

**NOR HORIZON UCO**  
**UNIVERSAL CREDIT ORGANIZATION LLC**

**FINANCIAL STATEMENTS**

**in Armenian Drams**

**31 DECEMBER 2009**



**BAKER TILLY**  
**ARMENIA**

**YEREVAN 2010**



## BAKER TILLY ARMENIA

22 Hanrapetutyan Street  
0010 Yerevan  
Republic of Armenia  
Tel: +374(10) 582-487  
Tel: +374(10) 582-478  
Fax: +374(10) 562-404  
Email: [info@bakertillyarmenia.com](mailto:info@bakertillyarmenia.com)  
[www.bakertillyarmenia.com](http://www.bakertillyarmenia.com)

26 March, 2010  
N 09110



**CONFIRMED BY:**

**P. GEVORGYAN**

**Managing Partner  
Baker Tilly Armenia CJSC**

License for auditing N054 awarded by Ministry of Finance  
and Economy of the Republic of Armenia

### INDEPENDENT AUDITOR'S REPORT

To Founder of Nor Horizon  
Universal Credit Organization LLC

We have audited the accompanying financial statements of "Nor Horizon" UCO LLC (further in the text - the Organization), which comprise the balance sheet as at December 31, 2009, 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.

#### THE AUDITOR'S OPINION ON THE FINANCIAL STATEMENTS

In our opinion, the financial statements of Nor Horizon UCO Limited Liability Company give a true and fair view of the financial position of the Organization as of 31 December 2009, and of its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards (IFRS).

M. Mkrtychyan  
Auditor





**Comprehensive Income Statement**

For the year ended 31 December 2009

	Notes	Year ended December 31, 2009 (audited)	<u>AMD ths</u> Year ended December 31, 2008 (audited)
Interest and similar income	6	190,771	188,532
Interest and similar expense	6	(49,751)	(48,556)
<b>Net interest income</b>		<b>141,020</b>	<b>139,977</b>
Commissions and similar expenses	7	(3,356)	(1,130)
Net trading income	8	252	(1,000)
Other income	9	9,934	490
Impairment charge for credit losses	10	(8,299)	(1,541)
Staff costs	11	(83,284)	(83,821)
Depreciation of property and equipment	16	(9,424)	(7,891)
Amortization of intangible assets	17	(315)	(316)
Other expenses	12	(73,846)	(41,903)
<b>Profit before taxation</b>		<b>(27,318)</b>	<b>2,864</b>
Profit tax expense	13	(1,404)	(1,338)
<b>Net profit for the year</b>		<b>(28,722)</b>	<b>1,528</b>

Khoren Kerobyan  
Executive Director



Monica Khachatryan  
Chief Accountant



**Statement on Financial Position**

As at 31 December 2009

AMD ths.

	Notes	As of December 31, 2009 (audited )	As of December 31, 2008 (audited )
<b>ASSETS</b>			
Cash and deposits with banks	14	71,890	19,155
Loans and advances provided to customers	15	936,310	780,233
Property, plant and equipment	16	92,426	85,335
Intangible assets	17	2,024	2,339
Deferred tax assets	13	273	485
Other assets	18	2,024	1,958
<b>TOTAL ASSETS</b>		<b>1,104,947</b>	<b>889,505</b>
<b>LIABILITIES AND EQUITY</b>			
<b>Liabilities</b>			
Amounts due to financial and international institutions	19	302,400	139,776
Borrowings	20	434,321	441,692
Current Profit tax liabilities		-	585
Other liabilities	21	2,631	2,606
<b>Total liabilities</b>		<b>739,352</b>	<b>584,659</b>
<b>Equity</b>			
Chartered capital	22	280,000	280,000
Fair value reserve	20	-	10,104
Other items of equity	20	89,471	-
Retained earnings		(3,876)	14,742
<b>Total equity</b>		<b>365,595</b>	<b>304,846</b>
<b>TOTAL LIABILITIES AND EQUITY</b>		<b>1,104,947</b>	<b>889,505</b>

The presented financial statements have been approved by the Organization's Management as at 22.03.10 and signed by the Organization's Executive Director and Chief Accountant. The attached notes 1-28 represent an integral part of these financial statements

Khoren Kerobyan  
Executive Director

Monica Khachatryan  
Chief Accountant





**STATEMENT OF CHANGES IN EQUITY**

For the year ended 31 December 2009

	Share capital	Fair value reserve	Retained earnings	Other items of equity	Total
<b>Items</b>					
Balance as of December 31, 2008	280,000	10,104	14,742	-	304,846
The overall result of accounting policy and adjustments of material misstatements	-	-	-	-	-
<b>Recalculated balance</b>					-
Other increase/(decrease) in equity items	-	-	-	89,471	89,471
Dividends	-	-	-	-	-
Net gain/(loss)	-	-	(28,722)	-	(28,722)
Internal movement	-	(10,104)	10,104	-	-
Balance as of December 31, 2009	280,000	-	(3,876)	89,471	365,595

Kh. Kerobyan  
Executive Director



Monica Khachatryan  
Chief Accountant



**CASH FLOW STATEMENT**

For the year ended 31 December 2009

	2009 (audited)	<i>AMD ths</i> 2008 (audited)
<b>Cash flows from operating activities</b>		
Interest received	156,321	186,281
Interest paid	(45,621)	(38,328)
Commissions and similar amounts paid	-	(1,171)
Realized gains less losses from dealing in foreign currencies	252	(1,000)
Other income received/recovery of the written off loans	84	132
Increase/decrease in the means involved	239,246	114,534
Salaries and benefits paid	(63,272)	(64,378)
Other operating expenses paid	(22,458)	(68,229)
<b>Cash flows from operating activities before changes in operating assets and liabilities</b>	<b>264,552</b>	<b>127,841</b>
<i>Net increase in operating assets</i>		
Loans and advances provided to customers	(163,791)	(153,657)
<b>Net cash flow from operating activities before profit tax</b>	<b>100,761</b>	<b>(25,816)</b>
Profit tax paid	(5,824)	(2,472)
<b>Net cash flow from operating activity</b>	<b>94,937</b>	<b>(28,288)</b>
<b>Cash flows from investing activities</b>		
Purchase of property and equipment	(15,770)	(5,997)
Purchase of intangible assets	-	-
<b>Net cash flow from investing activities</b>	<b>(15,770)</b>	<b>(5,997)</b>
<b>Cash flow from financing activities</b>		
Proceeds from issue of share capital		
Loans received from financial institutions	(30,810)	(30,020)
Borrowings		
<b>Net cash flow from financing activities</b>	<b>(30,810)</b>	<b>(30,020)</b>
<b>Net increase in cash and cash equivalents</b>	<b>48,357</b>	<b>(64,305)</b>
Cash and cash equivalents at the beginning of the year	19,155	80,983
Effect of exchange rate changes on cash and cash equivalents	4,378	2,477
Cash and cash equivalents at the end of the year (Note 14)	<b>71,890</b>	<b>19,155</b>

Kh. Kerobyan  
Executive Director



Monica Khachatryan  
Chief Accountant

## NOTES ATTACHED TO THE FINANCIAL STATEMENTS

### 1. Principal activities

“Nor Horizon” UCO LLC (the “Organization”) is a limited liability company, which was incorporated in the Republic of Armenia on 28.03.06. The Organization is regulated by the legislation of RA and conducts its business under the License 12, awarded as of 28.03.06 by the Central Bank of Armenia (CBA).

The objective of the Organization is to foster economic and social development of Armenian population by providing loans for development of small and medium sized enterprises.

The Organization’s registered office is located in Yerevan, and it has 4 branches and 2 representative offices in Yerevan and Armenian regions.

Organization’s legal address is 54 Komitas str., Yerevan.

### 2. Armenian business environment

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

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

In addition, economic conditions continue to limit the volume of activity in the financial markets.

Market quotations in generally illiquid markets may not be reflective of the fair values for financial instruments, which would be determined in an efficient, active market involving many willing buyers and willing sellers.

### 3. Basis of the reports preparation

#### Statement of compliance

The financial statements of the Organization have been prepared in accordance with the International Financial Reporting Standards (“IFRS”) as approved and published by the International Accounting Standards Board (IASB), and Interpretations issued by the International Financial Reporting Interpretations Committee (“IFRIC”). The comparative information and financial statements include the results of the Organization’s financial performance and cash flow for year ended 31 December 08.

#### 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 for those assets, for which a reliable measure of fair value is not available. Other financial assets and liabilities are stated at their amortized cost, and non-financial assets and liabilities are stated at their historical cost.

#### Functional and presentation currency

The Organization’s functional currency is the currency of the primary economic environment in which the Organization operates. The Organization’s functional and presentation currency is Armenian Drams (“AMD”), since this currency best reflects the economic substance of the Organization’s underlying events and

transactions. 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 the IFRS. The financial statements are presented in thousands of AMD, which is not convertible outside Armenia.

#### **Reclassifications**

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

#### **New standards and interpretations**

- IAS 23 Borrowing Costs (effective January 1, 2009)
- IFRS 8 *Operating Segments* (effective January 1, 2008)

### **4. Summary of significant accounting policies**

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

#### **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 accounted for at fair value and adjusted through profit or loss, are recognised within 'interest income' and 'interest expense' in the income statement using the effective interest rate method.

Once the carrying 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.

##### ***Income and expense from commissions and similar 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.

##### ***Net trading income***

Net trading income includes gains less losses from trading in foreign currencies.

#### **Foreign currency translation**

Transactions in foreign currencies are initially recorded at 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.

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 and losses from trading in foreign currencies in net trading income.

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

	<b>December 31, 2009</b>	<b>December 31, 2008</b>
AMD/ 1 US Dollar	377.89	306.73
AMD/ 1 Euro	542.23	435

### **Taxation**

Profit tax on the profit for the year comprises current and deferred tax. Profit 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 reflected in the financial reports, 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 realized 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.

### **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.

### **Amounts due from banks**

In the normal course of business, the Organization maintains advances or deposits for various periods of time with banks. Deposits to banks with a fixed maturity term are subsequently measured at amortized cost using the effective interest method. Those that do not have fixed maturities are carried at amortized cost based on maturities estimated by management.

### **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's carrying value is measured using the effective interest method. Loans to customers that do not have fixed maturities are accounted for under the effective interest method based on expected maturity. Loans to customers are carried net of any allowance for impairment losses.

#### ***Available-for-sale financial instruments***

Investments available for sale represent debt and equity investments that are intended to be held for an indefinite period of time, which may be sold in response to needs for liquidity or changes in interest rates, exchange rates or equity prices. After initial recognition available-for sale financial assets are measured at fair value with gains or losses being recognised as a separate component of equity until the investment is derecognised or until the investment is determined to be impaired at which time the cumulative gain or loss previously reported in equity is included in the statement of income. However, interest calculated using the

effective interest method is recognised in the statement of income. Dividends on available-for-sale equity instruments are recognised in profit or loss when the Organization's right to receive payment is established.

The fair value of investments that are actively traded in organised financial markets is determined by reference to quoted market bid prices at the close of business on the balance sheet date. For investments where there is no active market, fair value is determined using valuation techniques.

Such techniques include using recent arm's length market transactions, reference to the current market value of another instrument, which is substantially the same, and discounted cash flow analysis. Otherwise the investments are stated at cost less any allowance for impairment.

### **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 an 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.

### **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.

#### **Leases**

##### **Operating - Organization as lessee**

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

#### **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
Computers	3	33
Other fixed assets	5	20

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.

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

**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.

**Borrowings**

Borrowings, which include amounts due to financial institutions and due to founder party 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.

**Contributions to the Social Insurance Fund**

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.

**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.

**Share capital*****Share capital***

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.

**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 judgments

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 judgments 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 judgments 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 23.

## 6. Interest and similar income and expense

	2009	<i>AMD ths.</i> 2008
Loans and advances to customers	190,682	188,515
Debt investment securities available for sale	-	-
Amounts due from banks	89	17
<b>Total interest and similar income</b>	<b>89</b>	<b>188,532</b>
	<b>2009</b>	<b>2008</b>

Amounts due to banks	1,156	7,100
Amounts due to other institutions	30,468	20,815
Borrowing from the related parties	18,127	20,641
<b>Total interest and similar expense</b>	<b>49,751</b>	<b>48,556</b>
<b>7. Commissions and similar expenses</b>		
	<b>2009</b>	<b>2008</b>
Cash operations	3,356	1,130
<b>Total fee and commission expense</b>	<b>3,356</b>	<b>1,130</b>
<b>8. Net trading income</b>		
	<b>2009</b>	<b>2008</b>
Gains less losses from trading in foreign currency	252	(1,000)
<b>Net trading income</b>	<b>252</b>	<b>(1,000)</b>
<b>9. Other income</b>		
	<b>2009</b>	<b><i>AMD, ths</i></b> <b>2008</b>
Fines and penalties received	2,304	278
Other income	7,630	212
<b>Total other income</b>	<b>9,934</b>	<b>490</b>
<b>10. Impairment charge for credit losses</b>		
Loans and advances to customers	8,299	1,541
<b>Total impairment charge for credit losses</b>	<b>8,299</b>	<b>1,541</b>
<b>11. Staff costs</b>		
Wages and salaries	73,392	73,290
Social security contributions	8,897	8,980
Staff tuition expenses	995	1,551
<b>Total staff costs</b>	<b>1077,289</b>	<b>83,821</b>
<b>12. Other expenses</b>		
Fixed assets maintenance	9,403	10,180
Advertising costs	173	385
Business trip expenses	3,983	1,176
Communications	8,628	8,404

Operating lease	5,210	5,460
Taxes, other than profit tax, duties	5,222	5,287
Consulting and other expenses	1,667	7,355
Security	2,801	3,339
Representative expenses	109	188
Office supplies	3,095	2,123
Penalties paid	146	229
Net (gains)/losses from foreign currency translation	28,584	(4,129)
Other expenses	4,825	1,906
<b>Total other expense</b>	<b>501,418</b>	<b>41,903</b>

### 13. Profit tax expense

Current tax expense	1,192	1,438
Deferred tax	212	(100)
<b>Total profit tax expense</b>	<b>213,192</b>	<b>1,338</b>

The corporate profit tax within the Republic of Armenia is levied at the rate of 20% (2008 - 20%).

Differences between IFRS and RA statutory tax regulations give rise to certain temporary differences between the carrying value of certain assets and liabilities for financial reporting purposes and for profit tax purposes. Deferred profit tax is calculated using the principal tax rate of 20%.

Below is provided reconciliation between the tax expenses and accounting profit:

	2009	Effective rate (%)	2008	<u>AMD ths.</u> Effective rate (%)
<b>Profit before tax</b>	(27,318)		2,864	-
Profit tax at the rate of 20 %	(5,464)	20	573	20
Non-deductible expenses	714		763	
Foreign exchange (gains)/ negative	5,717			
Previous period expenses	(506)			
Result of national and international accounting's differences	731			
<b>Total profit tax expense</b>	<b>1,192</b>		<b>1,528</b>	

Deferred tax calculation in respect of temporary differences:

	2008	Recognized in income statement	2009
Accrued expenses and other liabilities	506	(173)	333
Allowances for impairment and provisions for credit losses	-	-	-
<b>Total deferred tax assets</b>	<b>506</b>	<b>(173)</b>	<b>333</b>

Allowances for impairment and provisions for bank accounts	(21)	(39)	(60)
<b>Total deferred tax liability</b>	<b>(21)</b>	<b>(39)</b>	<b>(60)</b>
<b>Net deferred tax asset</b>	<b>485</b>	<b>(212)</b>	<b>273</b>

	2007	Recognized in income statement	2008
Accrued expenses and other liabilities	516	(10)	506
Allowances for impairment and provisions for credit losses	-	-	-
<b>Total deferred tax assets</b>	<b>516</b>	<b>(10)</b>	<b>506</b>
Allowances for impairment and provisions for bank accounts	(131)	110	(21)
<b>Total deferred tax liability</b>	<b>(131)</b>	<b>110</b>	<b>(21)</b>
<b>Net deferred tax asset</b>	<b>385</b>	<b>100</b>	<b>485</b>

14. Cash and amounts due from banks	<u>AMD ths.</u>	
	2009	2008
Cash on hand	42,252	9,598
Bank accounts	29,638	9,557
<b>Total cash and cash equivalents</b>	<b>71,89</b>	<b>19,155</b>

15. Loans and advances to customers	<u>AMD ths.</u>	
	2009	2008
Loans to customers	948,185	788,050
Less allowances for loan impairment	(11,875)	(7,816)
<b>Total loans and advances to customers</b>	<b>936,310</b>	<b>788,050</b>

As of 31 December 2009, the accrued interest income included in loans and advances to customer amounted to AMD 7,985 thousand and future period income amounts AMD 969 thousand.

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

	Privately held companies	Natural persons	Sole properties	<u>AMD ths.</u> 2009 Total
At 1 January 2009	528	6,015	1,273	7,816

Charge for the year	(132)	7,448	983	8,299
Loan offsetting	-	(4,240)	-	(4,240)
As at 31 December 2009	<u>396</u>	<u>9,223</u>	<u>984,273</u>	<u>11,875</u>

Individual impairment				
Collective impairment	396	9,223	2,256	407,479
	<u>396</u>	<u>9,223</u>	<u>2,256</u>	<u>407,479</u>

	Privately held companies	Natural persons	Sole properties	2008 Total
At 1 January 2008	528	6,015	1,273	7,816
Charge for the year	180	1,356	-	1,536
As at 31 December 2008	<u>528</u>	<u>6,015</u>	<u>1,273</u>	<u>7,816</u>
Individual impairment	-	-	-	-
Collective impairment	528	6,015	1,273	7,816
	<u>528</u>	<u>6,015</u>	<u>1,273</u>	<u>7,816</u>

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

	2009	<u>AMD ths.</u> 2008
Privately held companies	39,615	22,313
Natural persons	734,483	590,767
Sole properties	171,310	167,957
Accrued interest	7,985	7,013
Future period income	(969)	-
	<u>(15,607)</u>	<u>788,050</u>
Less allowances for loan impairment	(11,875)	(7,816)
<b>Total loans and advances to customers</b>	<b><u>940,549</u></b>	<b><u>780,233</u></b>

During the reporting period loans amounting AMD 4,239 thousand were written off to off-balance sheet.

Loans to individuals comprise the following products:

	2009	<u>AMD ths.</u> 2008
Mortgage loans	56,224	17,497
Consumer loans	410,390	466,436
Other	267,869	106,834
<b>Total loans and advances to individuals (gross)</b>	<b><u>734,483</u></b>	<b><u>590,767</u></b>

As at 31 December 2009 and 2008, the estimated fair value of loans and advances approximates to their carrying value. Refer to Note 25.

Credit, currency, liquidity and interest rate analysis of loans and advances to customers is presented in Note 27. The information on related party balances is disclosed in Note 24.

## 16. Property, plant and equipment

	<i>AMD ths.</i>					
	Land and buildings	Machinery and equipment	Furniture	Transportation means	Other PPE	Total
<b>COST</b>						
Cost at 01 January, 2008	82,313	6,318	2,813	-	1,750	93,194
Additions	-	2,243	154	3,600	-	5,997
Disposal/(write-off)	-	-	-	-	-	-
At December 31, 2008	82,313	8,561	2,967	3,600	1,750	99,191
Additions	-	773	72	15,670	-	16,515
Disposal/(write-off)	-	(489)	-	-	-	(489)
At December 31, 2009	82,313	8,845	3,039	19,270	1,750	115,217
<b>DEPRECIATION</b>						
At January 01, 2008	3,033	2,376	507	-	49	5,965
Depreciation charge	4,127	2,560	555	321	328	7,891
Disposal/(write-off)	-	-	-	-	-	-
At December 31, 2008	7,160	4,936	1,062	321	377	13,856
Depreciation charge	4,116	2,264	589	2,105	350	9,424
Disposal/(write-off)	-	(489)	-	-	-	(489)
At December 31, 2008	11,276	6,711	1,651	2,426	727	22,791
<b>CARRYING VALUE</b>						
At December 31, 2009	<b>71,037</b>	<b>2,134</b>	<b>1,388</b>	<b>16,844</b>	<b>1,023</b>	<b>92,426</b>
At December 31, 2008	<b>75,153</b>	<b>3,625</b>	<b>1,905</b>	<b>3,279</b>	<b>1,373</b>	<b>85,335</b>

## 17. Intangible assets

	<i>AMD ths.</i>
	Acquired software
<b>COST</b>	
At January 01, 2008	3,150
Additions	-
At December 31, 2008	<b>3,150</b>
<b>At December 31, 2009</b>	<b>3,150</b>
<b>AMORTIZATION</b>	
At January 01, 2008	495
Amortization charge	316

At December 31, 2008	<u>811</u>
Amortization charge	315
At December 31, 2009	<u>1,126</u>
<b>CARRYING VALUE</b>	
At December 31, 2009	<u>2,024</u>
At December 31, 2008	<u>2,339</u>

#### 18. Other assets

	<u>2009</u>	<u><i>AMD ths.</i></u> <u>2008</u>
Prepayments and other debtors	1,716	1,374
Unamortized insurance premium	308	584
<b>Total other assets</b>	<u>309,716</u>	<u>1,958</u>

#### 19. Amounts due to financial and international institutions

	<u>2009</u>	<u>2008</u>
Loans from banks	-	30,999
Loans from international financial institutions	302,400	108,777
<b>Total amounts due to other financial institutions</b>	<u>302,4</u>	<u>139,776</u>

In 2009 "Nor Norizon" UCO LLC signed new loan agreements with non-resident investors like "Oikocredit" and "Kiva", as well as terms of loan agreement signed with Dutch company "Triple Jump" in 2007, were reviewed.

The Organization received a loan from "Oikocredit" in the amount of USD 500.000 at 10.5 % per annum and with 5 years of maturity term. Loan was provided by 2 (two) instalments: first instalment amounting to USD 200.000 was transferred on 24 September 2009, and the second instalment amounting to USD 300.000 – on 15 January, 2010.

Interests accrued as regards this loan are subject to quarterly payments and the principal amount should be paid by 17 equal installments starting from 24 September 2010.

Loan agreement with American company "Kiva" was signed in July 2009, by which the Organization was awarded by 3 stars. It means that the maximum limit of loan amount to be provided to the latter is USD 350.000 free of maturity term and interest rate.

By this program each loan provided by the Organization is collected via "Kiva"'s world network and confirmed on-line, and the difference of loans provided by the Organization to customers during the previous month and the difference of loans paid back by them is transferred to "Nor Horizon"'s bank account on monthly basis. The non-repayment risk as regards these loans bears the investor. First installment as regards "Kiva"'s loans was received on September 28, 2009 and as of 31 December, 2009 the balance in the balance sheet was USD 57,213.82. Taking into account loan agreement's terms and conditions, it is supposed that in case the Organization receives the whole loan amount of USD 350.000 from "Kiva", the Organization can provide new loans under this project only at the extent of customers' repayments, and if latter's amounts exceed amount of loans to be provided, the Organization should pay back to "Kiva" at the extent of that difference. According to the agreement there is no time limit for this process.

It was provided for by the agreement signed with Dutch company Triple Jump in 2007 that the latter would transfer to "Nor Horizon" EUR 150.000 of the agreement amount only when Organization involves another

loan from any socially responsible investor. Oikocredit was such an investor for Triple Jump. To manage the foreign currency risk the Organization agreed to fix at Armenian Drams the loan balance of EUR 100,000 received and the loan amount of EUR 150,000 to be received from Triple Jump by increasing the interest rate from 8% to 14.5%. Transaction was realized on 12 October, 2009 with the help of broker hedging company at exchange rate of Euro 1= AMD 566.17.

The Organization has not had any defaults of principal, interest or other breaches with respect to its liabilities during the period (2008 - nil).

## 20. Borrowings

In borrowings provided by related party are included borrowings from its participant "Horizon" foundation, (a) issued on 03 September 2007 in the amount of AMD 30,000 thousand at 5% per annum and payable AMD 10,000 thousand by the 15 November 2007, the rest by the contractual maturity date on 03 September 2008, and (b) issued on 31 January 2007 in the amount of AMD 250,000 thousand at 8% per annum and payable AMD 100,000 thousand by the 15 November 2009 by four equal semi-annual instalments, and the rest by the contractual maturity date on 31 January 2012.

During 2006 (02 October 2006) the Organization received borrowing amounting to AMD 190,000 thousand at zero interest rate from its participant "Horizon" foundation, contractual maturity date on 02 October 2009. As interest on the borrowing was not at a market rate, the difference of AMD 29,030 thousand between the fair value on inception of the loan calculated as a present value of future cash flows on the loan discounted at current annual market rate of 6% and the amount actually received has been recognized as part of the equity.

During 2008, from the loan of AMD 190,000 provided by the Founder, an amount of AMD 100,000 was directed to payment of the share capital. The difference between fair value of future cash flows on the loan discounted at a market rate and the amount actually received has been recalculated in the equity. According to the loan agreement as of 10 October, 2009 the borrowing was classified as subordinate. During 2009 the amount of fair value provision (AMD 10,104 thousand) was adjusted and equity was paid at the expense of loan balance (AMD 89,471 thousand), as there was an intention to direct the loan balance of 2010 to payment of share capital.

Information on related party balance is disclosed in Note 24.

The Organization has not had any defaults in payment of principal or interest, or other breaches with respect to its liabilities during the period (2008-nil).

## 21. Other liabilities

	<u>AMD ths.</u>	
	2009	2008
Accounts payables	2,319	2,048
Tax payable other than profit tax	312	28
Obligations towards personnel	-	530
<b>Total other liabilities</b>	<b>314,319</b>	<b>2,606</b>

## 22. Chartered Capital

As at 31 December 2008 the Organization's registered and paid-in share capital was AMD 280,000 thousand. In accordance with the Organization's Charter, the share capital consists of 1 share, which has a par value of AMD 280,000 thousand.

The only participant as at 31 December 2008 and 2009 is "Horizon" foundation.

The share capital of the Organization was contributed by the participant in Armenian Drams and they are entitled to dividends and any capital distribution in Armenian Drams.

## 23. Contingent liabilities

### 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 2009, 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 branch facilities.

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

	2009	<u>AMD ths.</u> 2008
Up to 1 year	5,544	5,544
From 1 to 5 years	18,555	18,555
More than 5 years	3,996	3,996
<b>Total operating lease commitments</b>	<b>28,095</b>	<b>28,095</b>

### Insurance

The Organization's premises have been insured for AMD 82,313 thousand. The Organization has not currently obtained insurance coverage related to liabilities arising from errors or omissions. Liability insurance is generally not available in Armenia at present.

## 24. Transactions with related parties

In accordance with IAS 24 Related Party Disclosures, parties are considered to be related if one party has an 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 participant and its ultimate controlling party is "Horizon" foundation.

A number of transactions are entered into with related parties in the normal course of business. These include loans and borrowings. These transactions were carried out on commercial terms and at market rates, except for borrowings, information on which is disclosed below.

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

	2009 Key management personnel	Participants	2008 Key management personnel	Participants
<b>Loans and advances to customers</b>				
Loans outstanding at the beginning of the period, gross	578		-	-
Loans issued during the period	2,450		-	2,350
Loan repayments during the period	(1,725)		-	(2,455)
Loans outstanding at December 31, gross	1,303		-	578
Less allowance for loan impairment	(13)		-	(6)
Loans outstanding at December 31	1,290		-	572
Interest income on loans	56		-	74
<b>Amounts due to founders</b>				
At the beginning of the period	277,656	377,794	-	-
Increase	-	-	-	-
Payment of charter capital	-	(100,000)	-	-
Payment of equity at the expense of subordinate borrowing	(89,471)	-	-	-
Guarantee increase/(decrease)	61	(138)	-	-
Paid during the period	-	-	-	-
At December 31	188,246	277,656	-	-
Commitments and guarantees received	89,432	89,410	-	-
Income statement items				
Interest expense on borrowings	14,280	14,319	-	-

Compensation of key management personnel was comprised of the following:

	2009	<u>AMD ths.</u> 2008
Salaries and other short-term benefits	11,650	11,768
Social security costs	1,016	1,035
<b>Total key management compensation</b>	<b>12,666</b>	<b>12,803</b>

The loans issued to key management personnel during the year of AMD 2,450 thousand are repayable monthly over two years and have interest rates of 5% and 10%.

## 25. 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.

#### Amounts due from and to other financial institutions

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

#### Loans and advances to customers

The 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.

#### Borrowings

The estimated fair value of fixed interest-bearing borrowings not quoted in an active market and zero interest rate borrowings is based on discounted cash flows using interest rates for new debts with similar remaining maturity. The fair value of borrowings, not presented on the Organization's balance sheet at their fair value, does not differ significantly from their carrying values.

### 26. Maturity analysis of assets and liabilities

The table below shows an analysis of assets and liabilities analysed according to when they are expected to be recovered or settled. See Note 27.3 for the Organization's contractual undiscounted repayment obligations.

	<i>AMD ths.</i>					
	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	Total
<b>ASSETS</b>						
Cash and cash equivalents	71,890			71,890	-	71,890
Amounts due from RA Government	1,716			1,716	-	1,716
Loans and advances to customers	62,176	132,797	384,800	579,773	368,412	948,185
Amounts due from legal persons and institutions	-	308	-	308	-	308
	<b>135,782</b>	<b>133,105</b>	<b>384,800</b>	<b>653,687</b>	<b>368,412</b>	<b>1,022,099</b>
<b>LIABILITIES</b>						
Borrowing	21,621	6,149	40,000	67,770	366,551	434,321
Amounts due to financial and international institutions		354	78,849	79,203	223,197	302,400
Amounts due to RA Government	312	-		312	-	312
Other liabilities	653	1,666	-	2,319	-	2,319
	<b>22,586</b>	<b>8,169</b>	<b>118,849</b>	<b>149,604</b>	<b>589,748</b>	<b>739,352</b>
<b>Net position</b>	<b>113,196</b>	<b>124,936</b>	<b>265,951</b>	<b>504,083</b>	<b>(221,336)</b>	<b>282,747</b>
<b>Accumulated gap</b>	<b>113,196</b>	<b>238,132</b>	<b>504,083</b>	<b>-</b>	<b>282,747</b>	

## 27. 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.

Risk management is carried out by Management under policies approved by the Board. The Management identifies, evaluates and hedges financial risks in close co-operation with the Organization's operating units. The Board provides written principles for overall risk management, as well as written policies covering specific areas, such as foreign exchange risk, interest rate risk, credit risk, use of derivative financial instruments and non-derivative financial instruments. In addition, internal audit is responsible for the independent review of risk management and the control environment. The most important types of risk are credit risk, liquidity risk, market risk and other operational risk. Market risk includes currency risk, interest rate and other price risk.

### 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. There is also credit risk in off-balance sheet financial instruments, such as loan commitments.

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

The table below presents the worst case scenario of credit risk exposure to the Organization as at 31 December 2009 and 2008, without taking account of any collateral held or other credit enhancements attached. For on-balance-sheet assets, the exposures set out above are based on net carrying amounts as reported in the balance sheet.

	Notes	Gross maximum exposure as of December 31, 2009	<u>AMD ths.</u> Gross maximum exposure as of December 31, 2008
Cash and cash equivalents	14	71,890	19,155
Loans and advances to customers	15	936,310	780,233
<b>Total credit risk</b>		<b>1008,2</b>	<b>799,388</b>

### 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.

	Financial institutions	Manufact	Agricult.	Trade	Service	Hypothecs	Consumer sector	Other	Total
Cash and cash equivalents	71,890	-	-	-	-	-	-	-	71,890
Loans and advances to customers	-	14,695	252,293	159,826	27,280	56,224	418,718	12,133	941,169
As at 31 December 2009	71,89	14,695	252,293	159,826	27,28	56,224	418,718	12,133	1013,059
As at 31 December 2008	80,983	7,938	57,876	124,034	14,090	22,656	400,116	812	708,505

### 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, and to industries and countries.

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. Similar risks are monitored on a revolving basis and subject to an annual or more frequent review, when considered necessary.

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 principal collateral types for loans and advances are:

- Mortgages over residential property;
- Charges over business assets such as premises, inventory and accounts receivable.

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

	2009	<u>AMD ths.</u> 2008
Loans collateralized by real estate	399,510	315,546
Loans collateralized by guarantees of financial institutions	17,005	90,861
Other collateral	515,387	374,630

Unsecured loans	9,267	-
Accrued interest	7,985	7,013
Future period income	(969)	-
<b>Total loans and advances to customers (gross)</b>	<b>(19,846)</b>	<b>788,050</b>

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

The collective assessment takes account of impairment that is likely to be present in the portfolio even though there is not yet objective evidence of the impairment in an individual assessment.

Impairment losses are estimated by taking into consideration of the following information: historical losses on the portfolio, current economic conditions, the approximate delay between the time a loss is likely to have

been incurred and the time it will be identified as requiring an individually assessed impairment allowance, and expected receipts and recoveries once impaired.

#### *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.

	2009	<u>AMD ths.</u> 2008
Loans and advances to customers		
Privately held companies	1%	1%
Individuals	1%	1%
Sole proprietors	1%	1%

**Past due and impaired loans**

As of 31 December 2009, the Organization has 5 (five) impaired loans, which are accounted in the off-balance.

**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 has no funds received and loans disbursed with floating interest rate. Except for the concentrations within foreign currency, the Organization has no significant concentration of market risk.

**Currency risk**

Currency risk is the risk that the value of a financial instrument will fluctuate due to changes in foreign exchange rates. The Executive Board has set limits on positions by currency. Positions are monitored on a daily basis.

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

	Armenian Drams	Freely convertible currencies	<u>AMD ths.</u> Total
<b>ASSETS</b>			
Cash and cash equivalents	65,535	6,355	71,890
Loans and advances to customers	751,212	197,942	949,154
Total financial assets	816,747	204,297	1021,044
<b>LIABILITIES</b>			
Amounts due to financial and international; borrowing	639,348	97,373	736,721
Total financial liabilities	639,348	97,373	736,721
Net positions as at 31 December 2009	177,399	106,924	284,323
Net positions as at 31 December 2008	318,233	(108,334)	217,920

Freely convertible currencies represent mainly EUR and US dollar amounts.

**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 in addition to its core deposit base, manages assets with liquidity in mind, and monitors future cash flows and liquidity on a daily bases. This incorporates an assessment of expected cash flows and the availability of high grade collateral which could be used to secure additional funding if required.

The 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 2009 based on contractual undiscounted repayment obligations. See note 26 for the expected maturities of these liabilities. Repayments which are subject to notice are treated as if notice were to be given immediately.

					<u>AMD ths.</u> 2009	
		Demand and less than 1 month	From 1 to 3 months	From 3 to 12 months	From 1 to 5 years	Total
<b>FINANCIAL LIABILITIES</b>						
Amounts due to financial and international institutions		-	354	78,849	223,197	656,046
Borrowing		21,621	6,149	40,000	366,551	434,321
Total undiscounted liabilities	financial	21,621	360,149	118,849	589,748	1090,367
					2008	
		Demand and less than 1 month	From 1 to 3 months	From 3 to 12 months	From 1 to 5 years	Total
<b>FINANCIAL LIABILITIES</b>						
Amounts due to other financial institutions		-	13,816	17,183	108,776	139,775
Borrowing		-		26,000	415,692	441,692
Total undiscounted liabilities	financial	-	13,816	43,183	524,468	581,467

The Organization has received significant funds from "Horizon" foundation. 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.

## 28. Capital adequacy

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 participant's 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. No changes were made in the objectives, policies and processes from the previous years.

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

The Central Bank of Armenia has set the minimal required total capital at AMD 150,000 thousand. The Organization has complied with all externally imposed capital requirements through the period.