read with IAS 39, where commission fee revenue is recognized using same proportion to the interest income recognized.

Foreign currency translation: For the purpose of these financial statements the functional currency is US dollars.

The financial statements and transactions of FINCA's foreign operations are generally maintained in the relevant local currency.

At each balance sheet date (a) local currency monetary items are translated into U.S. dollars using the closing rate; (b) non-monetary items that are measured in terms of historical cost in foreign currency are translated into U.S. dollars using the exchange rate at the date of the transaction. Revenues and expenses are translated at the average exchange rate for each period.

Exchange differences arising on the settlement of monetary items or on translating rate monetary items at rates different from those at which they were translated on initial recognition during the period or in previous financial statements are recognized in profit or loss in the period in which they arise.

The exchange rate as of December 31, 2008 and 2007 was AZN 0.8010 and AZN 0.8453 to \$ 1 respectively. The average AZN/USD exchange rates for the years ended December 31, 2008 and 2007 were 0.82315 and 0.8584, respectively. The translation of AZN-denominated assets and liabilities into USD as of 31 December does not indicate that the Organization could realize, or settle in USD, the translated value of these assets and liabilities.

Income tax: The income tax expense represents the sum of the tax currently payable and deferred income tax. The tax currently payable is based on taxable profit for the year. Taxable profit differs from net profit as reported in the income statement because it excludes items of income or expense that are taxable or deductible in other years and it further excludes items that are never taxable or deductible. The company's liability for current tax is calculated using tax rates in force as of the balance sheet date.

Deferred income tax is provided using the balance sheet liability method for tax loss carry forwards and temporary differences arising between the tax bases of assets and liabilities and their carrying amounts for financial reporting purposes. In accordance with the initial recognition exemption, deferred taxes are not recorded for temporary differences on initial recognition of an asset or a liability in a transaction other than a business combination if the transaction, when initially recorded, affects neither accounting nor taxable profit.

Deferred tax balances are measured at tax rates enacted or substantively enacted at the balance sheet date which are expected to apply to the period when the temporary differences will reverse or the tax loss carry forwards will be utilized. Deferred tax assets for deductible temporary differences and tax loss carry forwards are recorded only to the extent that it is probable that future taxable profit will be available against which the deductions can be utilized.

Estimates: The preparation of the financial statements requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, and disclosures of contingent assets and liabilities at the date of the financial statements, and the reported amounts of support and revenue and expenses during the reporting period. Actual results could differ from those estimates.

FINCA Azerbaijan
Notes to the Financial Statements for the year ended December 31, 2007
(in US Dollars)

Note 2. Intangible Assets

	Capitalized Software	2008 Capital Work in Progress	Total	2007 Capitalized Software	Total
Cost					
Balance at 1 January	123,144	-	123,144	57,439	57,439
Acquisitions	1,859	2,142,347	2,144,206	65,705	65,705
Balance at 31 December	125,003	2,142,347	2,267,350	123,144	123,144
Amortization and impairment					
Balance at 1 January	61,796	-	61,796	40,076	40,076
Amortization for the period	20,410	-	20,410	21,720	21,720
Impairment loss	-	-	-	-	-
Balance at 31 December	82,206	-	82,206	61,796	61,796
Carrying amounts					
Balance at 1 January	61,348	-	61,348	17,363	17,363
Balance at 31 December	42,797	2,142,347	2,185,144	61,348	61,348

Capital work in progress was made for the being implemented banking operation system.

Note 3. Property and equipment

Property and equipment and accumulated depreciation at December 31, 2008 and at December 31, 2007 consist of the following:

	Leasehold Improvements	IT equipment	Construction in progress	Furniture and office equipment	Vehicles and fittings	Total
Cost						
Balance January 1, 2007	16,621	119,104	-	153,238	18,900	287,863
Acquisitions	-	195,649	-	217,216	132,285	545,150
Disposals	-	(2,627)	-	-	-	(2,627)
Balance December 31, 2007	16,621	312,126	-	370,454	151,185	850,386
Balance January 1, 2008	16,621	312,126	-	370,454	151,185	850,386
Acquisitions	-	88,038	65,344	135,407	-	288,789
Disposals	-	(882)	-	-	-	(882)
Balance December 31, 2008	16,621	399,282	65,344	505,861	151,185	1,138,293
Depreciation and impairment losses						
Balance January 1, 2007	5,725	71,176	-	28,758	6,957	112,616
Depreciation for the period	4,757	32,591	-	44,685	9,336	91,369
Disposals	-	(2,574)	-	-	-	(2,574)
Balance December 31, 2007	10,482	101,193	-	73,443	16,293	201,411
Balance January 31, 2008	10,482	101,193	-	73,443	16,293	201,411
Depreciation for the period	6,139	88,510	-	83,163	27,998	205,810
Disposals	-	(882)	-	-	-	(882)
Balance December 31, 2008	16,621	188,821	-	156,606	44,291	406,339
Carrying amounts						
Balance January 1, 2007	10,896	47,928	-	124,480	11,943	195,247
Balance December 31, 2007	6,139	210,933	-	297,011	134,892	648,975
Balance December 31, 2008	-	210,461	65,344	349,255	106,894	731,954

There were not non-cash acquisitions of Property and equipment in 2008 & 2007. Management assessed the condition of the existing fixed assets and concluded that an impairment charge is not required, as at December 31, 2008 and as at December 31, 2007.

FINCA Azerbaijan

Notes to the Financial Statements for the year ended December 31, 2007

(in US Dollars)

Note 4. Loans to customers

Loans to customers are made within Azerbaijan, in cities including Baku, Agdash, Agstafa, Barda, Gazakh Guba, Imishli, Masalli, Gandja, Sheki, Sumgayit, and Naxichivan, as well as in rural areas.

The loan life for group loans is ranges up to 12 months. The principal and interest amounts for group loans are redeemable weekly, bi-weekly or monthly by equal installments. Interest on group loans is charged on the remaining balance of the loan after each repayment of principal, i.e. on a declining basis.

The loan life for individual loans ranges up to 24 months. The principal and interest amounts for individual loans are redeemable monthly. Interest on loans to individuals is charged on the remaining balance of the loan after each repayment of principal, i.e. on a declining basis.

The group loans are secured by Solidarity Group Guarantee. The individual loans are secured by movable & immovable property such as cars, equipment, home appliances, other household assets, and/or by gold items. Some individual loans are secured by the pledge of a third-party guarantor.

Loans and advances receivable at December 31, 2008 consist of the following:

	December 31, 2008	December 31, 2007
Loans to customers (current)	53,805,133	36,241,689
Loans to customers (non-current)	13,044,460	8,043,422
Loans to customers subtotal	66,849,593	44,285,111
Less provision for doubtful accounts of current loans to customers	(577,785)	(430,557)
Less provision for doubtful accounts of non-current loans to customers	(130,445)	(80,434)
Less provision for doubtful accounts subtotal	(708,230)	(510,992)
Net carrying amount of Loans to customers	66,141,363	43,774,119

The aging of those loans receivables at December 31, 2008 consist of the following:

Normal loans	Portfolio at risk	Amount	% for creation specific provisions	Provision
Current	99.73%	66,667,664	1%	665,496
1 - 7 days past due (including restructured)	0.13%	86,638	1%	866
8 - 30 days past due	0.03%	22,262	10%	2,226
31 – 60 days past due	0.03%	17,971	25%	4,493
61 – 90 days past due	0.05%	33,140	50%	16,570
91 - 180 days past due	0.02%	13,354	75%	10,015
181 or more days past due	0.01%	8,564	100%	8,564
Total	-	66,849,593	-	708,230

FINCA Azerbaijan
Notes to the Financial Statements for the year ended December 31, 2007
(in US Dollars)

Note 4. Loans to customers (continued)

The aging of those loans receivables at December 31, 2007 consist of the following:

Normal loans	Portfolio at risk	Amount	% for creation specific provisions	Provision
Current	99.60%	44,109,720	1%	441,097
1 - 7 days past due (including restructured)	0.09%	41,567	1%	416
8 - 30 days past due	0.07%	30,008	10%	3,001
31 – 60 days past due	0.05%	22,469	25%	5,617
61 – 90 days past due	0.03%	14,898	50%	7,449
91 - 180 days past due	0.12%	52,149	75%	39,112
181 or more days past due	0.03%	14,300	100%	14,300
Total		44,285,111	-	510,992

The change in the loan loss provision for the year ended December 31, 2008, consists of the following:

	Year ended December 31, 2008	Year ended December 31, 2007
Beginning balance	510,992	462,132
Current year allowance for doubtful accounts of loans to customers	179,675	398,525
Recovery of losses	133,477	138,008
Write offs	(115,914)	(487,672)
Total	708,230	510,992

Note 5. Other Receivables

The Organization's loan products are not available to employees. The only exception to this is a loan facility that is made available to operations personnel for the purpose of purchasing an automobile that will be used for FINCA business purposes as required. The interest rate on auto loans to employees is 11% per annum. Automobile loans can be made with maturities of up to 60 months. Loans are be made and repaid in Azerbaijani manats. The maximum automobile loan size is 6,000 AZN.

Accounts receivable at December 31, 2008, consist of the following:

	December 31, 2008	December 31, 2007
CURRENT		
Interest income accrued on loans to customers	998,537	608,128
Auto loans to employees	238,250	221,081
Employee Advances	29,147	35,682
Other Account receivable	6,373	681
	1,272,307	865,572
NON-CURRENT		
Auto loans to employees	279,283	384,342
	279,283	384,342

FINCA Azerbaijan
Notes to the Financial Statements for the year ended December 31, 2007
(in US Dollars)

Note 6. Cash and cash equivalents

	December 31, 2008	December 31, 2007
Cash in bank	3,269,229	2,960,710
Cash on hand	113,827	81,607
Total cash and cash equivalents	3,383,055	3,042,317

As of December 31, 2008 and as of December 31, 2007 the sum of cash and cash equivalents in local currency is \$ 664,844 and \$ 479,274 respectively, the sum of cash and cash equivalents in USD is \$ 2,718,212 and \$ 2,563,043.

Note 7. Borrowings /Notes Payable

Long-term notes payable as of December 31, 2008 consist of the following:

Lender	Interest rate (<i>contractual / net of taxes</i>)	Secured	Unsecured	December 31, 2008	December 31, 2007
Notes Issuer 1	10.40%		6,970,150	6,970,150	9,706,717
Notes Issuer 2	8.75%		2,550,001	2,550,001	285715
Notes Issuer 3	8.83%		9,100,000	9,100,000	8900000
Notes Issuer 4	8.50%		8,000,000	8,000,000	5,000,000
Notes Issuer 5	8.50%		1,000,000	1,000,000	1,000,000
Notes Issuer 6	5% + LIBOR		2,000,000	2000000	3,000,000
Notes Issuer 7	9.50%		3,000,000	3,000,000	3,000,000
Notes Issuer 8	8.75%		1,000,000	1,000,000	1,000,000
Notes Issuer 9	15.00%		-	-	-
Notes Issuer 10	0.00%		-	-	-
Notes Issuer 11	15.00%		-	-	-
Notes Issuer 12	9.00%		1,000,000	1,000,000	-
Notes Issuer 13	11.00%		6,089,638	6,089,638	-
Notes Issuer 14	9.00%		2,000,000	2,000,000	-
Total long-term borrowings		0	42,709,789	42,709,789	31,892,432

FINCA Azerbaijan
Notes to the Financial Statements for the year ended December 31, 2007
(in US Dollars)

Note 7. Borrowings / Notes Payable (continued)

Short-term notes payable as of December 31, 2008 consist of the following:

Lender	Interest rate (<i>contractual / net of taxes</i>)	Secured	Unsecured	December 31, 2008	December 31, 2007
Notes Issuer 1	10.40%		2,319,900	2,319,900	2,718,283
Notes Issuer 2	8.75%	217,857	217,857	935,714	285,714
Notes Issuer 3	8.83%		6,500,000	6,500,000	1,900,000
Notes Issuer 4	8.50%		-	-	-
Notes Issuer 5	8.50%		2,000,000	2,000,000	500,000
Notes Issuer 6	5% + LIBOR		1,000,000	1,000,000	-
Notes Issuer 7	9.50%		-	-	-
Notes Issuer 8	8.75%		1,000,000	1,000,000	-
Notes Issuer 9	15.00%		-	-	1,183,012
Notes Issuer 10	0.00%		-	-	57,139
Notes Issuer 11	15.00%		-	-	-
Notes Issuer 12	9.00%		1,000,000	1,000,000	-
Notes Issuer 13	11.00%		-	-	-
Notes Issuer 14	9.00%		-	-	-
Total short-term borrowings		217,857	14,037,757	14,755,614	6,644,148

Maturities of notes payable at December 31, 2008, are due in future fiscal years as follows:

Years ending December 31,	2008	2007
2009	14,755,614	12,105,615
2010	19,549,780	8,719,900
2011	17,679,659	8,319,900
2012	5,330,350	2,747,017
2013	150,000	-
Total borrowings	57,465,403	31,892,432

Out of the above notes payable, at 31st December 2008, \$ 1,000,000 is in the "Subordinated" type and rest are of the "Senior" type. As at 31st December 2007 \$ 0 was in "Subordinated" type and all are of the "Senior" type.

The Organization is current in all its payment obligations with respect to the notes payable.

As of December 31, 2008 and as of December 31, 2007 total notes payable in local currency are \$ 6,089,638 and \$ 1,240,151 respectively, total notes payable in USD are \$ 51,375,765 and \$ 37,296,430.

FINCA Azerbaijan
Notes to the Financial Statements for the year ended December 31, 2007
(in US Dollars)

Note 8. Trade and other Payables

	December 31, 2008	December 31, 2007
Social security obligations	2,823,988	-
Deferred commission fee (<i>see note 1</i>)	1,396,826	1,036,782
Accrued payroll	396,830	269,716
Royalty payable to FINCA	163,741	369,819
Vendor payables	50,501	-
Audit fee payable	34,000	28,000
Total	4,865,886	1,704,317

As of December 31, 2008 the Organization has the balance of trade payables and accrued expenses in local currency in the amount of \$ 3,483,286 (as of December 31, 2007: \$ 593,075) and in USD in the amount of \$ 197,741 (as of December 31, 2007: \$ 397,819).

Note 9. Taxes payable

	December 31, 2008	December 31, 2007
Provision for profit tax	56,276	95,712
Other taxes	122,974	13,699
Total taxes payable	179,250	109,411

As of December 31, 2008 and as of December 31, 2007 the Organization has all balances of taxes payable in the local currency.

Note 10. Interest payable

	December 31, 2008	December 31, 2007
Notes Issuer 1	-	100,902
Notes Issuer 2	80,381	6,764
Notes Issuer 3	393,208	220,388
Notes Issuer 4	122,043	75,114
Notes Issuer 5	36,771	38,520
Notes Issuer 6	68,845	81,601
Notes Issuer 7	-	18,247
Notes Issuer 8	-	-
Notes Issuer 9	-	11,337
Notes Issuer 10	-	-
Notes Issuer 11	-	-
Notes Issuer 12	47,000	-
Notes Issuer 13	112,248	-
Notes Issuer 14	97	-
Total Interest payable	860,593	552,873

The Organization has balance of interest payable in the amount as of December 31, 2008 \$112,248 and as of December 31, 2007 \$ 11,337 in local currency (AZN), other balances of interest payable in USD.

FINCA Azerbaijan
Notes to the Financial Statements for the year ended December 31, 2007
(in US Dollars)

Note 11. Income tax

Income tax charge	Year ended December 31, 2008	Year ended December 31, 2007
Current income tax charge	(1,043,934)	(429,696)
Deferred tax expense relating to the origination and reversal of temporary differences	488,045	217,605,
Total income tax charge	(555,889)	(212,090)

During 2008 the Organization was subject to a 22% income tax rate on taxable profits (2007: 22%).

Net profit before income tax for financial reporting purposes is reconciled to income tax expenses as follows:

	Year ended December 31, 2008	Year ended December 31, 2007
Profit before income tax		
Theoretical tax (charge) at statutory tax rate of 22 percent	(787,931)	(394,773)
Tax effect of items which are not deductible or assessable for taxation purposes	232,042	182,683
Total income tax charge	(555,889)	(212,090)

Deferred income tax: Differences between IFRS and statutory taxation regulations give rise to certain temporary differences between the carrying value of certain assets and liabilities for financial reporting purposes and for tax purposes. Deferred tax assets and liabilities are measured at 22 percent, the rate applicable when the asset or liability will reverse.

Deferred income tax liabilities as at December 31, 2008:

	December 31, 2007	Movement for the period recognized in the Income Statement	December 31, 2008
Other receivables	130,349	85,886	216,235
Intangible assets	-	238,997	238,997
Total	130,349	324,883	455,232

Deferred income tax assets as at December 31, 2008:

	31 December, 2007	Movement for the period recognized in the Income Statement	31 December, 2008
Trade and other payables	374,950	695,544	1,070,494
Interest payable	121,632	67,699	189,331
Loans to customers	112,418	43,393	155,811
Property and equipment	2,308	5,003	7,311
Prepaid and other assets	-	1,288	1,288
Total	611,308	812,927	1,424,235

FINCA Azerbaijan
Notes to the Financial Statements for the year ended December 31, 2007
(in US Dollars)

Note 11. Income tax (continued)

Deferred income tax liabilities as at December 31, 2007:

	December 31, 2006	Movement for the period recognized in the Income Statement	December 31, 2007
Loans to customers	130,760	(130,760)	-
Other receivables	-	130,349	130,349
Total	130,760	(411)	130,349

Deferred income tax assets as at December 31, 2007:

	December 31, 2006	Movement for the period recognized in the Income Statement	December 31, 2007
Trade and other payables	294,807	80,143	374,950
Interest payable	60,174	61,458	121,632
Property and equipment	39,133	(36,825)	2,308
Loans to customers	-	112,418	112,418
Total	394,114	217,194	611,308

Note 12. Financial cost

	Year ended December 31, 2008	Year ended December 31, 2007
Notes Issuer 1	1,297,730	1,056,642
Notes Issuer 2	247,047	67,423
Notes Issuer 3	1,338,916	410,150
Notes Issuer 4	636,986	385,872
Notes Issuer 5	233,729	69,558
Notes Issuer 6	285,061	241,680
Notes Issuer 7	301,774	122,643
Notes Issuer 8	165,669	24,568
Notes Issuer 9	33,914	11,337
Notes Issuer 10	-	-
Notes Issuer 11	18,053	-
Notes Issuer 12	144,652	-
Notes Issuer 13	403,055	-
Notes Issuer 14	58,268	-
Total financial cost	5,164,854	2,389,873

Withholding taxes and commission fees are included in the content of the other financial costs. As at 31 December 2008 withholding taxes are accrued in the amount of \$375,553, commission fees and other costs are accrued in the amount of \$112,000. The withholding taxes were paid to tax authorities in the moment of interest payment to the lenders. As at 31 December 2007 withholding taxes are accrued in the amount of \$ 78,024 and commission fees are accrued in the amount of \$ 18,394. The withholding taxes were paid to tax authorities in the moment of interest payment to the lenders.

FINCA Azerbaijan
Notes to the Financial Statements for the year ended December 31, 2007
(in US Dollars)

Note 13. Personnel Expenses

	Year ended December 31, 2008	Year ended December 31, 2007
Wages and salaries	7,463,386	4,266,792
Compulsory social security obligations for 2008	1,643,180	-
Compulsory social security obligations for 2007	1,104,818	-
Employee benefits	122,663	117,260
Total Personnel cost	10,334,047	4,384,052

Also refer– i) note 1 section on Taxation and other Statutory Regulations and ii) note 19 on Contingencies and commitments regarding the social security contributions.

Note 14. Operating Expenses

	Year ended December 31, 2008	Year ended December 31, 2007
Motor vehicle expenses	15,246	13,040
Rent expense	767,169	463,599
Utilities	52,930	40,588
Security	252,550	47,076
Communication expense	363,400	210,864
Bank charges	709,151	498,493
Maintenance & repair	48,002	38,440
Consumables & printing	237,607	235,136
Travel and accommodation expenses	339,413	365,009
Training and hiring	37,951	16,898
Audit	66,736	29,977
Royalty	1,092,792	881,016
Meeting and Conferences	45,136	114,402
Marketing/Advertisement	204,014	120,581
Professional services	86,903	27,504
Other input taxes including VAT	607,878	518,461
Software support	23,465	40,309
Miscellaneous expenses	23,328	4,631
Total Operating expenses	4,973,671	3,666,024

Expenses of Audit, Royalty, and Software support include withholding tax.

FINCA Azerbaijan

Notes to the Financial Statements for the year ended December 31, 2007

(in US Dollars)

Note 15. Equity Contributed

In November 2007, Finca entered into a grant agreement with British Petroleum (Community Investment Program) Azerbaijan for development of the Baku Corridor with the objective of increasing economic opportunity and sustainable, equitable economic growth in the target areas.

The total amount of investment over a period of two years been envisaged by this agreement is \$1,022,636 which would be contributed by – i) \$422,636 by BP in the form of loan capital grant and ii) \$600,000 by the Organization in the form of portfolio increase from own resources. As at 31st December 2008, \$995,860 worth of portfolio was achieved in the target areas (i.e. 97.3% achieved) and as at 31st December 2007, \$105,728 worth of portfolio was achieved in the target areas (i.e. 10.3% achieved).

A direct responsibility has been entrusted on Organization by this agreement to achieve the total investment and hence Finca has transferred these funds to the Organization during 2008 in the form of Contribution by the “sole shareholder” i.e. Finca. This has been shown in the Equity.

Note 16. Related Party Transactions

Loans from FINCA International, Inc. and Finca Capital Fund LLC:

As of December 31, 2008 the Organization had liabilities for long-term loans in the amount of \$ 6,970,150 (as of December 31, 2007: \$ 9,706,717), and for short-term loans as of December 31, 2008: \$6,500,000 (as of December 31, 2007: \$1,900,000). As of 31 December 2008 the Organization had liabilities in respect of interest payable on loans in the amount of \$ 0 (as of December 31, 2007: \$ 100,902). See also Note 6.

Royalty payments to FINCA International, Inc.:

For year ended December 31, 2008 the Organization accrued royalties due to FINCA in the amount of \$ 1,233,027 out of which \$ 149,097 has been capitalized towards MIS implementation project (refer note 5 Intangible assets) and balance \$ 1,083,930 has been charged to Income Statement. As of December 31, 2008 the accounts payable for royalties due to FINCA were \$ 163,741 after payments of \$ 1,439,105.

For year ended December 31, 2007 the Organization accrued royalties due to FINCA in the amount of \$ 740,070. As of December 31, 2007 the accounts payable for royalties due to FINCA was \$ 239,650 and for other reimbursable expenses were \$ 130,169.

Note 17. Lease Obligations

The Organization leases office space throughout the Republic of Azerbaijan, including the Autonomous Republic of Naxichivan to support its operations and project activity. Future minimum lease payments are presented as follows:

	December 31, 2008	December 31, 2007
Less than one year	1,070,578	465,837
Between one year and five years	411,753	592,770
Total	1,482,331	1,058,607

Total office rent expense for The Organization for the year ended December 31, 2008 was \$ 767,169 (2007: \$ 463,599).

FINCA Azerbaijan

Notes to the Financial Statements for the year ended December 31, 2007

(in US Dollars)

Note 18. Financial instruments: Information on financial risks

The Organization has exposure to the following risks from its use of financial instruments:

- Credit risk
- Liquidity risk
- Market risks
- Currency risk
- Operational risks.

This note presents information about the Organization's exposure to each of the above risks, the Organization's objectives, policies and processes for measuring and managing risk, and the Organization's management of capital.

Risk management framework

The Board of Directors has overall responsibility for the establishment and oversight of the Organization's risk management framework. All Board committees have both executive and non-executive members and report regularly to the Board of Directors on their activities.

The Organization's risk management policies are established to identify and analyze the risks faced by the Organization, to set appropriate risk limits and controls, and to monitor risks and adherence to limits. Risk management policies and systems are reviewed regularly to reflect changes in market conditions, products and services offered. The Organization, through its training and management standards and procedures, aims to develop a disciplined and constructive control environment, in which all employees understand their roles and obligations.

The Organization's Audit Committee is responsible for monitoring compliance with the Organization's risk management policies and procedures, and for reviewing the adequacy of the risk management framework in relation to the risks faced by the Organization. The Organization's Audit Committee is assisted in these functions by Internal Audit. Internal Audit undertakes both regular and ad-hoc reviews of risk management controls and procedures, the results of which are reported to the Audit Committee.

Credit risk

Credit risk is the risk of financial loss to the Organization if a customer or counterparty to a financial instrument fails to meet its contractual obligations, and arises principally from the Organization's loans and advances to customers and other banks and investment securities. For risk management reporting purposes, the Organization considers and consolidates all elements of credit risk exposure (such as individual obligor default risk, country and sector risk).

For risk management purposes, credit risk arising on trading securities is managed independently, but reported as a component of market risk exposure.

Management of credit risk

The Board of Directors has delegated responsibility for the management of credit risk to its Credit Committee. A separate Credit department, reporting to the Credit C committee, is responsible for oversight of the Organization's credit risk, including:

- Formulating credit policies in consultation with business units, covering collateral requirements, credit assessment, risk grading and reporting, documentary and legal procedures, and compliance with regulatory and statutory requirements.
- Establishing the authorization structure for the approval and renewal of credit facilities. Authorization limits are allocated to business unit credit Officers. Larger facilities require approval by credit, Head of credit; credit Committee or the Board of Directors as appropriate.
- Reviewing and assessing credit risk. Credit assesses all credit exposures in excess of designated limits, prior to facilities being committed to customers by the business unit concerned. Renewals and reviews of facilities are subject to the same review process.
- Limiting concentrations of exposure to counterparties, geographies and industries (for loans and advances), and by issuer, credit rating band, market liquidity and country (for investment securities).

FINCA Azerbaijan

Notes to the Financial Statements for the year ended December 31, 2007

(in US Dollars)

Note 18. Financial instruments: Information on financial risks (continued)

- Developing and maintaining the Organization's risk grading in order to categorize exposures according to the degree of risk of financial loss faced and to focus management on the attendant risks. The risk grading system is used in determining where impairment provisions may be required against specific credit exposures. The current risk grading framework consists of eight grades reflecting varying degrees of risk of default and the availability of collateral or other credit risk mitigation. The responsibility for setting risk grades lies with the final approving executive / committee as appropriate. Risk grades are subject to regular reviews by Risk.

- Reviewing compliance of business units with agreed exposure limits, including those for selected industries, country risk and product types. Regular reports are provided to Credit on the credit quality of local portfolios and appropriate corrective action is taken.

- Providing advice, guidance and specialist skills to business units to promote best practice throughout the Organization in the management of credit risk.

Each business unit is required to implement the Organization credit policies and procedures, with credit approval authorities delegated from the Credit Committee. Each business unit has a Chief Credit Risk officer who reports on all credit related matters to local management and the Credit Committee. Each business unit is responsible for the quality and performance of its credit portfolio and for monitoring and controlling all credit risks in its portfolios, including those subject to central approval.

Settlement risk

The Organization's activities may give rise to risk at the time of settlement of transactions and trades. Settlement risk is the risk of loss due to the failure of a company to honor its obligations to deliver cash, securities or other assets as contractually agreed.

For certain types of transactions the Organization mitigates this risk by conducting settlements through a settlement / clearing agent to ensure that a trade is settled only when both parties have fulfilled their contractual settlement obligations. Settlement limits form part of the credit approval / limit monitoring process described earlier. Acceptance of settlement risk on free settlement trades requires transaction specific or counterparty specific approvals from Risk.

Liquidity risk

Liquidity risk is the risk that the Organization will encounter in meeting obligations from its financial liabilities.

Management of liquidity risk

The Organization's approach to managing liquidity is to ensure, as far as possible, that it will always have sufficient liquidity to meet its liabilities when due, under both normal and stressed conditions, without incurring unacceptable losses or risking damage to the Organization's reputation.

Treasury receives information from other business units regarding the liquidity profile of their financial assets and liabilities and details of other projected cash flows arising from projected future business. Treasury then maintains a portfolio of short-term liquid assets, largely made up of short-term liquid investment securities as well as loans and advances to customers, to ensure that sufficient liquidity is maintained within the company as a whole.

Cash flow interest rate risk

Cash flow interest rate risk is the risk that the future cash flow of a financial instrument will fluctuate because of changes in market interest rates. Due to specific nature of the micro-financial market the management of the Company believes that the Company does not run a significant interest rate risk and relevant cash flow risk.

The following table presents an analysis of interest rate risk and thus the potential of the Company for gain or loss. Effective interest rates are presented by categories of financial assets and liabilities to determine interest rate exposure and effectiveness of the interest rate policy used by the Company.

FINCA Azerbaijan

Notes to the Financial Statements for the year ended December 31, 2007

(in US Dollars)

Note 18. Financial instruments: Information on financial risks (continued)

	December 31, 2008		December 31, 2007	
	AZN	USD	AZN	USD
Assets:				
Loans to customers	30-36%	30-40%	30-36%	30-36%
Loans to employees	11 %	-	10-11 %	-
Liabilities:				
Due to banks	15%	5% plus Interbank rate	15%	5% plus Interbank rate
Other borrowed funds	-	8-11%	-	8-10%

Interest rate sensitivity risk

The Company manages fair value interest rate risk through periodic estimation of potential losses that could arise from adverse changes in market conditions. The Finance Department conducts monitoring of the Company's current financial performance, estimates the Company's sensitivity to changes in fair value interest rates and its influence on the Company's profitability.

The following table presents a sensitivity analysis of interest rate risk, which has been determined based on "reasonably possible changes in the risk variable". The level of these changes is determined by management and is contained within the risk reports provided to key management personnel.

	December 31, 2008		December 31, 2007	
	Interest rate change		Interest rate change	
	-1%	+1%	-1%	+1%
Liabilities with floating rate:				
Due to banks	30,000	(30,000)	30,000	(30,000)
Other borrowed funds	-	-	14,750	(14,750)
Net impact on profit before tax	30,000	(30,000)	44,750	(44,750)
Liabilities with fixed rate:				
Due to banks	-	-	11,830	(11,830)
Other borrowed funds	544,654	(544,654)	328,786	(328,786)
Net impact on profit before tax	544,654	(544,654)	340,616	(340,616)

FINCA Azerbaijan

Notes to the Financial Statements for the year ended December 31, 2007

(in US Dollars)

Note 18. Financial instruments: Information on financial risks (continued)

The following table summarizes the carrying amount of financial assets and liabilities at 31 December 2008 by remaining contractual undiscounted cash flows maturity, the analysis of interest sensitivity gap and liquidity risk.

	Up to 1 month	1 month to 3 months	3 months to 1 year	1 year to 5 years	December 31, 2008 Total
ASSETS:					
Cash and cash equivalents	3,383,055	-	-	-	3,383,055
Loans to customers	492,465	7,027,919	46,284,749	13,044,460	66,849,593
Loans to employees			238,250	279,283	517,533
Total interest bearing assets	492,465	7,027,919	46,522,999	13,323,743	67,367,126
Receivables	998,537	-	-	-	998,537
TOTAL ASSETS	4,874,057	7,027,919	46,522,999	13,323,743	71,748,719
LIABILITIES:					
Due to banks	-	500,000	500,000	2,000,000	3,000,000
Other borrowed funds	-	1,750,000	12,005,615	39,709,788	53,465,403
Subordinated debt	-	-	-	1,000,000	1,000,000
Total interest bearing liabilities	-	2,250,000	12,505,615	42,709,788	57,465,403
Trade payables	451,030	409,563	-	-	860,593
Other liabilities		197,741	-	-	197,741
TOTAL LIABILITIES	451,030	2,857,304	12,505,615	42,709,788	58,523,737
Liquidity gap	4,423,027	4,170,616	34,017,384	(29,386,045)	
Interest sensitivity gap	492,465	4,777,919	34,017,384	(29,386,045)	
Cumulative interest sensitivity gap	492,465	5,270,384	39,287,768	9,901,723	
Cumulative interest sensitivity gap as a percentage of total assets	1%	7%	55%	14%	

FINCA Azerbaijan
Notes to the Financial Statements for the year ended December 31, 2007
(in US Dollars)

Note 18. Financial instruments: Information on financial risks (continued)

The following table summarizes the carrying amount of financial assets and liabilities at 31 December 2007 by remaining contractual undiscounted cash flows maturity, the analysis of interest sensitivity gap and liquidity risk.

	Up to 1 month	1 month to 3 months	3 months to 1 year	1 year to 5 years	December 31, 2007 Total
ASSETS:					
Cash	3,042,317				3,042,317
Loans to customers	357,164	1,693,088	34,191,437	8,043,422	44,285,111
Loan to employees	17,021	51,967	152,093	384,342	605,423
Total interest bearing assets	374,185	1,745,055	34,343,530	8,427,764	44,890,534
Other assets	608,128				608,128
TOTAL ASSETS	4,024,630	1,745,055	34,343,530	8,427,764	48,540,979
LIABILITIES:					
Due to banks		1,183,012	-	3,000,000	4,183,012
Other borrowed funds	28,563	0	5,432,573	28,892,432	34,353,568
Total interest bearing liabilities	28,563	1,183,012	5,432,573	31,892,432	38,536,580
Trade payables			369,819		369,819
Other liabilities	205,848	252,328	122,697		580,873
TOTAL LIABILITIES	234,411	1,435,340	5,925,089	31,892,432	39,487,272
Liquidity gap	3,790,219	309,715	28,418,441	-23,464,668	
Interest sensitivity gap	345,622	562,043	28,910,957	-23,464,668	
Cumulative interest sensitivity gap	345,622	907,665	29,818,622	6,353,954	
Cumulative interest sensitivity gap as a percentage of financial assets	1%	2%	61%	13%	

FINCA Azerbaijan

Notes to the Financial Statements for the year ended December 31, 2007

(in US Dollars)

Note 18. Financial instruments: Information on financial risks (continued)

Currency risk

Currency risk is defined as the risk that the value of a financial instrument will fluctuate due to changes in foreign exchange rates. The Company is exposed to the effects of fluctuations in the prevailing foreign currency exchange rates on its financial position and cash flows.

The management controls currency risk by management of the open currency position on the estimated basis of AZN revaluation and other macroeconomic indicators, which gives the Company an opportunity to minimize losses from significant currency rates fluctuations toward its national currency.

The Company's financial assets and financial liabilities are analyzed by currency as follows:

	December 31, 2008		Total
	AZN	USD	
Financial assets by currency			
Cash and cash equivalents	664,844	2,718,211	3,383,055
Loans to customers	7,370,718	59,478,876	66,849,593
Loans to employees	517,533	-	517,533
Receivables	110,097	888,440	998,537
Balance at December 31, 2008	8,663,192	63,085,527	71,748,719
Financial liabilities by currency			
Due to banks	-	3,000,000	3,000,000
Other borrowed funds	6,089,638	47,375,765	53,465,403
Subordinated debt	-	1,000,000	1,000,000
Trade payables	-	860,593	860,593
Other liabilities	-	197,741	197,741
Balance at December 31, 2008	6,089,638	52,434,099	58,523,737
NET BALANCE SHEET POSITION	2,573,554	10,651,428	13,224,982

	December 31, 2007		Total
	AZN	USD	
Financial assets by currency:			
Cash and cash equivalents	479,274	2,563,043	3,042,317
Loans to customers	10,985,132	33,299,979	44,285,111
Receivables	605,424	-	605,424
Balance at 31 December, 2007	150,846	457,282	608,128
	12,220,676	36,320,304	48,540,979
Financial liabilities by currency:			
Other borrowed funds	1,183,012	3,000,000	4,183,012
Trade Payable	57,139	34,296,429	34,353,568
Other liabilities	-	369,819	109,411
Balance at 31 December, 2007	11,337	569,536	850,589
Net Balance Sheet Position	1,251,488	38,235,784	39,487,272
	10,969,187	(1,915,480)	

FINCA Azerbaijan

Notes to the Financial Statements for the year ended December 31, 2007

(in US Dollars)

Note 18. Financial instruments: Information on financial risks (continued)

Currency risk sensitivity

For the purpose of these financial statements the functional currency is US dollars. The following table details the sensitivity to a 5% increase and decrease in the USD against the AZN. 5% is the sensitivity rate used when reporting foreign currency risk internally to key management personnel and represents management's assessment of the possible change in foreign currency exchange rates. The sensitivity analysis includes only outstanding foreign currency denominated monetary items and adjusts their translation at the end of the period for a 5% change in foreign currency rates.

	December 31, 2008		December 31, 2007	
	+5%	-5%	+5%	-5%
Net impact on profit before tax	128,678	(128,678)	522,342	(522,342)

Operational risks

Operational risk is the risk of direct or indirect loss arising from a wide variety of causes associated with the Organization's processes, personnel, technology and infrastructure, and from external factors other than credit, market and liquidity risks such as those arising from legal and regulatory requirements and generally accepted standards of corporate behavior. Operational risks arise from all of the Organization's operations.

The Organization's objective is to manage operational risk so as to balance the avoidance of financial losses and damage to the Organization's reputation with overall cost effectiveness and to avoid control procedures that restrict initiative and creativity.

The primary responsibility for the development and implementation of controls to address operational risk is assigned to senior management within each business unit. This responsibility is supported by the development of overall the Organization standards for the management of operational risk in the following areas:

- requirements for appropriate segregation of duties, including the independent authorization of transactions
- Requirements for the reconciliation and monitoring of transactions
- Compliance with regulatory and other legal requirements
- Documentation of controls and procedures
- Requirements for the periodic assessment of operational risks faced, and the adequacy of controls and procedures to address the risks identified
- Requirements for the reporting of operational losses and proposed remedial action
- Development of contingency plans
- Training and professional development
- Ethical and business standards
- risk mitigation, including insurance where this is effective."

Compliance with the Organization standards is supported by a program of periodic reviews undertaken by Internal Audit. The results of Internal Audit reviews are discussed with the management of the business unit to which they relate, with summaries submitted to the Audit Committee and senior management of the Organization.

Limitations of sensitivity analysis

The above tables demonstrate the effect of a change in a key assumption while other assumptions remain unchanged. In reality, there is a correlation between the assumptions and other factors. It should also be noted that these sensitivities are non-linear, and larger or smaller impacts should not be interpolated or extrapolated from these results.

FINCA Azerbaijan
Notes to the Financial Statements for the year ended December 31, 2007
(in US Dollars)

Note 18. Financial instruments: Information on financial risks (continued)

The sensitivity analyses do not take into consideration that the Company's assets and liabilities are actively managed. Additionally, the financial position of the Company may vary at the time that any actual market movement occurs. For example, the Company's financial risk management strategy aims to manage the exposure to market fluctuations. As investment markets move past various trigger levels, management actions could include selling investments, changing investment portfolio allocation and taking other protective action. Consequently, the actual impact of a change in the assumptions may not have any impact on the liabilities, whereas assets are held at market value on the balance sheet. In these circumstances, the different measurement bases for liabilities and assets may lead to volatility in shareholder equity.

Other limitations in the above sensitivity analyses include the use of hypothetical market movements to demonstrate potential risk that only represent the Company's view of possible near-term market changes that cannot be predicted with any certainty.

Note 19. Commitments and Contingencies

Based on an inspection conducted in December, 2008, the Social Protection Fund has challenged the Organization's exemption from social fund contributions for the period from 1 January, 2007 to 31 December, 2008. The Social Protection Fund has issued an "Act" challenging the exemption, and assessing retroactive Social Fund dues from the Organization in the amount of AZN 1,966,826. In addition, the Social Protection Fund has assessed penalties for unremitted contributions in the amount of AZN 983,413 (i.e. 50% of the unremitted amount – the maximum applicable penalty under the law). Management believes that it had a valid basis for the exemption, and that the imposition of this tax is related to the Organization's plans to transform into a corporate entity that would going forward no longer be entitled to claim the exemption. The government has advised the Organization that it would mandate the social fund contributions retroactively upon such a change in corporate form.

The Organization has formally disputed the findings of the audit, and the matter is currently under discussion between the parties. The retroactive social fund contributions have been applied to the profit and loss statement presented above. Pending resolution of discussions as to the transformation, no payment has been made. However, no provision has been made in these financial statements for penalties assessed, as management believes, based on advice of counsel, that the penalty assessments are illegitimate, and that they will not stand legal challenge by the Organization. As per Article 21 of the Law on Social Contributions, penalties can only be applied when salaries and other income to employees has been concealed.

In addition, the government has also taken the position that equity attributable to tax exempted donations be permanently restricted to charitable activities in Azerbaijan, including microfinance. We anticipate that we would in any event continue to use these funds for our microfinance activities. The fact, nature or specific requirements of any such restrictions cannot be determined pending further discussions with the government. The Organization now has approximately 3.5 million USD in equity that is derived from original grant funding. In the view of management, this is the amount most likely to be subject to any such restrictions.

The government, as part of a review of microfinance activities in Azerbaijan, may impose additional requirements for operation or structure of microfinance organizations operating in the country. No determination can be made at this time whether any additional conditions would be imposed or whether, if imposed, the impact if any that such conditions would have on the Organization.

Note 20. Prior period adjustment

As a result of adoption of IFRS, the Company reported an adjustment to the retained earnings for 2007 associated with the accounting error related to the application of IAS 18 "Revenue" and IAS 39 "Financial Instruments" and use of the effective interest method. Management has adjusted its financial statements as summarized in the table below:

	From Financial Statements 2007	Corrected comparative figures 2007	Adjustments
Balance Sheet			
Deferred tax assets	383,216	611,308	(228,092)
Trade and other payables	667,535	1 704,317	(1 036,782)
Retained Earnings	9,412,047	8 603,357	808,690
Income Statement			
Commission fees	2,293,636	1 723,725	569,911
Income tax expense	(337,471)	(212,090)	(125,381)
Profit for the period	2,026,862	1 582,331	444,531