

AccessBank Closed Joint Stock Company
International Financial Reporting Standards
Financial Statements and Independent Auditor's
Report

31 December 2010

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INDEPENDENT AUDITOR'S REPORT

To the Management Board and Shareholders of the AccessBank Closed Joint Stock Company (CJSC):

We have audited the accompanying financial statements of the AccessBank CJSC (the "Bank") which comprise the statement of financial position as at 31 December 2010 and the related statement of comprehensive income, statement of changes in equity and statement of cash flows for the year then ended and a summary of significant accounting policies and other explanatory notes.

Management's Responsibility

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 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 accompanying financial statements present fairly, in all material respects, the financial position of the Bank as of 31 December 2009, and its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards.

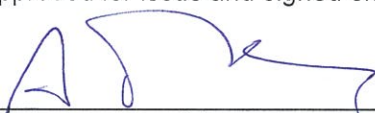
PricewaterhouseCoopers Audit Azerbaijan LLC

Baku, the Republic of Azerbaijan
29 April 2011

AccessBank CJSC
Statement of Financial Position

<i>In thousands of Azerbaijani Manats</i>	Note	31 December 2010	31 December 2009
ASSETS			
Cash and cash equivalents	7	57,805	46,567
Mandatory cash balances with the Central Bank of Azerbaijan Republic ("CBAR")		371	253
Investment securities available for sale		40	40
Due from other banks	8	7,023	9,828
Loans and advances to customers	9	266,185	233,681
Investment properties	10	21,708	-
Property, plant and equipment	11	9,382	7,123
Intangible assets	11	1,615	1,994
Deferred income tax asset	22	51	-
Other financial assets	12	527	289
Other assets	13	1,316	997
TOTAL ASSETS		366,023	300,772
LIABILITIES			
Due to other banks		-	3,005
Customer accounts	14	126,671	64,999
Other borrowed funds	15	153,692	169,120
Current income tax liability	22	130	-
Other financial liabilities	16	2,766	2,107
Other liabilities		129	34
Subordinated debt	17	8,180	8,222
TOTAL LIABILITIES		291,568	247,487
EQUITY			
Share capital	18	41,800	20,000
Retained earnings		32,655	33,285
TOTAL EQUITY		74,455	53,285
TOTAL LIABILITIES AND EQUITY		366,023	300,772

Approved for issue and signed on behalf of the Management Board on 29 April 2011.


 Dr. Andrew Pospelovsky
 Chairman of the Management Board




 Mr. Elshan Hajiyev
 Finance Director, member of the
 Management Board

At 31 December 2010, the prevailing exchange rates were USD 1 = AZN 0.7979 and EUR 1 = AZN 1.056 (31 December 2009: USD 1 = AZN 0.8031 and EUR 1 = AZN 1.1499), refer to Note 3.

AccessBank CJSC
Statement of Comprehensive Income

<i>In thousands of Azerbaijani Manats</i>	Note	2010	2009
Interest income	19	87,703	68,198
Interest expense	19	(25,589)	(18,733)
Net interest income		62,114	49,465
Provision for loan impairment	9	(2,067)	(2,599)
Net interest income after provision for loan impairment		60,047	46,866
Fee and commission income	20	1,129	767
Fee and commission expense	20	(175)	(171)
Gains less losses from foreign currency dealing		749	893
Foreign exchange (loss)/ gain		75	(528)
Other operating income		78	34
Impairment loss on property, plant and equipment		(257)	-
Administrative and other operating expenses	21	(35,397)	(27,879)
Profit before tax		26,249	19,982
Income tax (expense) / credit	22	(79)	4
Profit for the year		26,170	19,986
Other comprehensive income for the year		-	-
Total comprehensive income for the year		26,170	19,986
Earnings per share for profit attributable to the equity holders of the Bank, basic and diluted (expressed in AZN per share)	23	1.31	0.99

AccessBank CJSC
Statement of Changes in Equity

<i>In thousands of Azerbaijani Manats</i>	Share capital	Retained earnings	Total
Balance at 31 December 2008	20,000	13,299	33,299
Total recognised profit for the year attributable to ordinary shareholders	-	19,986	19,986
Balance at 31 December 2009	20,000	33,285	53,285
Increase in share capital	21,800	(21,800)	-
Dividend paid/declared	-	(5,000)	(5,000)
Total recognised profit for the year attributable to ordinary shareholders	-	26,170	26,170
Balance at 31 December 2010	41,800	32,655	74,455

AccessBank CJSC
Statement of Cash Flows

<i>In thousands of Azerbaijani Manats</i>	Note	2010	2009
Cash flows from operating activities			
Interest received		87,573	67,157
Interest paid		(22,207)	(16,741)
Fees and commissions received		1,129	767
Fees and commissions paid		(175)	(171)
Income received from foreign currency dealing		749	893
Other operating income received		78	33
Staff costs paid		(20,761)	(15,494)
Administrative and other operating expenses paid		(11,696)	(10,052)
Income tax paid		-	(1,755)
Cash flows from operating activities before changes in operating assets and liabilities			
		34,690	24,637
Net (increase) / decrease in mandatory cash balances with the CBAR		(118)	742
Net decrease / (increase) in due from other banks		2,658	(9,637)
Net increase in loans and advances to customers		(34,294)	(71,739)
Net increase in other financial assets and other assets		(576)	(126)
Net (decrease) / increase in due to other banks		(3,005)	3,003
Net increase in customer accounts		58,525	41,534
Net increase in other financial liabilities		181	90
Net increase in other liabilities		95	34
Net cash generated from / (used in) operating activities			
		58,156	(11,462)
Cash flows from investing activities			
Proceeds on sale of investment securities available for sale		-	5,945
Acquisition of investment property	10	(21,708)	-
Acquisition of property and equipment		(4,400)	(2,906)
Acquisition of intangible assets		(179)	(1,566)
Net cash (used in) / generated from investing activities			
		(26,287)	1,473
Cash flows from financing activities			
Proceeds from other borrowed funds	15	26,203	52,330
Repayment of other borrowed funds		(41,909)	(11,606)
Dividend paid		(5,000)	-
Net cash (used in) / generated from financing activities			
		(20,706)	40,724
Effect of exchange rate changes on cash and cash equivalents			
		75	(528)
Net increase in cash and cash equivalents			
Cash and cash equivalents at the beginning of the year		46,567	16,360
Cash and cash equivalents at the end of the year			
	7	57,805	46,567

1 Introduction

These financial statements have been prepared in accordance with International Financial Reporting Standards for the year ended 31 December 2010 for AccessBank Closed Joint Stock Company (the "Bank").

The Bank was incorporated in the Republic of Azerbaijan on 5 September 2002 as Closed Joint Stock Company Micro Finance Bank of Azerbaijan. The Bank is regulated by the Central Bank of the Republic of Azerbaijan (the "CBAR") and conducts its business under license number 245. On 6 September 2008 the Bank changed its legal name from CJSC Micro Finance Bank of Azerbaijan to AccessBank CJSC.

Principal activity. The Bank's principal business activity is commercial and retail banking operations within the Republic of Azerbaijan, with a focus on serving agricultural, and micro and small business customers.

The Bank participates in the state deposit insurance scheme, which was introduced by the Azerbaijani Law, "Deposits of individuals insurance in Azerbaijan Republic" dated 29 December 2006. The State Deposit Insurance Fund guarantees full repayment of deposits of individuals in the amount up to AZN 30,000.

The Bank has twenty eight branches within the Republic of Azerbaijan. (31 December 2009: twenty three branches).

Registered address and place of business. The Bank's registered address is:

176 B.Safaroglu Street,
Baku AZ1000,
Republic of Azerbaijan

Presentation currency. These financial statements are presented in thousands of Azerbaijani Manats ("AZN").

2 Operating Environment of the Bank

The Republic of Azerbaijan. The Republic of Azerbaijan displays certain characteristics of an emerging market, including existence of a currency that is not freely convertible in most countries outside the Republic of Azerbaijan, restrictive currency controls and relatively high inflation. The banking sector in the Republic of Azerbaijan is sensitive to adverse fluctuations in confidence and economic conditions. The Azerbaijani economy occasionally experiences falls in investors' confidence in the banking sector accompanied by reductions in liquidity.

The tax, currency and customs legislation within the Republic of Azerbaijan is subject to varying interpretations, and changes, which can occur frequently. Furthermore, the need for further developments in the bankruptcy laws, the absence of formalised procedures for the registration and enforcement of collateral, and other legal and fiscal impediments contribute to the difficulties experienced by banks currently operating in the Republic of Azerbaijan. The future economic direction of the Republic of Azerbaijan is largely dependent upon the effectiveness of economic, financial and monetary measures undertaken by the Government, together with tax, legal, regulatory and political developments.

2 Operating Environment of the Bank (continued)

Impact of the ongoing global financial and economic crisis. The global financial and economic crisis which commenced in the middle of 2007 has resulted in, among other things, at times a lower level of capital market funding and higher interbank lending rates and lower liquidity levels across the Azerbaijani banking sector. At times this has resulted in a significant reduction in the number of new loans and advances made to customers and higher funding costs where it remains possible to obtain debt finance from International Institutions or other local banks. The uncertainties in the global financial market have also led to bank failures and bank rescues in the United States of America, Western Europe and in Russia. Such circumstances could affect the ability of the Bank to obtain new borrowings and re-finance its existing borrowings at terms and conditions similar to those applied to earlier transactions. The borrowers of the Bank may also be affected by the lower liquidity situation which could in turn impact their ability to repay their outstanding loans. Deteriorating operating conditions for borrowers may also have an impact on management's cash flow forecasts and assessment of the impairment of financial and non-financial assets. To the extent that information is available, management has reflected revised estimates of expected future cash flows in their impairment assessments.

Management is unable to reliably estimate the effects on the Bank's financial position of any further deterioration in the liquidity of the financial markets and the increased volatility in the currency and equity markets. Management believes that they are taking all the necessary measures to support the development of the Bank's business in the current circumstances and notes that Bank has strong relations with refinancing partners and has not experience any liquidity difficulties to date.

3 Summary of Significant Accounting Policies

Basis of preparation. These financial statements have been prepared in accordance with International Financial Reporting Standards under the historical cost convention, as modified by initial recognition of financial instruments at fair value and the revaluation of certain financial instruments. The principal accounting policies applied in the preparation of these financial statements are set out below. Management, being the Management Board who approved these financial statements for issue, have the power to amend these financial statements. Any such change requires the approval of the Management Board.

Going concern. Management prepared these financial statements on a going concern basis.

Financial instruments - key measurement terms. Depending on their classification financial instruments are carried at fair value, or amortised cost as described below.

Fair value is the amount for which an asset could be exchanged, or a liability settled, between knowledgeable, willing parties in an arm's length transaction. Fair value is the current bid price for financial assets and current asking price for financial liabilities which are quoted in an active market. For assets and liabilities with offsetting market risks, the Bank may use mid-market prices as a basis for establishing fair values for the offsetting risk positions and apply the bid or asking price to the net open position as appropriate. A financial instrument is regarded as quoted in an active market if quoted prices are readily and regularly available from an exchange or other institution and those prices represent actual and regularly occurring market transactions on an arm's length basis.

Valuation techniques such as discounted cash flow models or models based on recent arms length transactions or consideration of financial data of the investees are used to determine the fair value of certain financial instruments for which external market pricing information is not available. Valuation techniques may require assumptions not supported by observable market data. Disclosures are made in these financial statements if changing any such assumptions to a reasonably possible alternative would result in significantly different profit, income, total assets or total liabilities.

Cost is the amount of cash or cash equivalents paid or the fair value of the other consideration given to acquire an asset at the time of its acquisition and includes transaction costs. Measurement at cost is only applicable to investments in equity instruments that do not have a quoted market price and whose fair value cannot be reliably measured.

3 Summary of Significant Accounting Policies (continued)

Transaction costs are incremental costs that are directly attributable to the acquisition, issue or disposal of a financial instrument. An incremental cost is one that would not have been incurred if the transaction had not taken place. Transaction costs include fees and commissions paid to agents (including employees acting as selling agents), advisors, brokers and dealers, levies by regulatory agencies and securities exchanges and transfer taxes and duties. Transaction costs do not include debt premiums or discounts, financing costs or internal administrative or holding costs.

Amortised cost is the amount at which the financial instrument was recognised at initial recognition less any principal repayments, plus accrued interest, and for financial assets less any write-down for incurred impairment losses. Accrued interest includes amortisation of transaction costs deferred at initial recognition and of any premium or discount to maturity amount using the effective interest method. Accrued interest income and accrued interest expense, including both accrued coupon and amortised discount or premium (including fees deferred at origination, if any), are not presented separately and are included in the carrying values of related balance sheet items.

The effective interest method is a method of allocating interest income or interest expense over the relevant period so as to achieve a constant periodic rate of interest (effective interest rate) on the carrying amount. The effective interest rate is the rate that exactly discounts estimated future cash payments or receipts (excluding future credit losses) through the expected life of the financial instrument or a shorter period, if appropriate, to the net carrying amount of the financial instrument. The effective interest rate discounts cash flows of variable interest instruments to the next interest re-pricing date except for the premium or discount, which reflects the credit spread over the floating rate specified in the instrument, or other variables that are not reset to market rates. Such premiums or discounts are amortised over the whole expected life of the instrument. The present value calculation includes all fees paid or received between parties to the contract that are an integral part of the effective interest rate.

Initial recognition of financial instruments. Trading securities, derivatives and other “financial instruments at fair value through profit or loss” are initially recorded at fair value. All other financial instruments are initially recorded at fair value plus transaction costs. Fair value at initial recognition is best evidenced by the transaction price. A gain or loss on initial recognition is only recorded if there is a difference between fair value and transaction price, which can be evidenced by other observable current market transactions in the same instrument or by a valuation technique whose inputs include only data from observable markets.

All purchases and sales of financial assets that require delivery within the time frame established by regulation or market convention (“regular way” purchases and sales) are recorded at trade date, which is the date that the Bank commits to deliver a financial asset. All other purchases are recognised when the entity becomes a party to the contractual provisions of the instrument.

De-recognition of financial assets. The Bank derecognises financial assets when (a) the assets are redeemed or the rights to cash flows from the assets otherwise expired or (b) the Bank has transferred the rights to the cash flows from the financial assets or entered into a qualifying pass-through arrangement while (i) also transferring substantially all the risks and rewards of ownership of the assets or (ii) neither transferring nor retaining substantially all risks and rewards of ownership but not retaining control. Control is retained if the counterparty does not have the practical ability to sell the asset in its entirety to an unrelated third party without needing to impose restrictions on the sale.

Cash and cash equivalents. Cash and cash equivalents are cash at hand and in bank accounts and items which are readily convertible to known amounts of cash and which are subject to an insignificant risk of changes in value. Cash and cash equivalents include all interbank placements with original maturities of less than three months. Restricted funds are excluded from cash and cash equivalents. Cash and cash equivalents are carried at amortised cost.

Mandatory cash balances with the CBAR. Mandatory cash balances in AZN and foreign currency held with the CBAR are carried at amortised cost and represent non-interest bearing mandatory reserve deposits, which are not available to finance the Bank’s day-to-day operations, and hence are not considered as part of cash and cash equivalents for the purposes of the statement of cash flows.

3 Summary of Significant Accounting Policies (continued)

Due from other banks. Amounts due from other banks are recorded when the Bank advances money to counterparty banks with no intention of trading the resulting unquoted non-derivative receivable due on fixed or determinable dates. Amounts due from other banks are carried at amortised cost.

Loans and advances to customers. Loans and advances to customers are recorded when the Bank advances money to purchase or originate an unquoted non-derivative receivable from a customer due on fixed or determinable dates and has no intention of trading the receivable. Loans and advances to customers are carried at amortised cost.

Impairment of financial assets carried at amortised cost. Impairment losses are recognised in profit or loss when incurred as a result of one or more events (“loss events”) that occurred after the initial recognition of the financial asset and which have an impact on the amount or timing of the estimated future cash flows of the financial asset or group of financial assets that can be reliably estimated. If the Bank determines that no objective evidence exists that impairment was incurred for an individually assessed financial asset, whether significant or not, it includes the asset in a group of financial assets with similar credit risk characteristics and collectively assesses them for impairment. The primary factors that the Bank considers whether a financial asset is impaired is its overdue status and realisability of related collateral, if any.

The following other principal criteria are also used to determine that there is objective evidence that an impairment loss has occurred:

- any instalment is overdue and the late payment cannot be attributed to a delay caused by the settlement systems;
- the borrower experiences a significant financial difficulty as evidenced by borrower’s financial information that the bank obtains;
- the borrower considers bankruptcy or a financial reorganisation;
- there is adverse change in the payment status of the borrower as a result of changes in the national or local economic conditions that impact the borrower; or
- the value of collateral significantly decreases as a result of deteriorating market conditions.

For the purposes of a collective evaluation of impairment, financial assets are grouped based on similar credit risk characteristics. Those characteristics are relevant to the estimation of future cash flows for groups of such assets by being indicative of the debtors’ ability to pay all amounts due according to the contractual terms of the assets being evaluated.

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 and the experience of management in respect of the extent to which amounts will become overdue as a result of past loss events and the success of recovery of overdue amounts. Past experience is adjusted on the basis of current observable data to reflect the effects of current conditions that did not affect past periods and to remove the effects of past conditions that do not exist currently.

If the terms of a financial asset held at amortised cost are renegotiated or otherwise modified because of financial difficulties of the borrower or issuer, impairment is measured using the original effective interest rate before the modification of terms.

Impairment losses are always recognised through an allowance account to write down the asset’s carrying amount to the present value of expected cash flows (which exclude future credit losses that have not been incurred) discounted at the original effective interest rate of the asset. 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 foreclosure is probable.

3 Summary of Significant Accounting Policies (continued)

If, in a subsequent period, the amount of the impairment loss decreases and the decrease can be related objectively to an event occurring after the impairment was recognised (such as an improvement in the debtor's credit rating), the previously recognised impairment loss is reversed by adjusting the allowance account through profit or loss.

Uncollectible assets are written off against the related impairment loss provision after all the necessary procedures to recover the asset have been completed and the amount of the loss has been determined. Subsequent recoveries of amounts previously written off are credited to impairment loss account in profit or loss for the year.

Reposessed collateral. Reposessed collateral represents financial and non-financial assets acquired by the Bank in settlement of overdue loans. The assets are initially recognised at fair value when acquired and included in other non-financial assets or inventories within other assets depending on their nature and the Bank's intention in respect of recovery of these assets and are subsequently remeasured and accounted for in accordance with the accounting policies for these categories of assets.

Where reposessed collateral results in acquiring control over a business, the business combination is accounted for using the purchase method of accounting with fair value of the settled loan representing the cost of acquisition. Accounting policy for associates is applied to reposessed shares where the Bank obtains significant influence but not control. Cost of the associate is the fair value of the loan settled by reposessing the pledged shares.

Credit related commitments. The Bank enters into credit related commitments, including letters of credit and financial guarantees. Financial guarantees represent irrevocable assurances to make payments in the event that a customer cannot meet his/her obligations to third parties and carry the same credit risk as loans. Financial guarantees and commitments to provide a loan are initially recognised at their fair value, which is normally evidenced by the amount of fees received. This amount is amortised on a straight line basis over the life of the commitment, except for commitments to originate loans if it is probable that the Bank will enter into a specific lending arrangement and does not expect to sell the resulting loan shortly after origination; such loan commitment fees are deferred and included in the carrying value of the loan on initial recognition. At the end of each reporting period, the commitments are measured at the higher of (i) the unamortised balance of the amount at initial recognition and (ii) the best estimate of expenditure required to settle the commitment at the end of each reporting period.

Investment securities available for sale. This classification includes investment securities which the Bank intends to hold for an indefinite period of time and which may be sold in response to needs for liquidity or changes in interest rates, exchange rates or equity prices.

Investment securities available for sale are carried at fair value. Interest income on available-for-sale debt securities is calculated using the effective interest method and recognised in profit or loss for the year. Dividends on available-for-sale equity instruments are recognised in profit or loss for the year when the Bank's right to receive payment is established and it is probable that the dividends will be collected. All other elements of changes in the fair value are recognised in other comprehensive income until the investment is derecognised or impaired, at which time the cumulative gain or loss is reclassified from other comprehensive income to profit or loss for the year.

Impairment losses are recognised in profit or loss for the year when incurred as a result of one or more events ("loss events") that occurred after the initial recognition of investment securities available for sale. A significant or prolonged decline in the fair value of an equity security below its cost is an indicator that it is impaired. The cumulative impairment loss – measured as the difference between the acquisition cost and the current fair value, less any impairment loss on that asset previously recognised in profit or loss – is reclassified from other comprehensive income to profit or loss for the year. Impairment losses on equity instruments are not reversed and any subsequent gains are recognised in other comprehensive income. If, in a subsequent period, the fair value of a debt instrument classified as available for sale increases and the increase can be objectively related to an event occurring after the impairment loss was recognised in profit or loss, the impairment loss is reversed through profit or loss for the year.

3 Summary of Significant Accounting Policies (continued)

Investment property. Investment property is property held by the Bank to earn rental income or for capital appreciation, or both and which is not occupied by the Bank. Investment property includes assets under construction for future use as investment property.

Investment property is initially recognised at cost, and subsequently measured by using cost model whereby carrying amount is equal to assets acquired less accumulated depreciation and provision for impairment, where required. If any indication exists that investment properties may be impaired, the Bank estimates the recoverable amount as the higher of value in use and fair value less costs to sell. The carrying amount of an investment property is written down to its recoverable amount through a charge to profit or loss for the year. An impairment loss recognised in prior years is reversed if there has been a subsequent change in the estimates used to determine the asset's recoverable amount.

Earned rental income is recorded in profit or loss for the year within other operating income.

Subsequent expenditure is capitalised only when it is probable that future economic benefits associated with it will flow to the Bank and the cost can be measured reliably. All other repairs and maintenance costs are expensed when incurred. If an investment property becomes owner-occupied, it is reclassified to premises and equipment. Depreciation on items of investment property is calculated using the straight-line method to allocate their cost to their residual values over their estimated useful lives. Estimated useful lives of investment property are 20 years.

Property, Plant and Equipment. Property, plant and equipment are stated at cost less accumulated depreciation and provision for impairment, where required.

Costs of minor repairs and maintenance are expensed when incurred. Cost of replacing major parts or components of property and equipment are capitalised and the replaced part is retired.

At the end of each reporting period management assesses whether there is any indication of impairment of premises and equipment. If any such indication exists, management estimates the recoverable amount, which is determined as the higher of an asset's fair value less costs to sell and its value in use. The carrying amount is reduced to the recoverable amount and the impairment loss is recognised in profit or loss for the year. An impairment loss recognised for an asset in prior years is reversed if there has been a change in the estimates used to determine the asset's value in use or fair value less costs to sell.

Gains and losses on disposals determined by comparing proceeds with carrying amount are recognised in profit or loss for the year (within other operating income or expenses).

Depreciation. Land and construction in progress are not depreciated. Depreciation on items of property and equipment is calculated using the straight-line method to allocate their cost to their residual values over their estimated useful lives as follows:

Computers and communication equipment	4 years
Furniture, fixtures and other	4 to 5 years
Vehicles	4 years
Leasehold improvements	5 years
Own buildings	10 years
Investment properties	20 years

The residual value of an asset is the estimated amount that the Bank would currently obtain from disposal of the asset less the estimated costs of disposal if the asset were already of the age and in the condition expected at the end of its useful life. The assets' residual values and useful lives are reviewed, and adjusted if appropriate, at the end of each reporting period.

3 Summary of Significant Accounting Policies (continued)

Intangible assets. The Bank's intangible assets other than goodwill have definite useful life and primarily include capitalised computer software.

Acquired computer software licences, patents and trademarks are capitalised on the basis of the costs incurred to acquire and bring them to use.

Development costs that are directly associated with identifiable and unique software controlled by the Bank are recorded as intangible assets if the inflow of incremental economic benefits exceeding costs is probable. Capitalised costs include staff costs of the software development team and an appropriate portion of relevant overheads. All other costs associated with computer software, e.g. its maintenance, are expensed when incurred. Capitalised computer software is amortised on a straight-line basis over expected useful life of 5 years.

Acquired computer software licences are capitalised on the basis of the costs incurred to acquire and bring to use the specific software. Development costs that are directly associated with identifiable and unique software controlled by the Bank are recorded as intangible assets if the inflow of incremental economic benefits exceeding costs is probable. Capitalised costs include staff costs of the software development team and an appropriate portion of relevant overhead. All other costs associated with computer software, e.g. its maintenance, are expensed when incurred. Capitalised computer software is amortised on a straight line basis over expected useful life of 4 to 5 years.

Operating leases. Where the Bank is a lessee in a lease which does not transfer substantially all the risks and rewards incidental to ownership from the lessor to the Bank, the total lease payments are charged to profit or loss for the year (rental expense) on a straight-line basis over the period of the lease.

Leases embedded in other agreements are separated if (a) fulfilment of the arrangement is dependent on the use of a specific asset or assets and (b) the arrangement conveys a right to use the asset.

Due to other banks. Amounts due to other banks are recorded when money or other assets are advanced to the Bank by counterparty banks. The non-derivative liability is carried at amortised cost. If the Bank purchases its own debt, it is removed from the statement of financial position and the difference between the carrying amount of the liability and the consideration paid is included in gains or losses arising from retirement of debt.

Customer accounts. Customer accounts are non-derivative liabilities to individuals, state or corporate customers and are carried at amortised cost.

Other borrowed funds. Other borrowed funds include loans from non-resident financial institution with fixed maturity and fixed or floating interest rates. Other borrowed funds are carried at amortised cost.

Shareholder loans are carried at amortised cost. Obligations to return securities borrowed and sold to third parties are carried at fair value through profit or loss.

Subordinated debt. Subordinated debt includes long-term non-derivative liabilities to international financial institutions and is carried at amortised cost. Debt is classified as subordinated debt when its repayment ranks after all other creditors in case of liquidation. Subordinated debt is included in "tier 2 capital" of the Bank, for the capital adequacy calculation purposes.

Income taxes. Income taxes have been provided for in the financial statements in accordance with Azerbaijani legislation enacted or substantively enacted by the end of the reporting period. The income tax charge comprises current tax and deferred tax and is recognised in the statement of comprehensive income, except if it is recognised directly in equity because it relates to transactions that are also recognised, in the same or a different period, directly in equity.

Current tax is the amount expected to be paid to or recovered from the taxation authorities in respect of taxable profits for the current and prior periods. Taxable profits are based on estimates if financial statements are authorised prior to filing relevant tax returns. Taxes, other than on income, are recorded within administrative and operating expenses.

3 Summary of Significant Accounting Policies (continued)

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 end of the reporting period, which are expected to apply to the period when the temporary differences will reverse or the tax loss carry forwards will be utilised. 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 utilised.

On 14 November 2008, a new Law on “Stimulation of Increasing the Capitalization of Banks, Insurance and Reinsurance Companies” (“the Law”) was enacted. According to the Law the profit tax rate for banks, insurance and reinsurance companies is reduced to 0% for three fiscal years starting from 1 January 2009, for the portion of the profit which is transferred to registered share capital. Management of the Bank considered the impact of the enactment of the Law on the Bank’s deferred tax calculation. As the Management is anticipating to transfer current year profit to share capital in the next 3 years period covered by the Law, the Bank will be able to utilise the benefits of this Law. Therefore, as at 31 December 2010, the Bank did not recognise deferred taxes for those temporary taxable and deductible differences which will be reversed between 31 December 2010 and 31 December 2011.

Uncertain tax positions. The Bank’s uncertain tax positions are reassessed by management at the end of each reporting period. Liabilities are recorded for income tax positions that are determined by management as more likely than not to result in additional taxes being levied if the positions were to be challenged by the tax authorities. The assessment is based on the interpretation of tax laws that have been enacted or substantively enacted by the end of the reporting period and any known court or other rulings on such issues. Liabilities for penalties, interest and taxes other than on income are recognised based on management’s best estimate of the expenditure required to settle the obligations at the end of the reporting period.

Trade and other payables. Trade payables are accrued when the counterparty has performed its obligations under the contract and are carried at amortised cost.

Share capital. Ordinary shares and non-redeemable preference shares with discretionary dividends are both classified as equity. Incremental costs directly attributable to the issue of new shares are shown in equity as a deduction, net of tax, from the proceeds. Any excess of the fair value of consideration received over the par value of shares issued is recorded as share premium in equity.

Preference shares which carry a mandatory coupon or are redeemable on a specific date or at the option of the shareholder are classified as financial liabilities and are presented in other borrowed funds. The dividends on these preference shares are recognised as interest expense on an amortised cost basis using the effective interest method.

Dividends. Dividends are recorded in equity in the period in which they are declared. Any dividends declared after the end of the reporting period and before the financial statements are authorised for issue are disclosed in the subsequent events note. The statutory accounting reports of the Bank are the basis for profit distribution and other appropriations.

Income and expense recognition. Interest income and expense are recorded in the statement of comprehensive income for all debt instruments on an accrual basis using the effective interest method. This method defers, as part of interest income or expense, all fees paid or received between the parties to the contract that are an integral part of the effective interest rate, transaction costs and all other premiums or discounts.

3 Summary of Significant Accounting Policies (continued)

Fees integral to the effective interest rate include origination fees received or paid by the entity relating to the creation or acquisition of a financial asset or issuance of a financial liability, for example fees for evaluating creditworthiness, evaluating and recording guarantees or collateral, negotiating the terms of the instrument and for processing transaction documents. Commitment fees received by the Bank to originate loans at market interest rates are integral to the effective interest rate if it is probable that the Bank will enter into a specific lending arrangement and does not expect to sell the resulting loan shortly after origination. The Bank does not designate loan commitments as financial liabilities at fair value through profit or loss.

When loans and other debt instruments become doubtful of collection, they are written down to present value of expected cash inflows and interest income is thereafter recorded for the unwinding of the present value discount based on the asset's effective interest rate which was used to measure the impairment loss.

All other fees, commissions and other income and expense items are generally recorded on an accrual basis by reference to completion of the specific transaction assessed based on the actual service provided as a proportion of the total services to be provided. Loan syndication fees are recognised as income when the syndication has been completed and the Bank retained no part of the loan package for itself or retained a part at the same effective interest rate for the other participants.

Commissions and fees arising from negotiating, or participating in the negotiation of a transaction for a third party, such as the acquisition of loans, shares or other securities or the purchase or sale of businesses, and which are earned on execution of the underlying transaction, are recorded on its completion. Portfolio and other management advisory and service fees are recognised based on the applicable service contracts, usually on a time-proportion basis. Asset management fees related to investment funds are recorded rateably over the period the service is provided. The same principle is applied for wealth management, financial planning and custody services that are continually provided over an extended period of time.

Foreign currency translation. The Bank's functional and presentation currency is the national currency of the Republic of Azerbaijan, Azerbaijani Manats ("AZN").

Monetary assets and liabilities are translated into entity's functional currency at the official exchange rate of the CBAR at the end of the respective reporting period. Foreign exchange gains and losses resulting from the settlement of transactions and from the translation of monetary assets and liabilities into the Bank's functional currency at year-end official exchange rates of the CBAR are recognised in profit or loss. Translation at year-end rates does not apply to non-monetary items.

At 31 December 2010, the principal exchange rates were USD 1 = AZN 0.7979 and EUR 1 = AZN 1.0560 (31 December 2009: USD 1 = AZN 0.8031 and EUR 1 = AZN 1.1499).

Offsetting. Financial assets and liabilities are offset and the net amount reported in the statement of financial position only when there is a legally enforceable right to offset the recognised amounts, and there is an intention to either settle on a net basis, or to realise the asset and settle the liability simultaneously.

Earnings per share. Preference shares are not redeemable and are considered to be participating shares. Earnings per share are determined by dividing the profit or loss attributable to owners of the Bank by the weighted average number of participating shares outstanding during the reporting year.

Staff costs and related contributions. Wages, salaries, contributions to the Republic of Azerbaijan state pension and social insurance funds, paid annual leave and sick leave, bonuses and non-monetary benefits are accrued in the year in which the associated services are rendered by the employees of the Bank.

The Bank has no legal or constructive obligation to make pension or similar benefit payments beyond the payments to the statutory defined contribution scheme.

3 Summary of Significant Accounting Policies (continued)

Segment reporting. Operating segments are reported in a manner consistent with the internal reporting provided to the Bank's chief operating decision maker. Segments whose revenue, result or assets are ten percent or more of all the segments are reported separately.

Changes in presentation. Where necessary, corresponding figures have been adjusted to conform to the presentation of the current year amounts.

The revised IAS 1, Presentation of Financial Statements, which became effective from 1 January 2009 requires an entity to present a statement of financial position as at the beginning of the earliest comparative period ('opening statement of financial position'), when the entity applies an accounting policy retrospectively or makes a retrospective restatement or when it reclassifies items in its financial statements.

The third statement of financial position as of 1 January 2009 is not presented in these financial statements as a result of the below described changes in presentation. Management considered this requirement in the context of applying the revised IAS 1 and in the context of the reclassification presented in this note. Management concluded that it is not essential for the Bank to present the opening statement of financial position as of 1 January 2009 or additional disclosures in the notes in the financial statements since the reclassification does not have a material impact on these financial statements. The omission of those disclosures is therefore, in management's view, not material.

The following table presents changes in classification performed for the reporting purposes:

Balances as per IFRS at 31.12.2009	Changed IFRS figures of 31.12.2009 in 31.12.2010 financial statements	Reason for reclassification
Fee and commission income Settlement transactions – AZN 37 thousand Other – AZN 71 thousand	Fee and commission income Settlement transactions – AZN 25 thousand Commission from plastic cards – AZN 180 thousand Other – AZN 17 thousand	Commission from Plastic card transactions have been removed from "Settlement transactions" and from "Other" and added as a separate line for consistency with current year's figures.
Fee and commission expense Settlement transactions – AZN 38 thousand Plastic cards – AZN 76 thousand Other – AZN 14 thousand	Fee and commission expense Settlement transactions – AZN 35 thousand Plastic cards – AZN 88 thousand Other – AZN 5 thousand	Commission expense has been removed from "Plastic card" subsection to "Settlement transactions" subsection and Commission expense has been removed from "Other" subsection to "Settlement transactions" subsection to achieve a more appropriate presentation.
Statement of Cash Flows 2010	Statement of Cash Flows 2009	Reason for changes
Gross Income received from trading in foreign currencies – AZN 749 thousand (2009: AZN 893 thousand) Effect of exchange rate changes on cash and cash equivalents – AZN 75 thousand (2009: AZN (528) thousand)	Net Effect of exchange rate changes on cash and cash equivalents – AZN 365 thousand	Management decided to change presentation of the gains and losses from foreign currencies and present them separately on the face of the Statement of Cash Flows, including the comparative information. Management concluded that this change in presentation was immaterial, therefore not further disclosures were made in this financial statements regarding this change.

4 Critical Accounting Estimates, and Judgements in Applying Accounting Policies

The Bank makes estimates and assumptions that affect the amounts recognised in the financial statements and the carrying amounts of assets and liabilities within the next financial year. Estimates and judgements are continually evaluated and are based on management's experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances. Management also makes certain judgements, apart from those involving estimations, in the process of applying the accounting policies. Judgements that have the most significant effect on the amounts recognised in the financial statements and estimates that can cause a significant adjustment to the carrying amount of assets and liabilities within the next financial year include:

Impairment losses on loans and advances. The Bank regularly reviews its loan portfolios to assess impairment. In determining whether an impairment loss should be recorded in profit or loss for the year, the Bank makes judgements as to whether there is any observable data indicating that there is a measurable decrease in the estimated future cash flows from a portfolio of loans before the decrease can be identified with an individual loan in that portfolio. This evidence may include observable data indicating that there has been an adverse change in the payment status of borrowers in a group, or national or local economic conditions that correlate with defaults on assets in the group. Management uses estimates based on historical loss experience for assets with credit risk characteristics and objective evidence of impairment similar to those in the portfolio when scheduling its future cash flows. The methodology and assumptions used for estimating both the amount and timing of future cash flows are reviewed regularly to reduce any differences between loss estimates and actual loss experience.

Initial recognition of related party transactions. In the normal course of business the Bank enters into transactions with its related parties. IAS 39 requires initial recognition of financial instruments based on their fair values. 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. Terms and conditions of related party balances are disclosed in Note 30.

Classification of the partially leased out building as "Investment property". Main part of a premise that the Bank possessed as at 31 December 2010 with a carrying value of AZN 21,708 thousands was leased out to third parties. Management considered the relevant clause in IAS 40 requiring that, if the portions of the premise could not be sold separately, the property would be classified as investment property only if an insignificant portion is held for use for administrative purposes. Therefore, this premise was classified as Investment Property as at 31 December 2010.

5 Adoption of New or Revised Standards and Interpretations

Certain new standards and interpretations became effective for the Bank from 1 January 2010:

IFRIC 17, Distributions of Non-Cash Assets to Owners (effective for annual periods beginning on or after 1 July 2009). The interpretation clarifies when and how distribution of non-cash assets as dividends to the owners should be recognised. An entity should measure a liability to distribute non-cash assets as a dividend to its owners at the fair value of the assets to be distributed. A gain or loss on disposal of the distributed non-cash assets should be recognised in profit or loss when the entity settles the dividend payable.

IFRIC 18, Transfers of Assets from Customers (effective for annual periods beginning on or after 1 July 2009). The interpretation clarifies the accounting for transfers of assets from customers, namely, the circumstances in which the definition of an asset is met; the recognition of the asset and the measurement of its cost on initial recognition; the identification of the separately identifiable services (one or more services in exchange for the transferred asset); the recognition of revenue, and the accounting for transfers of cash from customers.

5 Adoption of New or Revised Standards and Interpretations (continued)

IAS 27, Consolidated and Separate Financial Statements (revised January 2008; effective for annual periods beginning on or after 1 July 2009). The revised IAS 27 requires an entity to attribute total comprehensive income to the owners of the parent and to the non-controlling interests (previously “minority interests”) even if this results in the non-controlling interests having a deficit balance (the previous standard required the excess losses to be allocated to the owners of the parent in most cases). The revised standard specifies that changes in a parent’s ownership interest in a subsidiary that do not result in the loss of control must be accounted for as equity transactions. It also specifies how an entity should measure any gain or loss arising on the loss of control of a subsidiary. At the date when control is lost, any investment retained in the former subsidiary has to be measured at its fair value.

IFRS 3, Business Combinations (revised January 2008; effective for business combinations for which the acquisition date is on or after the beginning of the first annual reporting period beginning on or after 1 July 2009). The revised IFRS 3 allows entities to choose to measure non-controlling interests using the previous IFRS 3 method (proportionate share of the acquiree’s identifiable net assets) or at fair value. The revised IFRS 3 is more detailed in providing guidance on the application of the purchase method to business combinations. The requirement to measure at fair value every asset and liability at each step in a step acquisition for the purposes of calculating a portion of goodwill has been removed. Instead, in a business combination achieved in stages, the acquirer has to re-measure its previously held equity interest in the acquiree at its acquisition-date fair value and recognise the resulting gain or loss, if any, in profit or loss for the year. Acquisition-related costs are accounted for separately from the business combination and therefore recognised as expenses rather than included in goodwill. An acquirer has to recognise a liability for any contingent purchase consideration at the acquisition date. Changes in the value of that liability after the acquisition date are recognised in accordance with other applicable IFRSs, as appropriate, rather than by adjusting goodwill. The revised IFRS 3 brings into its scope business combinations involving only mutual entities and business combinations achieved by contract alone.

Group Cash-settled Share-based Payment Transactions - Amendments to IFRS 2, Share-based Payment (effective for annual periods beginning on or after 1 January 2010). The amendments provide a clear basis to determine the classification of share-based payment awards in both consolidated and separate financial statements. The amendments incorporate into the standard the guidance in IFRIC 8 and IFRIC 11, which are withdrawn. The amendments expand on the guidance given in IFRIC 11 to address plans that were previously not considered in the interpretation. The amendments also clarify the defined terms in the Appendix to the standard.

Eligible Hedged Items—Amendment to IAS 39, Financial Instruments: Recognition and Measurement (effective with retrospective application for annual periods beginning on or after 1 July 2009). The amendment clarifies how the principles that determine whether a hedged risk or portion of cash flows is eligible for designation should be applied in particular situations.

IFRS 1, First-time Adoption of International Financial Reporting Standards (following an amendment in December 2008, effective for the first IFRS financial statements for a period beginning on or after 1 July 2009). The revised IFRS 1 retains the substance of its previous version but within a changed structure in order to make it easier for the reader to understand and to better accommodate future changes.

Additional Exemptions for First-time Adopters - Amendments to IFRS 1, First-time Adoption of IFRS (effective for annual periods beginning on or after 1 January 2010). The amendments exempt entities using the full cost method from retrospective application of IFRSs for oil and gas assets and also exempt entities with existing leasing contracts from reassessing the classification of those contracts in accordance with IFRIC 4, 'Determining Whether an Arrangement Contains a Lease' when the application of their national accounting requirements produced the same result.

5 Adoption of New or Revised Standards and Interpretations (continued)

Improvements to International Financial Reporting Standards (issued in April 2009; amendments to IFRS 2, IAS 38, IFRIC 9 and IFRIC 16 are effective for annual periods beginning on or after 1 July 2009; amendments to IFRS 5, IFRS 8, IAS 1, IAS 7, IAS 17, IAS 36 and IAS 39 are effective for annual periods beginning on or after 1 January 2010). The improvements consist of a mixture of substantive changes and clarifications in the following standards and interpretations: clarification that contributions of businesses in common control transactions and formation of joint ventures are not within the scope of IFRS 2; clarification of disclosure requirements set by IFRS 5 and other standards for non-current assets (or disposal groups) classified as held for sale or discontinued operations; requiring to report a measure of total assets and liabilities for each reportable segment under IFRS 8 only if such amounts are regularly provided to the chief operating decision maker; amending IAS 1 to allow classification of certain liabilities settled by entity's own equity instruments as non-current; changing IAS 7 such that only expenditures that result in a recognised asset are eligible for classification as investing activities; allowing classification of certain long-term land leases as finance leases under IAS 17 even without transfer of ownership of the land at the end of the lease; providing additional guidance in IAS 18 for determining whether an entity acts as a principal or an agent; clarification in IAS 36 that a cash generating unit shall not be larger than an operating segment before aggregation; supplementing IAS 38 regarding measurement of fair value of intangible assets acquired in a business combination; amending IAS 39 (i) to include in its scope option contracts that could result in business combinations, (ii) to clarify the period of reclassifying gains or losses on cash flow hedging instruments from equity to profit or loss for the year and (iii) to state that a prepayment option is closely related to the host contract if upon exercise the borrower reimburses economic loss of the lender; amending IFRIC 9 to state that embedded derivatives in contracts acquired in common control transactions and formation of joint ventures are not within its scope; and removing the restriction in IFRIC 16 that hedging instruments may not be held by the foreign operation that itself is being hedged. In addition, the amendments clarifying classification as held for sale under IFRS 5 in case of a loss of control over a subsidiary published as part of the *Annual Improvements to International Financial Reporting Standards*, which were issued in May 2008, are effective for annual periods beginning on or after 1 July 2009.

Unless otherwise stated above, the amendments and interpretations did not have any significant effect on the Bank's consolidated financial statements.

6 New Accounting Pronouncements

Certain new standards and interpretations have been issued that are mandatory for the annual periods beginning on or after 1 January 2011 or later and which the Bank has not adopted early.

Classification of Rights Issues - Amendment to IAS 32 (issued on 8 October 2009; effective for annual periods beginning on or after 1 February 2010). The amendment exempts certain rights issues of shares with proceeds denominated in foreign currencies from classification as financial derivatives.

Amendment to IAS 24, Related Party Disclosures (issued in November 2009 and effective for annual periods beginning on or after 1 January 2011). IAS 24 was revised in 2009 by: (a) simplifying the definition of a related party, clarifying its intended meaning and eliminating inconsistencies; and by (b) providing a partial exemption from the disclosure requirements for government-related entities.

IFRIC 19, Extinguishing Financial Liabilities with Equity Instruments (effective for annual periods beginning on or after 1 July 2010). This IFRIC clarifies the accounting when an entity renegotiates the terms of its debt with the result that the liability is extinguished through the debtor issuing its own equity instruments to the creditor. A gain or loss is recognised in profit or loss based on the fair value of the equity instruments compared to the carrying amount of the debt.

Prepayments of a Minimum Funding Requirement – Amendment to IFRIC 14 (effective for annual periods beginning on or after 1 January 2011). This amendment will have a limited impact as it applies only to companies that are required to make minimum funding contributions to a defined benefit pension plan. It removes an unintended consequence of IFRIC 14 related to voluntary pension prepayments when there is a minimum funding requirement.

6 New Accounting Pronouncements (Continued)

Limited exemption from comparative IFRS 7 disclosures for first-time adopters - Amendment to IFRS 1 (effective for annual periods beginning on or after 1 July 2010). Existing IFRS preparers were granted relief from presenting comparative information for the new disclosures required by the March 2009 amendments to IFRS 7, *Financial Instruments: Disclosures*. This amendment to IFRS 1 provides first-time adopters with the same transition provisions as included in the amendment to IFRS 7.

IFRS 9, Financial Instruments Part 1: Classification and Measurement. IFRS 9 issued in November 2009 replaces those parts of IAS 39 relating to the classification and measurement of financial assets. IFRS 9 was further amended in October 2010 to address the classification and measurement of financial liabilities. Key features of the standard are as follows:

- Financial assets are required to be classified into two measurement categories: those to be measured subsequently at fair value, and those to be measured subsequently at amortised cost. The decision is to be made at initial recognition. The classification depends on the entity's business model for managing its financial instruments and the contractual cash flow characteristics of the instrument.
- An instrument is subsequently measured at amortised cost only if it is a debt instrument and both (i) the objective of the entity's business model is to hold the asset to collect the contractual cash flows, and (ii) the asset's contractual cash flows represent only payments of principal and interest (that is, it has only "basic loan features"). All other debt instruments are to be measured at fair value through profit or loss.
- All equity instruments are to be measured subsequently at fair value. Equity instruments that are held for trading will be measured at fair value through profit or loss. For all other equity investments, an irrevocable election can be made at initial recognition, to recognise unrealised and realised fair value gains and losses through other comprehensive income rather than profit or loss. There is to be no recycling of fair value gains and losses to profit or loss. This election may be made on an instrument-by-instrument basis. Dividends are to be presented in profit or loss, as long as they represent a return on investment.
- Most of the requirements in IAS 39 for classification and measurement of financial liabilities were carried forward unchanged to IFRS 9. The key change is that an entity will be required to present the effects of changes in own credit risk of financial liabilities designated as at fair value through profit or loss in other comprehensive income.

While adoption of IFRS 9 is mandatory from 1 January 2013, earlier adoption is permitted.

Disclosures—Transfers of Financial Assets – Amendments to IFRS 7 (issued in October 2010 and effective for annual periods beginning on or after 1 July 2011.) The amendment requires additional disclosures in respect of risk exposures arising from transferred financial assets. The amendment includes a requirement to disclose by class of asset the nature, carrying amount and a description of the risks and rewards of financial assets that have been transferred to another party yet remain on the entity's statement of financial position. Disclosures are also required to enable a user to understand the amount of any associated liabilities, and the relationship between the financial assets and associated liabilities. Where financial assets have been derecognised but the entity is still exposed to certain risks and rewards associated with the transferred asset, additional disclosure is required to enable the effects of those risks to be understood.

6 New Accounting Pronouncements (Continued)

Improvements to International Financial Reporting Standards (issued in May 2010 and effective from 1 January 2011). The improvements consist of a mixture of substantive changes and clarifications in the following standards and interpretations: IFRS 1 was amended (i) to allow previous GAAP carrying value to be used as deemed cost of an item of property, plant and equipment or an intangible asset if that item was used in operations subject to rate regulation, (ii) to allow an event driven revaluation to be used as deemed cost of property, plant and equipment even if the revaluation occurs during a period covered by the first IFRS financial statements and (iii) to require a first-time adopter to explain changes in accounting policies or in the IFRS 1 exemptions between its first IFRS interim report and its first IFRS financial statements; IFRS 3 was amended (i) to require measurement at fair value (unless another measurement basis is required by other IFRS standards) of non-controlling interests that are not present ownership interest or do not entitle the holder to a proportionate share of net assets in the event of liquidation, (ii) to provide guidance on acquiree's share-based payment arrangements that were not replaced or were voluntarily replaced as a result of a business combination and (iii) to clarify that the contingent considerations from business combinations that occurred before the effective date of revised IFRS 3 (issued in January 2008) will be accounted for in accordance with the guidance in the previous version of IFRS 3; IFRS 7 was amended to clarify certain disclosure requirements, in particular (i) by adding an explicit emphasis on the interaction between qualitative and quantitative disclosures about the nature and extent of financial risks, (ii) by removing the requirement to disclose carrying amount of renegotiated financial assets that would otherwise be past due or impaired, (iii) by replacing the requirement to disclose fair value of collateral by a more general requirement to disclose its financial effect, and (iv) by clarifying that an entity should disclose the amount of foreclosed collateral held at the reporting date and not the amount obtained during the reporting period; IAS 27 was amended by clarifying the transition rules for amendments to IAS 21, 28 and 31 made by the revised IAS 27 (as amended in January 2008); IAS 34 was amended to add additional examples of significant events and transactions requiring disclosure in a condensed interim financial report, including transfers between the levels of fair value hierarchy, changes in classification of financial assets or changes in business or economic environment that affect the fair values of the entity's financial instruments; and IFRIC 13 was amended to clarify measurement of fair value of award credits. The Bank does not expect the amendments to have any material effect on its financial statements, except the amendment to IAS 1 which was early adopted by the Bank as explained in Note 5.

Unless otherwise described above, the new standards and interpretations are not expected to significantly affect the Bank's financial statements.

7 Cash and Cash Equivalents

<i>In thousands of Azerbaijani Manats</i>	31 December 2010	31 December 2009
Cash balances with the CBAR (other than mandatory reserve deposits)	28,001	11,239
Cash on hand	20,935	12,081
Correspondent accounts and overnight placements with other banks:		
- Republic of Azerbaijan	3,540	17,332
- Other countries	5,329	5,915
Total cash and cash equivalents	57,805	46,567

7 Cash and Cash Equivalents (continued)

The credit quality of cash and cash equivalents balances may be summarised as follows at 31 December 2010:

	Cash balances with the CBAR	Correspondent accounts and overnight placements	Total
<i>In thousands of Azerbaijani Manats</i>			
<i>Neither past due nor impaired</i>			
- Government of the Republic of Azerbaijan	28,001	-	28,001
- Rated Azerbaijani banks:			
Moody's/B2 with a stable outlook	-	143	143
Fitch/B with a stable outlook	-	12	12
Moody's/Ba2 with a negative outlook	-	1	1
Fitch/B with a negative outlook	-	11	11
- Other unrated Azerbaijani banks	-	3,373	3,373
- OECD banks	-	4,999	4,999
- Non-OECD banks	-	330	330
Total cash and cash equivalents, excluding cash on hand	28,001	8,869	36,870

The most recently published international ratings for the Republic of Azerbaijan are BBB-/Stable (Fitch Ratings-issued on 20 May 2010), Ba1/Positive (Moody's investors' Service-issued on 8 March 2011) and BB+/Positive (Standard Poor's-issued on 21 December 2010).

Interest rate analysis of cash and cash equivalents is disclosed in Note 25. Information on related party balances is disclosed in Note 30.

The credit quality of cash and cash equivalents balances may be summarised as follows at 31 December 2009:

	Cash balances with the CBAR	Correspondent accounts and overnight placements	Total
<i>In thousands of Azerbaijani Manats</i>			
<i>Neither past due nor impaired</i>			
- Government of the Republic of Azerbaijan	11,239	-	11,239
- Rated Azerbaijani banks:			
Moody's/B2 with a stable outlook	-	4,716	4,716
Fitch/B with a stable outlook	-	72	72
Moody's/Ba2 with a negative outlook	-	37	37
Fitch/B with a negative outlook	-	26	26
Moody's/B2 with a stable outlook	-	1	1
- Other unrated Azerbaijani banks	-	12,480	12,480
- OECD banks	-	5,478	5,478
- Non-OECD banks	-	437	437
Total cash and cash equivalents, excluding cash on hand	11,239	23,247	34,486

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8 Due from Other Banks

<i>In thousands of Azerbaijani Manats</i>	31 December 2010	31 December 2009
Short-term placements with other banks	7,023	9,828
Total due from other banks	7,023	9,828

On 12 November 2010 the Bank signed a deposit agreement with a rated local bank in the amount of AZN 3,000 thousand with maturity date of 12 May 2011. The deposit bears market interest rate. The outstanding amount of this deposit as of 31 December 2010 is AZN 3,023 thousand.

On 23 December 2010 the Bank signed a deposit agreement with a rated local bank in the amount of AZN 4,000 thousand with maturity date of 01 July 2011. The deposit bears market interest rate. The outstanding amount of this deposit as of 31 December 2010 is AZN 4,000 thousand.

An analysis by credit quality of amounts due from other banks outstanding at 31 December 2010 is as follows:

<i>In thousands of Azerbaijani Manats</i>	Short-term placements with other banks
<i>Neither past due nor impaired</i>	
- Rated Azerbaijani banks:	
Fitch/B- with a stable outlook	7,023
Total due from other banks	7,023

Management of the Bank did not determine any objective evidence of impairment of the balances due from other banks and therefore, no provision for impairment was recorded at 31 December 2010 or 31 December 2009.

Amounts due from other banks are not collateralised. An analysis by credit quality of amounts due from other banks outstanding at 31 December 2009 is as follows:

<i>In thousands of Azerbaijani Manats</i>	Short-term placements with other banks
<i>Neither past due nor impaired</i>	
- Rated Azerbaijani banks:	
Fitch/B- with a negative outlook	4,088
Fitch/B+ with a stable outlook	1,635
Fitch/B- with a stable outlook	20
Other unrated Azerbaijani banks	4,085
Total due from other banks	9,828

Interest rate analysis of due from other banks is disclosed in Note 25. Refer to Note 28 for the estimated fair value of each class of amounts due from other banks. Information on related party balances is disclosed in Note 30.

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9 Loans and Advances to Customers

<i>In thousands of Azerbaijani Manats</i>	31 December 2010	31 December 2009
Micro loans (up to AZN 16,000)	142,718	125,182
Small and medium enterprises loans ("SME loans" – over AZN 16,000)	108,477	98,426
Retail loans to salaried individuals	17,275	11,651
Staff loans	5,350	5,016
Less: Provision for loan impairment	(7,635)	(6,594)
Total loans and advances to customers	266,185	233,681

The movements in the provision for loan impairment during 2010 are as follows:

<i>In thousands of Azerbaijani Manats</i>	Micro loans	SME loans	Retail loans to salaried individuals	Staff loans	Total
Provision for loan impairment at 1 January 2010	2,918	3,250	330	96	6,594
Provision for impairment during the year	1,318	590	147	12	2,067
Amounts written-off during the year as uncollectible	(280)	(1,048)	(47)	-	(1,375)
Recovery of previously written-off loans	21	323	5	-	349
Provision for loan impairment at 31 December 2010	3,977	3,115	435	108	7,635

The movements in the provision for loan impairment during 2009 are as follows:

<i>In thousands of Azerbaijani Manats</i>	Micro loans	SME loans	Retail loans to salaried individuals	Staff loans	Total
Provision for loan impairment at 1 January 2009	1,713	1,966	352	85	4,116
Provision for impairment during the year	1,250	1,284	54	11	2,599
Amounts written-off during the year as uncollectible	(68)	-	(76)	-	(144)
Recovery of previously written-off loans	23	-	-	-	23
Provision for loan impairment at 31 December 2009	2,918	3,250	330	96	6,594

Economic sector risk concentrations within the customer loan portfolio are as follows:

<i>In thousands of Azerbaijani Manats</i>	31 December 2010		31 December 2009	
	Amount	%	Amount	%
Trade	146,339	53.4	132,936	55.3
Service	44,054	16.1	35,288	14.7
Agriculture	37,124	13.6	27,411	11.4
Household	22,707	8.3	16,659	6.9
Manufacturing	16,882	6.2	18,692	7.8
Transportation	6,714	2.4	9,289	3.9
Total loans and advances to customers (before impairment)	273,820	100	240,275	100.0

9 Loans and Advances to Customers (continued)

At 31 December 2010, the Bank had 14 borrowers (31 December 2009: 11 borrowers) with aggregated loan amounts above AZN 500 thousand. The total aggregate amount of these loans was AZN 10,672 thousand (31 December 2009: AZN 8,631 thousand) or 3.9% (31 December 2009: 3.6%) of the gross loan portfolio. The Bank is concentrated in agricultural, and micro and small business lending. The largest loan exposure to a single customer as at 31 December 2010 was the outstanding amount of loan to a local company in the amount of AZN 1,099 thousand (31 December 2009: AZN 1,526 thousand).

Information about collateral at 31 December 2010 is as follows:

	Micro loans	SME loans	Retail loans to salaried individuals	Staff loans	Total
<i>In thousands of Azerbaijani Manats</i>					
Unsecured loans	-	-	-	707	707
Loans collateralised by:					
- real estate	10,856	92,372	68	4,564	107,860
- vehicle	1,492	690	723	10	2,915
- inventory and equipment	130,303	14,637	7,190	10	152,140
- other assets	67	778	9,294	59	10,198
Total loans and advances to customers	142,718	108,477	17,275	5,350	273,820

Information about collateral at 31 December 2009 is as follows:

	Micro loans	SME Loans	Retail loans to salaried individuals	Staff loans	Total
<i>In thousands of Azerbaijani Manats</i>					
Unsecured loans	-	-	-	543	543
Loans collateralised by:					
- real estate	7,920	81,864	49	4,459	94,292
- vehicle	1,815	466	720	14	3,015
- inventory and equipment	115,414	14,405	10,632	-	140,451
- other assets	33	1,691	250	-	1,974
Total loans and advances to customers	125,182	98,426	11,651	5,016	240,275

Other assets pledged as collateral mainly include furniture, fixture and gold. The disclosure above represents the carrying value of the loan based on the assets taken as collateral.

9 Loans and Advances to Customers (continued)

An analysis by credit quality of loans outstanding at 31 December 2010 is as follows:

	Micro loans	SME loans	Retail loans to salaried individuals	Staff loans	Total
<i>In thousands of Azerbaijani Manats</i>					
Total current and not impaired	140,414	106,506	17,160	5,344	269,424
<i>Past due but not impaired</i>					
- less than 7 days overdue and/or restructured loans	571	806	8	-	1,385
Total past due but not impaired	571	806	8	-	1,385
<i>Loans individually determined to be impaired (gross)</i>					
- 8 to 30 days overdue and/or restructured loans	582	157	52	-	791
- 30 to 90 days overdue and/or restructured loans	194	195	15	-	404
- over 90 days overdue and/or restructured loans	957	813	40	6	1,816
Total individually impaired loans (gross)	1,733	1,165	107	6	3,011
Gross carrying value of loans	142,718	108,477	17,275	5,350	273,820
Less impairment provisions	(3,977)	(3,115)	(435)	(108)	(7,635)
Total loans and advances to customers	138,741	105,362	16,840	5,242	266,185

9 Loans and Advances to Customers (continued)

An analysis by credit quality of loans outstanding at 31 December 2009 is as follows:

<i>In thousands of Azerbaijani Manats</i>	Micro loans	SME loans	Retail loans to salaried individuals	Staff loans	Total
Total current and not impaired	124,377	96,122	11,510	5,016	237,025
<i>Past due but not impaired</i>					
- less than 7 days overdue and/or restructured loans	173	793	13	-	979
Total past due but not impaired	173	793	13	-	979
<i>Loans individually determined to be impaired (gross)</i>					
- 8 to 30 days overdue and/or restructured loans	178	121	89	-	388
- 30 to 90 days overdue and/or restructured loans	98	33	8	-	139
- over 90 days overdue and/or restructured loans	356	1,357	31	-	1,744
Total individually impaired loans (gross)	632	1,511	128	-	2,271
Gross carrying value of loans	125,182	98,426	11,651	5,016	240,275
Less impairment provisions	(2,918)	(3,250)	(330)	(96)	(6,594)
Total loans and advances to customers	122,264	95,176	11,321	4,920	233,681

Past due but not impaired loans primarily include collateralised loans where the fair value of collateral covers the overdue interest and principal repayments. The amount reported as past due but not impaired is the whole balance of such loans, not only the individual instalments that are past due.

The Bank applied the portfolio provisioning methodology prescribed by IAS 39, Financial Instruments: Recognition and Measurement, and created portfolio provisions for impairment losses that were incurred but have not been specifically identified with any individual loan by the end of the reporting period. The Bank's policy is to classify each loan as 'current and not impaired' until a specific objective evidence of impairment of the loan is identified. The impairment provisions may exceed the total gross amount of individually impaired loans as a result of this policy and the portfolio impairment methodology.

The primary factors that the Bank considers in determining whether a loan is impaired are its overdue status and realisability of related collateral, if any. As a result, the Bank presents above an ageing analysis of loans that are individually determined to be impaired.

9 Loans and Advances to Customers (continued)

The fair value of collateral in respect of loans past due but not impaired and in respect of loans individually determined to be impaired at 31 December 2010 was as follows:

	Micro loans	SME loans	Retail loans to salaried individuals	Total
<i>In thousands of Azerbaijani Manats</i>				
<i>Fair value of collateral - loan past due but not impaired</i>				
- real estate	116	2,897	-	3,013
- vehicle	-	-	-	-
- inventory and equipment	733	799	3	1,535
<i>Fair value of collateral - individually impaired loans</i>				
- real estate	621	3,853	-	4,474
- vehicle	47	62	19	128
- inventory and equipment	5,295	319	198	5,812
Total	6,812	7,930	220	14,962

The fair value of collateral in respect of loans past due but not impaired and in respect of loans individually determined to be impaired at 31 December 2009 was as follows:

	Micro loans	SME loans	Retail loans to salaried individuals	Total
<i>In thousands of Azerbaijani Manats</i>				
<i>Fair value of collateral - loan past due but not impaired</i>				
- real estate	37	1,845	-	1,882
- vehicle	19	-	-	19
- inventory and equipment	582	748	27	1,357
<i>Fair value of collateral - individually impaired loans</i>				
- real estate	84	3,215	-	3,299
- vehicle	103	62	-	165
- inventory and equipment	1,800	733	280	2,813
Total	2,625	6,603	307	9,535

Refer to Note 28 for the estimated fair value of each class of loans and advances to customers. Interest rate analysis of loans and advances to customers is disclosed in Note 25, Information on related party balances is disclosed in Note 30.

10 Investment Properties

<i>In thousands of Azerbaijani Manats</i>	2010	2009
Investment properties at cost at the beginning of the year	-	-
Investment properties acquired during the year	21,708	-
Investment properties at cost at the end of the year	21,708	-

As at 31 December 2010, the carrying value of investment property approximated its fair value.

The Bank purchased this premises on 5 November 2010. The Bank intends to use this premises in the future for its own needs as head office. Starting from 1 December 2010 the Bank took over the right to lease out 5,058 square metres of this premises.

The rental income on investment property in 2010 amounted to AZN 68 thousand and is included in other operating income.

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11 Property, Equipment and Intangible Assets

<i>In thousands of Azerbaijani Manats</i>	Computer	Furniture and office equipment	Motor vehicles	Premises and leasehold improvement	Total property and equipment	Computer software licences	Total
Cost at 1 January 2009	1,088	2,326	238	4,136	7,788	1,059	8,847
Accumulated depreciation / amortisation	(500)	(1,020)	(103)	(1,038)	(2,661)	(82)	(2,743)
Carrying amount at 1 January 2009	588	1,306	135	3,098	5,127	977	6,104
Additions	353	1,588	93	1,339	3,373	1,489	4,862
Disposals	-	(136)	(9)	(637)	(782)	-	(782)
Accumulated depreciation / amortisation of disposals	-	50	9	637	696	-	696
Depreciation / amortisation charge	(255)	(612)	(65)	(359)	(1,291)	(472)	(1,763)
Carrying amount at 31 December 2009	686	2,196	163	4,078	7,123	1,994	9,117
Cost at 31 December 2009	1,441	3,778	322	4,838	10,379	2,548	12,927
Accumulated depreciation / amortisation	(755)	(1,582)	(159)	(760)	(3,256)	(554)	(3,810)
Carrying amount at 31 December 2009	686	2,196	163	4,078	7,123	1,994	9,117
Additions	626	1,068	183	2,252	4,129	221	4,350
Disposals	(61)	(55)	-	-	(116)	(1)	(117)
Transfers	33	9	-	-	42	(42)	-
Accumulated depreciation / amortisation of disposals	54	34	-	-	88	1	89
Depreciation / amortisation charge	(369)	(898)	(97)	(520)	(1,884)	(558)	(2,442)
Carrying amount at 31 December 2010	969	2,354	249	5,810	9,382	1,615	10,997
Cost at 31 December 2010	2,039	4,800	505	7,090	14,434	2,726	17,160
Accumulated depreciation / amortisation	(1,070)	(2,446)	(256)	(1,280)	(5,052)	(1,111)	(6,163)
Carrying amount at 31 December 2010	969	2,354	249	5,810	9,382	1,615	10,997

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Notes to the Financial Statements – 31 December 2010

12 Other Financial Assets

<i>In thousands of Azerbaijani Manats</i>	31 December 2010	31 December 2009
Settlements with money transfer systems	126	180
Settlements with plastic cards	83	69
Other	318	40
Total other financial assets	527	289

Analysis by credit quality of other financial assets outstanding at 31 December 2010 is as follows:

<i>In thousands of Azerbaijani Manats</i>	Settlements with money transfer systems	Settlements with plastic cards	Other	Total
<i>Neither past due nor impaired</i> - Collected or settled after the end of the reporting period	126	83	318	527
Total neither past due nor impaired	126	83	318	527

Analysis by credit quality of other financial assets outstanding at 31 December 2009 was as follows:

<i>In thousands of Azerbaijani Manats</i>	Settlements with money transfer systems	Settlements with plastic cards	Other	Total
<i>Neither past due nor impaired</i> - Collected or settled after the end of the reporting period	180	69	40	289
Total neither past due nor impaired	180	69	40	289

The primary factors that the Bank considers in determining whether the other financial asset is impaired are its overdue status and realisation ability of related collateral, if any. As a result, the Bank presents above an ageing analysis of other financial assets that are individually determined to be impaired. Neither past due nor impaired, but renegotiated balances represent the carrying amount of other financial asset that would otherwise be past due or impaired whose terms have been renegotiated.

Refer to Note 28 for the disclosure of the fair value of each class of other financial assets. Information on related party balances is disclosed in Note 30.

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13 Other Assets

<i>In thousands of Azerbaijani Manats</i>	31 December 2010	31 December 2009
Advances for purchase of intangible assets and equipment	496	732
Prepaid expenses	356	265
Prepayments for operating lease agreement	102	-
Other	362	-
Total other assets	1,316	997
Current	718	265
Non-current	598	732

14 Customer Accounts

<i>In thousands of Azerbaijani Manats</i>	31 December 2010	31 December 2009
Public organisations		
- Term deposits	6,173	3,003
Other legal entities		
- Current/settlement accounts	5,027	2,651
- Term deposits	26,228	10,575
Individuals		
- Current/demand accounts	10,649	6,265
- Term deposits	78,594	42,505
Total customer accounts	126,671	64,999

Economic sector concentrations within customer accounts are as follows:

<i>In thousands of Azerbaijani Manats</i>	31 December 2010		31 December 2009	
	Amount	%	Amount	%
Individuals	89,243	70.5	48,770	75.0
Insurance and other financial services	28,217	22.3	10,610	16.3
Public organisations	6,173	4.8	3,003	4.6
Trade, services, manufacturing	3,038	2.4	2,616	4.1
Total customer accounts	126,671	100	64,999	100

At 31 December 2010, the Bank had 97 active customers (31 December 2009: 51 customers) with balances above AZN 150 thousand. The aggregate balance of these customers was AZN 59,737 thousand (31 December 2009: AZN 32,709 thousand) or 47% (31 December 2009: 50%) of total customer accounts.

Refer to Note 28 for the disclosure of the fair value of each class of customer accounts. Interest rate analysis of customer accounts is disclosed in Note 25. Information on related party balances is disclosed in Note 30.

15 Other Borrowed Funds

<i>In thousands of Azerbaijani Manats</i>	31 December 2010	31 December 2009
European Bank for Reconstruction and Development	20,698	22,317
Developing World Markets Securitizations S.A. - MFBA BOND 1	20,568	20,606
Kreditanstalt für Wiederaufbau	18,291	19,335
International Finance Corporation	12,263	13,847
Pettelaar Effectenbewaarbedrijf N.V	10,078	11,573
Blue Orchard Loan for Development	9,636	9,697
Triodos Custody B.V (custodian of Triodos Fair Share Fund)	8,341	9,993
Global Microfinance Facility	8,112	8,165
Microfinance Enhancement Facility – Cyrano	6,018	-
Bank im Bistum Essen	5,697	5,720
OPEC Fund for International Development	5,310	2,235
MINLAM Microfinance Offshore Master Fund LP	4,124	4,110
Swiss Investment Fund for Emerging markets	3,663	4,914
Impulse Microfinance Investment Fund	3,645	4,068
Dexia Micro Credit Fund	2,876	6,608
Microfinance Loan Obligations S.A. - Compartment Local	2,450	2,467
Developing World Markets SCA – SICAV SIF	2,404	-
VDK Spaarbank N.V.	2,389	4,836
Black Sea Trade and Development Bank	1,789	2,521
Developing World Markets Securitizations S.A – SNS Microfinance Fund	1,604	1,611
Dual Return Find S.I.C.A.V.	1,251	1,259
OikoCredit Ecumenical Development Cooperative Society U.A.	882	1,812
Finethic Microfinance Fund	798	841
Asian Development Bank	517	1,305
Vantage Mutual Fund	288	274
Global Commercial Microfinance Consortium, LTD	-	3,207
Triple Jump B.V.	-	2,486
ReponsAbility S.I.C.A.V.	-	2,095
EMF Microfinance AgmvK	-	1,218
Total term borrowings	153,692	169,120

On 12 March 2009 the Bank signed a loan agreement with the International Development Fund of OPEC in the amount USD 5,000 thousand. The Bank received this loan on 27 May 2010. Principal amount is to be repaid in semi-annual instalments starting on 27 May 2012 and ending on 27 May 2013. Interest is paid in semi-annual instalments starting from 27 November 2010. At 31 December 2010, the balance of borrowing under this facility was USD 4,985 thousand or AZN 3,978 thousand.

On 8 December 2009 the Bank signed a loan agreement with the European Bank for Reconstruction and Development in the amount AZN equivalent of USD 10,000 thousand. The Bank received this loan in two tranches in the amount of USD 5,000 thousand each on 7 April 2010 and 7 August 2010. Principal amount is to be repaid in semi-annual instalments starting on 7 February 2011 and ending on 7 April 2014. Interest is paid in semi-annual instalments starting from 7 October 2010. At 31 December 2010, the balance of borrowing under this facility was AZN 8,238 thousand.

On 20 August 2010 the Bank signed a loan agreement with Microfinance Enhancement Facility SA, SICAV - SIF in the amount USD 7,500 thousand. Principal amount is to be repaid on 30 August 2013. Interest is paid in semi-annual instalments starting from 31 January 2011. At 31 December 2010, the balance of borrowing from Microfinance Enhancement Facility SA, SICAV - SIF was USD 7,542 thousand or AZN 6,018 thousand.

On 8 November 2010 the Bank signed a loan agreement with the Developing World Markets SCA – SICAV SIF in the amount of AZN equivalent of USD 3,000 thousand. Principal amount is to be repaid on 30 November 2012. Interest is paid in quarterly instalments starting from 28 February 2011. At 31 December 2010, the balance of borrowing from Developing World Markets SCA – SICAV SIF was AZN 2,404 thousand.

15 Other Borrowed Funds (continued)

All the above loans as well as the loans granted in earlier years bear market interest rates.

The Bank is obliged to comply with certain financial covenants stipulated by the aforementioned borrowing agreements. At 31 December 2010, management believes that the Bank was in compliance with those covenants.

Refer to Note 28 for disclosure of the fair value of each class of other borrowed funds. Interest rate analysis of other borrowed funds is disclosed in Note 25. Information on related party balances is disclosed in Note 30.

16 Other Financial Liabilities

Other financial liabilities comprise the following:

<i>In thousands of Azerbaijani Manats</i>	31 December 2010	31 December 2009
Accrued staff cost	2,140	1,661
Accrued expenses	259	176
Settlements with money transfer systems	157	136
Other	210	134
Total other financial liabilities	2,766	2,107

Refer to Note 28 for disclosure of the fair value of each class of other financial liabilities.

17 Subordinated Debt

On 2 July 2007 the Bank signed a subordinated loan agreement with Deutsche Bank Aktiengesellschaft (registered in Germany) for USD 10,211 thousand. The loan bears market interest rate. Principal is to be repaid on maturity, which is 31 December 2014. Interest is paid quarterly, starting from 31 August 2007. The debt ranks after all other creditors in case of liquidation. The Bank is obliged to comply with certain financial covenants stipulated by the aforementioned borrowing agreement. At 31 December 2010, management believes that the Bank was in compliance with those covenants. At 31 December 2010, the balance of the borrowing under this facility was USD 10,252 thousand or AZN 8,180 thousand (31 December 2009: USD 10,223 thousand or AZN 8,222 thousand).

Refer to Note 28 for the disclosure of the fair value of subordinated debt. Interest rate analysis of subordinated debt is disclosed in Note 25. Information on related party balances is disclosed in Note 30.

18 Share Capital

<i>In thousands of Azerbaijani Manats except for number of shares</i>	Number of outstanding shares	Ordinary shares	Total
At 1 January 2009	20,000	20,000	20,000
New shares issued	-	-	-
At 1 January 2010	20,000	20,000	20,000
Increase in nominal value of shares	-	21,800	21,800
At 31 December 2010	20,000	41,800	41,800

The total authorised number of shares is 20,000 thousand shares (31 December 2009: 20,000 thousand) with a par value of AZN 2.09 per share (31 December 2009: AZN 1 per share). All issued ordinary shares are fully paid. Each share carries one vote. The Bank did not issue any new shares in year ending 31 December 2010, however, funds amounting AZN 21,800 thousand were transferred from retained earnings to Share Capital which increased the nominal value of the shares.

As at 31 December 2010 and 2009, the following shareholders owned the issued shares of the Bank:

Owners	31 December 2010, % of shareholding	31 December 2009, % of shareholding
International Finance Corporation	20.00	20.00
Black Sea Trade and Development Bank	20.00	20.00
Kreditanstalt für Wiederaufbau	20.00	20.00
European Bank for Reconstruction and Development	20.00	20.00
Access Microfinance Holding AG	16.53	16.53
LFS Financial Systems GmbH	3.47	3.47
Total	100.0	100.0

19 Interest Income and Expense

<i>In thousands of Azerbaijani Manats</i>	2010	2009
Interest income		
Loans and advances to customers	86,861	66,647
Due from other banks	815	1,507
Investment securities available for sale	27	44
Total interest income	87,703	68,198
Interest expense		
Other borrowed funds	14,163	13,411
Customer accounts	10,491	4,231
Subordinated debt	935	933
Term placements of other banks	-	158
Total interest expense	25,589	18,733
Net interest income	62,114	49,465

20 Fee and Commission Income and Expense

<i>In thousands of Azerbaijani Manats</i>	2010	2009
Fee and commission income		
- Settlement transactions	351	251
- Commission from plastic cards	280	180
- Commission income on purchase or sale of foreign currency	253	147
- Cash collection	185	132
- Guarantees issued	35	40
- Other	25	17
Total fee and commission income	1,129	767
Fee and commission expense		
- Plastic cards	101	88
- Settlement transactions	57	35
- Cash transactions	2	43
- Other	15	5
Total fee and commission expense	175	171
Net fee and commission income	954	596

21 Administrative and Other Operating Expenses

<i>In thousands of Azerbaijani Manats</i>	Note	2010	2009
Staff costs		21,013	16,595
Advertising and marketing services		2,150	1,817
Depreciation of property and equipment	11	1,884	1,291
Printing, stationery and office supplies		1,698	1,314
Rent on office premises		1,384	1,245
Repair and maintenance		1,258	1,158
Service and membership fees		1,154	800
Security services		1,132	936
Communication		803	779
Software program support expense		717	525
Amortisation of software	11	558	472
Business travel expense		226	152
Utilities		182	134
Deposit Insurance Fund fees		144	110
Other		1,094	551
Total administrative and other operating expenses		35,397	27,879

Included in staff costs are social security contributions of AZN 3,524 thousand (2009: AZN 2,915 thousand).

22 Income Taxes

Income tax credit recorded in the statement of comprehensive income comprises the following:

<i>In thousands of Azerbaijani Manats</i>	2010	2009
Current tax expense	130	8
Deferred tax credit	(51)	(12)
Income tax charge / (credit) for the year	79	(4)

The income tax rate applicable to the majority of the Bank's income during the year ended 31 December 2010 is 20% (22% in 2009). The reconciliation between the expected and the actual taxation charge is provided below.

<i>In thousands of Azerbaijani Manats</i>	2010	2009
Profit before tax	26,249	19,982
Theoretical tax charge at statutory rate (20/22%)	5,250	4,396
Tax effect of permanent differences	29	106
Current income tax liability not accrued due to three-year tax holiday	(5,200)	(4,786)
Reversal of tax effect of temporary differences due to three-year tax holiday	-	280
Income tax charge / (credit) for the year	79	(4)

On 14 November 2008, a new law on "Stimulation of Increasing the Capitalization of Banks, Insurance and Reinsurance Companies" was enacted. According to the law the profit tax rate for banks, insurance and reinsurance companies is reduced to 0% for three fiscal years from 1 January 2009, for the portion of the profit which is transferred to the registered share capital. As management intended to transfer AZN 26,000 thousand of 2010 profit to registered share capital (2009: AZN 21,800 thousand) management accrued AZN 130 in current income tax liability for the remaining portion of profit which will not be transferred to registered share capital.

On 19 June 2009, the Republic of Azerbaijan reduced the standard corporate income tax rate from 22% to 20% with effect from 1 January 2010.

Differences between IFRS and statutory taxation regulations in Azerbaijan give rise to temporary differences between the carrying amount of assets and liabilities for financial reporting purposes and their tax bases. The tax effect of the movements in these temporary differences is detailed below:

<i>In thousands of Azerbaijani Manats</i>	1 January 2010	Credited to profit or loss	31 December 2010
Tax effect of deductible temporary differences			
Property, equipment and intangible assets	-	51	51
Net deferred tax asset	-	51	51

22 Income Taxes (continued)

<i>In thousands of Azerbaijani Manats</i>	1 January 2009	Credited/ (charged) to profit or loss	31 December 2009
Tax effect of deductible/(taxable) temporary differences			
Property, equipment and intangible assets	(18)	18	-
Other liabilities	6	(6)	-
Net deferred tax asset / (liability)	(12)	12	-

23 Earnings per Share

Basic earnings/(loss) per share are calculated by dividing the profit or loss attributable to equity holders of the Bank by the weighted average number of ordinary shares in issue during the year, excluding treasury shares.

The Bank has no dilutive potential ordinary shares; therefore, the diluted earnings per share equal the basic earnings per share. Earnings per share are calculated as follows:

<i>In thousands of Azerbaijani Manats except for number of shares</i>	2010	2009
Profit for the year attributable to ordinary shareholders	26,170	19,986
Weighted average number of ordinary shares in issue (thousands)	20,000	20,000
Basic and diluted profit per ordinary share (expressed in AZN per share)	1.31	0.99

24 Segment Information

The chief operating decision maker, the Management Board, reviews the Bank's internal reporting which primarily comprise the information prepared for IFRS reporting purposes in order to assess performance and allocate resources. The operating segments have been determined based on these reports as follows:

- Micro – Loans up to AZN 8 thousand issued to entrepreneurs and farmers;
- Trust – Loans between AZN 8 thousand and AZN 16 thousand issued to entrepreneurs and farmers;
- SME – Loans above AZN 16 thousand issued to entrepreneurs and small and medium enterprises for corporate purposes;
- Retail – Consumer loans issued to salaried individuals and attracted deposits and bank transaction business; and
- Staff Loans – Loans issued to employees of the Bank.

For the purposes of these financial statements the Bank aggregated Micro loans with Trust loans and called this reportable segment as "Micro"; and aggregated Retail with Staff Loans and called this reportable segment as "Retail". The aggregations were done in accordance with the qualitative and quantitative aggregation requirements as set out in IFRS 8.

24 Segment Information (continued)

The Management Board assesses the performance of the operating segments based on a measure of adjusted profit before income tax. This measurement basis excludes the effect of certain expenses from the operating segments as disclosed in the relevant reconciliation below. Other information provided to the Management Board is measured in a manner consistent with that in these financial statements, except for the items presented in the relevant reconciliation below. The reconciling items are managed at the Bank level and are not allocated to the segments for management and/or reporting purposes.

Segment information for the reportable segments of the Bank for the years ended 31 December 2010 and 31 December 2009 is set out below:

<i>In thousands of Azerbaijani Manats</i>	Micro	SME	Retail	Total
Year ended 31 December 2010				
External revenues:				
- Interest income	54,393	25,601	6,631	86,625
- Fee and commission income			1,129	1,129
- Other operating income			902	902
Revenue from external customers	54,393	25,601	8,662	88,656
External expenses:				
- Interest expense	13,360	10,118	2,111	25,589
- Fee and commission expense			175	175
- Provision for loan impairment	1,288	622	157	2,067
Expense from external customers	14,648	10,740	2,443	27,831
Adjusted profit before non-segment income, administrative and other expense and income tax	39,745	14,861	6,219	60,825
Total assets reported	138,741	105,362	22,082	266,185
Year ended 31 December 2009				
External revenues:				
- Interest income	40,250	21,706	4,611	66,567
- Fee and commission income	-	-	767	767
- Other operating income	-	-	399	399
Revenue from external customers	40,250	21,706	5,777	67,733
External expenses:				
- Interest expense	9,760	7,674	1,299	18,733
- Fee and commission expense	-	-	171	171
- Provision for loan impairment	1,250	1,284	65	2,599
Expense from external customers	11,010	8,958	1,535	21,503
Adjusted profit before non-segment income, administrative and other expense and income tax	29,240	12,748	4,242	46,230
Total assets reported	122,264	95,176	16,241	233,681

24 Segment Information (continued)

A reconciliation of adjusted profit before income tax to total profit before income tax is provided as follows:

<i>In thousands of Azerbaijan Manats</i>	Year ended 31 December 2010	Year ended 31 December 2009
Adjusted profit before non-segment income, administrative and other expense and income tax	60,825	46,230
Non-segment interest income	1,078	1,631
Impairment loss on property, plant and equipment	257	-
Administrative and other operating expenses	35,397	27,879
Profit before income tax	26,249	19,982

Reportable segments' assets are reconciled to total assets as follows:

<i>In thousands of Azerbaijan Manats</i>	31 December 2010	31 December 2009
Total segment assets (loans and advances to customers)	266,185	233,681
Cash and cash equivalents	57,805	46,567
Mandatory cash balances with CBAR	371	253
Investment securities available for sale	40	40
Due from other banks	7,023	9,828
Investment properties	21,708	-
Property, plant and equipment	9,382	7,123
Intangible assets	1,615	1,994
Deferred income tax asset	51	-
Other financial assets	527	289
Other assets	1,316	997
Total assets per statement of financial position	366,023	300,772

The above segment information is prepared in USD and then converted into AZN for the purposes of these financial statements. The balance sheet items are translated using the official exchange rate as of the reporting date. Management believes that, the exchange rates used to translate income and expenses approximate the exchange rates at the date of respective transactions.

As all of the Bank's operations are carried out in Azerbaijan, the Bank does not provide geographical information regarding its segments.

The Bank does not have any major customer that it relies on as prescribed in IFRS 8. Therefore, the Bank does not provide additional information on major customers.

25 Financial Risk Management

The Bank has exposure to financial risks which include credit, liquidity, market and operational risks. The taking of risk is integral to the Bank's business. The Bank's risk management function's aim is to achieve an appropriate balance between risk and return and to minimise potential adverse effects on the Bank's financial performance.

Risk Management Framework. The Management Board is the primary body responsible for the risk management function in the Bank. The risk management function is carried out in respect of financial risks (credit, market, and liquidity risks) and operational risks. Financial risk comprises market risk (including currency risk, interest rate risk and other price risk), credit risk and liquidity risk. The primary objectives of the financial risk management function of the Management Board are to establish risk limits and then ensure that exposure to risks stays within these limits. The Management Board is also responsible for ensuring an appropriate balance is established between risk and return, whilst minimizing any potential adverse effects on the Bank's financial performance. The operational and legal risk management functions are intended to ensure proper functioning of internal policies and procedures to minimise operational and legal risks.

25 Financial Risk Management (continued)

The Bank’s risk management methodology, policies and assessment procedures are designed to identify, analyse, mitigate and manage the risks faced by the Bank. This is accomplished through setting of appropriate risk limits and controls, whilst ensuring suitable monitoring of risk levels and compliance with the limits and procedures on an ongoing basis. The risk management policies and procedures are reviewed regularly to reflect changes in market conditions, and new products and services offered. This is to ensure that “best practices” are implemented in the Bank.

Risk Management Bodies and Governance. Risk management policies and processes around the assessment, approval, monitoring and control of risks are performed by a number of specialized bodies within the Bank, including committees and departments which comply with the requirement of the respective Azerbaijani laws, the CBAR regulations and industry best practices.

The Supervisory Board has overall responsibility for the oversight of the risk management framework. This includes the management of key risks, along with the review and approval of risk management policies and key risk limits such as large exposures, economic and product sector limits. It also delegates certain risk supervision authority levels to the Management Board, the Risk Management Committee, the Credit Committee, and the Asset and Liability Committee (“ALCO”).

Overall roles and responsibilities for the risk management framework are shown below:

Responsibility area	Decision-making body	Executive Management
Preparation of policies and procedures regarding Risk management	Management Board-level Risk Management Committee	
Market and liquidity risk	ALCO	Treasury
Credit, country, concentration risk	Risk Committee	Credit Department
Operational risks	Management Board	Bank’s Departments
Strategic and organisational risk	Supervisory Board	Management Board

In May 2010 the bank introduced a position of branch control officer on a pilot basis, dedicated full-time to performing control functions aimed at reducing credit and operational risks. Management intends to expand the appointment of branch control officers to all of its large branches.

Credit risk. The Bank takes on exposure to credit risk, which is the risk that one party to a financial instrument will cause a financial loss for the other party by failing to discharge an obligation. An exposure to credit risk arises as a result of the Bank’s lending and other transactions with counterparties giving rise to financial assets including likelihood that borrower or counterparty fails to meet their obligations in accordance with agreed terms.

The Bank’s maximum exposure to credit risk is reflected in the carrying amounts of financial assets on the statement of financial position. For guarantees and commitments to extend credit, the maximum exposure to credit risk is the amount of the commitment. Refer to Note 27. The credit risk is mitigated by collateral and other credit enhancements as disclosed in Note 9.

The principal credit risk management methods used is described in the formal Credit Policy adopted and implemented by the Bank. These include the setting of limits and the diversification of the credit portfolio based upon defined criterion (such as industry, duration, related persons, region, etc.). Credits will also be classified at initiation and throughout the life of the loan based upon a risk level determined using best practice rating systems. Such tools will also be used to establish appropriate provisions for potential losses as necessary. All restrictions and norms issued by the CBAR, related to lending operations, have also been carefully considered and embedded into the Bank’s Credit Policy.

The Bank also structures the levels of credit risk it undertakes by placing limits on the amount of risk accepted in relation to one borrower, or borrowers, and to geographical and industry segments. The limits on the level of credit risk by product and industry sector are approved regularly by management. Such risks are monitored on a revolving basis and subject to an annual or more frequent review.

25 Financial Risk Management (continued)

The general credit risk approval structure, for corporate legal entities, private individuals and financial organisations, is as follows:

For secured loans:

- The Supervisory Board reviews and approves limits above 3% of the total statutory equity up to a maximum limit of 20% of the total statutory equity for all loans and meets on a regular basis;
- The Credit Committee reviews and approves all limits below 3% of the total statutory equity. The Credit Committee meets on a regular basis.

Loan applications originated by the relevant client relationship managers are passed on to the relevant credit committee for approval of credit limit. Exposure to credit risk is also managed, in part, by obtaining collateral and corporate and personal guarantees.

The Bank uses formalised internal credit ratings to monitor exposures to credit risk. The Bank's credit department reviews ageing analysis of outstanding loans and follows up on past due balances. Management therefore considers it appropriate to provide ageing and other information about credit risk as disclosed in Notes 8 and 9.

Credit risk for off-balance sheet financial instruments is defined as the possibility of sustaining a loss as a result of another party to a financial instrument failing to perform in accordance with the terms of the contract. The Bank uses the same credit policies in assuming conditional obligations as it does for on-balance sheet financial instruments, through established credit approvals, risk control limits and monitoring procedures.

Market risk. The Bank takes on exposure to market risks. Market risks arise from open positions in (a) currency, (b) interest rate and (c) equity products, all of which are exposed to general and specific market movements. Management sets limits on the value of risk that may be accepted, which is monitored on a daily basis. However, the use of this approach does not prevent losses outside of these limits in the event of more significant market movements.

Currency risk. The Bank is exposed to the effects of fluctuations in the prevailing local/foreign currency exchange rates on its financial position. Currency risk is the risk that movements in foreign exchange rates will affect the Bank's income or the value of its portfolios of financial instruments.

The Bank uses every effort to match its assets and liabilities by currency. Exposure to foreign exchange risks faced by the Bank are also limited by the CBAR normative requirements, which place a 10% of capital limit on open positions in any single foreign currency and a 20% open limit on all foreign currencies.

25 Financial Risk Management (continued)

In respect of currency risk, management sets limits on the level of exposure by currency and in total for both overnight and intra-day positions, which are monitored daily.

The table below summarises the Bank's exposure to foreign currency exchange rate risk at the end of the reporting period:

<i>In thousands of Azerbaijani Manats</i>	At 31 December 2010			At 31 December 2009		
	Monetary financial assets	Monetary financial liabilities	Net position	Monetary financial assets	Monetary financial liabilities	Net position
Azerbaijani Manats	140,882	98,801	42,081	89,678	44,420	45,258
US Dollars	188,068	188,177	(109)	198,745	199,029	(284)
Euros	2,902	4,315	(1,413)	2,011	3,996	(1,985)
Other	99	16	83	224	8	216
Total	331,951	291,309	40,642	290,658	247,453	43,205

The following table presents sensitivities of profit or loss and equity to reasonably possible changes in exchange rates applied at the end of the reporting period, with all other variables held constant:

<i>In thousands of Azerbaijani Manats</i>	At 31 December 2010 Impact on profit or loss	At 31 December 2009 Impact on profit or loss
US Dollar strengthening by 10%	(11)	(28)
US Dollar weakening by 10%	11	28
Euro strengthening by 10%	(141)	(199)
Euro weakening by 10%	141	199

All investment securities available for sale as at 31 December 2010 and 31 December 2009 were denominated in AZN, therefore, any reasonable possible change in exchange rates would not have any impact on equity.

The exposure was calculated only for monetary balances denominated in currencies other than the functional currency of the respective entity of the Bank.

Interest rate risk. The Bank takes on exposure to the effects of fluctuations in the prevailing levels of market interest rates on its financial position and cash flows. Interest margins may increase as a result of such changes but may reduce or create losses in the event that unexpected movements arise. Management monitors on a daily basis and sets limits on the level of mismatch of interest rate repricing that may be undertaken.

25 Financial Risk Management (continued)

The table below summarises the Bank's exposure to interest rate risks. The table presents the aggregated amounts of the Bank's financial assets and liabilities at carrying amounts, categorised by the earlier of contractual interest re-pricing or maturity dates.

<i>In thousands of Azerbaijani Manats</i>	Demand and less than 1 month	From 1 to 6 months	From 6 to 12 months	More than 1 year	Total
31 December 2010					
Total financial assets	75,865	105,234	81,491	69,361	331,951
Total financial liabilities	22,733	79,876	71,983	116,717	291,309
Net interest sensitivity gap at 31 December 2010					
	53,132	25,358	9,508	(47,356)	40,642
31 December 2009					
Total financial assets	67,880	92,737	69,241	60,800	290,658
Total financial liabilities	17,535	74,440	37,643	117,835	247,453
Net interest sensitivity gap at 31 December 2009					
	50,345	18,297	31,598	(57,035)	43,205

At 31 December 2010, if interest rates at that date had been 100 basis points lower (2009: 100 basis points lower) with all other variables held constant, profit for the year would have been AZN 621 thousand (2009: AZN 495 thousand) higher, mainly as a result of lower interest expense on variable interest liabilities. The impact of a reasonably possible shift in market interest rates on components of equity, other than due to the effects of the change in profit on retained earnings, would not be significant.

If interest rates had been 100 basis points higher (2009: 100 basis points higher), with all other variables held constant, profit would have been AZN 621 thousand (2009: AZN 495 thousand) lower, mainly as a result of higher interest expense on variable interest liabilities. The impact of a reasonably possible shift in market interest rates on components of equity, other than due to the effects of the change in profit on retained earnings, would not be significant.

The Bank monitors interest rates for its financial instruments. The table below summarises effective interest rates, including the effect of any fees, commissions, and / or tax liabilities that may be payable, based on reports reviewed by key management personnel:

<i>In % p.a.</i>	31 December 2010			31 December 2009		
	AZN	USD	EUR	AZN	USD	EUR
Assets						
Due from other banks	9.6	-	-	9.5	7.8	-
Loans and advances to customers	34.6	26.4	15.0	35.2	27.9	-
Investment securities available for sale	-	-	-	4.1	-	-
Liabilities						
Term deposits	12.1	13.1	8.0	13.6	13.6	8.5
Term placements of other banks	-	-	-	-	10.5	-
Other borrowed funds	11.1	8.1	-	12.1	8.2	-
Subordinated debt	-	11.1	-	-	11.1	-

The sign “-“ in the table above means that the Bank does not have the respective assets or liabilities in the corresponding currency.

25 Financial Risk Management (continued)

Geographical risk concentrations. The geographical concentration of the Bank's financial assets and liabilities at 31 December 2010 is set out below:

<i>In thousands of Azerbaijani Manats</i>	Azerbaijan	OECD	Non-OECD	Total
Assets				
Cash and cash equivalents	52,477	4,999	329	57,805
Mandatory cash balances with the CBAR	371	-	-	371
Due from other banks	7,023	-	-	7,023
Loans and advances to customers	266,185	-	-	266,185
Investment securities available for sale	40	-	-	40
Other financial assets	121	332	74	527
Total financial assets	326,217	5,331	403	331,951
Liabilities				
Customer accounts	126,671	-	-	126,671
Other borrowed funds	-	140,939	12,753	153,692
Other financial liabilities	2,610	134	22	2,766
Subordinated debt	-	8,180	-	8,180
Total financial liabilities	129,281	149,253	12,775	291,309
Net position	196,936	(143,922)	(12,372)	40,642
Credit related commitments	748	-	-	748

25 Financial Risk Management (continued)

The geographical concentration of the Bank's financial assets and liabilities at 31 December 2009 is set out below:

<i>In thousands of Azerbaijani Manats</i>	Azerbaijan	OECD	Non-OECD	Total
Assets				
Cash and cash equivalents	40,652	5,476	439	46,567
Mandatory cash balances with CBAR	253	-	-	253
Due from other banks	9,828	-	-	9,828
Loans and advances to customer	233,681	-	-	233,681
Investment securities available for sale	40	-	-	40
Other financial assets	-	143	146	289
Total financial assets	284,454	5,619	585	290,658
Liabilities				
Due to other banks	2	-	3,003	3,005
Customer accounts	64,999	-	-	64,999
Other borrowed funds	-	152,333	16,787	169,120
Other financial liabilities	2,040	67	-	2,107
Subordinated debt	-	8,222	-	8,222
Total financial liabilities	67,041	160,622	19,790	247,453
Net position	217,413	(155,003)	(19,205)	43,205
Credit related commitments	482	-	-	482

Assets, liabilities and credit related commitments have generally been based on the country in which the counterparty is located. Balances with Azerbaijan counterparties actually outstanding to/from off-shore companies of these Azerbaijan counterparties are allocated to the caption "Azerbaijan". Cash on hand and premises and equipment have been allocated based on the country in which they are physically held.

Liquidity risk. Liquidity risk is the risk that an entity will encounter difficulties as a result of unavailability of funding in meeting obligations associated with financial liabilities when they fall due. The Bank is exposed to daily calls on its available cash resources from overnight deposits, current accounts, maturing deposits and loan drawdowns. The Bank generally does not maintain cash resources to meet all of these needs as experience shows that a minimum level of reinvestment of maturing funds can be predicted with a high level of certainty.

The day-to-day liquidity management is performed by the Treasury Department within a comprehensive framework set by the Assets and Liabilities Committee, and monitored independently by the Management Board. The Bank monitors and reports liquidity risk daily, paying particular attention to ensuring that there are optimal levels of cash and cash equivalent instruments to fund increases in assets, unexpected decreases in liabilities, as well as meeting legal requirements, while optimizing the cost of carrying any excess liquidity.

To manage liquidity risk, the Bank performs daily monitoring of future expected cash flows on clients' and banking operations, which forms part of the asset and liability management process. The Bank also has to comply with minimum levels of liquidity required by the CBAR. The Bank seeks to maintain a stable funding base primarily consisting of amounts due to other banks, corporate and retail customer deposits. The Bank invests the funds in diversified portfolios of liquid assets, in order to be able to respond quickly and smoothly to unforeseen liquidity requirements.

25 Financial Risk Management (continued)

The liquidity management of the Bank requires considering the level of liquid assets necessary to settle obligations as they fall due; maintaining access to a range of funding sources; maintaining funding contingency plans; and monitoring statement of financial position liquidity ratios against regulatory requirements. The Bank calculates instant liquidity ratio on a daily basis in accordance with the requirement of the CBAR. This ratio is calculated as the ratio of highly-liquid assets to liabilities payable on demand. The ratio was 374% at 31 December 2010, whereas the minimum percentage required by the CBAR is 30%.

The Treasury Department receives information about the liquidity profile of the financial assets and liabilities. The Treasury Department then provides for an adequate portfolio of short-term liquid assets, largely made up of short-term liquid trading securities, deposits with banks and other inter-bank facilities, to ensure that sufficient liquidity is maintained within the Bank as a whole.

The table below shows assets and liabilities at 31 December 2010 by their remaining contractual maturity. The amounts disclosed in the maturity table are the contractual undiscounted cash flows, including contractual amounts to be exchanged under gross loan commitments. Such undiscounted cash flows differ from the amount included in the statement of financial position because statement of financial position amount is based on discounted cash flows.

When the amount payable is not fixed, the amount disclosed is determined by reference to the conditions existing at the reporting date. Foreign currency payments are translated using the spot exchange rate at the end of the reporting period.

The maturity analysis of financial instruments at 31 December 2010 is as follows:

<i>In thousands of Azerbaijani Manats</i>	Demand and less than 1 month	From 1 to 6 months	From 6 to 12 months	From 12 months to 5 years	Over 5 years	Total
Assets						
Cash and cash equivalents	57,805	-	-	-	-	57,805
Mandatory reserves with the CBAR	-	-	-	-	371	371
Due from other banks	79	3,243	4,002	-	-	7,324
Loans and advances to customers	18,813	110,582	96,528	121,405	3,099	350,427
Investment securities available for sale	-	-	-	-	40	40
Other financial assets	256	-	-	-	271	527
Total	76,953	113,825	100,530	121,405	3,781	416,494
Liabilities						
Due to other banks	-	-	-	-	-	-
Customer accounts	20,060	31,666	48,589	30,208	-	130,523
Other borrowed funds	-	28,984	37,634	108,911	-	175,529
Other financial liabilities	2,766	-	-	-	-	2,766
Subordinated debt	-	454	454	10,906	-	11,814
Financial guarantees	245	399	52	52	-	748
Total potential future payments for financial obligations	23,071	61,503	86,729	150,077	-	321,380
Liquidity gap arising from financial instruments	53,882	52,322	13,801	(28,672)	3,781	
Cumulative liquidity gap	53,882	106,204	120,005	91,333	95,114	

25 Financial Risk Management (continued)

The maturity analysis of financial instruments at 31 December 2009 is as follows:

<i>In thousands of Azerbaijani Manats</i>	Demand and less than 1 month	From 1 to 6 months	From 6 to 12 months	From 12 months to 5 years	Over 5 years	Total
Assets						
Cash and cash equivalents	46,567	-	-	-	-	46,567
Mandatory reserves with the CBAR	-	-	-	-	253	253
Due from other banks	3,315	6,672	-	-	20	10,007
Loans and advances to customers	17,963	93,309	86,290	108,626	2,185	308,373
Investment securities available for sale	-	-	-	-	40	40
Investments held to maturity	-	-	-	-	-	-
Other financial assets	289	-	-	-	-	289
Total	68,134	99,981	86,290	108,626	2,498	365,529
Liabilities						
Due to banks	2	3,095	-	-	-	3,097
Customer accounts	13,387	13,054	31,590	12,036	-	70,067
Other borrowed funds	2,102	21,109	19,280	154,635	362	197,488
Other financial liabilities	2,107	-	-	-	-	2,107
Subordinated debt	-	455	455	11,841	-	12,751
Financial guarantees	69	213	200	-	-	482
Total potential future payments for financial obligations	17,667	37,926	51,525	178,512	362	285,992
Liquidity gap arising from financial instruments	50,467	62,055	34,765	(69,886)	2,136	79,537
Cumulative liquidity gap	50,467	112,522	147,287	77,401	79,537	

Liquidity requirements to support calls under guarantees and standby letters of credit are considerably less than the amount of the commitment disclosed in the above maturity analysis because the Bank does not generally expect the third party to draw funds under the agreement. The total outstanding contractual amount of commitments to extend credit as included in the above maturity table does not necessarily represent future cash requirements, since many of these commitments will expire or terminate without being funded.

25 Financial Risk Management (continued)

The Bank does not use the above maturity analysis based on undiscounted contractual maturities of liabilities to manage liquidity. Instead, the Bank monitors expected maturities and the resulting expected liquidity gap as follows:

<i>In thousands of Azerbaijani Manats</i>	Demand and less than 1 month	From 1 to 6 months	From 6 to 12 months	From 12 months to 5 years	Over 5 years	Total
At 31 December 2010						
Financial assets	75,865	105,234	81,491	66,747	2,614	331,951
Financial liabilities	22,733	60,026	80,293	128,257	-	291,309
Net liquidity gap based on expected maturities	53,132	45,208	1,198	(61,510)	2,614	40,642
At 31 December 2009						
Financial assets	67,880	92,737	69,241	59,660	1,140	290,658
Financial liabilities	17,534	36,410	47,491	145,744	274	247,453
Net liquidity gap based on expected maturities	50,346	56,327	21,750	(86,084)	866	43,205

The above analysis is based on expected maturities. The entire portfolio of trading securities is therefore classified within demand and less than one month based on management's assessment of the portfolio's realisability.

The matching and/or controlled mismatching of the maturities and interest rates of assets and liabilities is fundamental to the management of the Bank. It is unusual for banks ever to be completely matched since business transacted is often of an uncertain term and of different types. An unmatched position potentially enhances profitability, but can also increase the risk of losses. The maturities of assets and liabilities and the ability to replace, at an acceptable cost, interest-bearing liabilities as they mature, are important factors in assessing the liquidity of the Bank and its exposure to changes in interest and exchange rates.

Management believes that in spite of a substantial portion of customer accounts being on demand, diversification of these deposits by number and type of depositors, and the past experience of the Bank would indicate that these customer accounts provide a long-term and stable source of funding for the Bank.

26 Management of Capital

The objectives of management when managing the Bank's capital are (i) to comply with the capital requirements set by the CBAR and (ii) to safeguard the Bank's ability to continue as a going concern. Compliance with capital adequacy ratios set by the CBAR is monitored monthly with reports outlining their calculation reviewed and signed by the Finance Director. The other objectives of capital management are evaluated annually.

Under the current capital requirements set by the CBAR banks have to: (a) hold the minimum level of total statutory capital of AZN 10,000 thousand; (b) maintain a ratio of regulatory capital to risk weighted assets ("statutory capital ratio") at or above a prescribed minimum of 12% and (c) maintain a ratio of tier-1 capital to the risk-weighted assets (the 'Tier-1 capital ratio') at or above the prescribed minimum of 6%. Regulatory capital is based on the Bank's reports prepared under the CBAR's regulations and comprises:

<i>In thousands of Azerbaijani Manats</i>	31 December 2010	31 December 2009
Net assets calculated based on CBAR rules	48,285	33,299
Less investments	(40)	(40)
Less intangible assets	(1,568)	(1,995)
Plus statutory profit for the year	26,372	19,986
Plus general provision for impairment	3,984	3,473
Plus subordinated debt	6,518	7,885
Total regulatory capital	83,551	62,608
Total capital adequacy ratio	28.2%	22.5%

The Bank is also subject to minimum capital requirements established by covenants stated in loan agreements, including capital adequacy levels calculated in accordance with the requirements of the Basel Accord, as defined in the International Convergence of Capital Measurement and Capital Standards (updated April 1998) and Amendment to the Capital Accord to incorporate market risks (updated November 2005), commonly known as Basel I. The composition of the Bank's capital calculated in accordance with Basel Accord is as follows:

<i>In thousands of Azerbaijani Manats</i>	2010	2009
Tier 1 capital		
Share capital	41,800	20,000
Retained earnings	32,655	33,285
Total tier 1 capital	74,455	53,285
Tier 2 capital		
Provision on risk weighted assets	3,757	3,076
Subordinated debt	6,518	8,200
Less: investments in financial institutions	(40)	(40)
Total tier 2 capital	10,235	11,236
Total capital	84,690	64,521
Total capital adequacy ratio	28.2%	26.2%

The Bank complied with all externally imposed capital requirements throughout the year ended 31 December 2010.

27 Contingencies and Commitments

Legal proceedings. From time to time and in the normal course of business, claims against the Bank may be received. On the basis of its own estimates and internal professional advice management is of the opinion that no material losses will be incurred in respect of claims and accordingly no provision has been made in these financial statements.

Tax legislation. Tax, currency and customs legislation of the Republic of Azerbaijan are subject to varying interpretations, and changes, which can occur frequently. Management's interpretation of such legislation as applied to the transactions and activity of the Bank may be challenged by the relevant tax authorities. As a result, significant additional taxes, penalties and interest may be assessed. According to the Tax Code of the Republic of Azerbaijan fiscal periods remain open to review by the authorities in respect of taxes for three calendar years preceding the year of review. Under certain legislative circumstances reviews may cover longer periods.

The Bank's management believes that its interpretation of the relevant legislation is appropriate and the Bank's tax, currency and customs positions will be sustained. Accordingly, at 31 December 2010 no provision for potential tax liabilities was recorded.

Capital expenditure commitments. As at 31 December 2010, the Bank had no capital expenditure commitments.

Operating lease commitments. As at 31 December 2010, the Bank had no commitments under non-cancellable lease agreements.

Contingent assets. The bank has entered into a contract with Nederlandse Financierings-Maatschappij Voor Ontwikkelingslanden N.V for a borrowing of USD 20,000 thousand on 24 December 2010 with a maturity date of 09 December 2013. The funds from this contract have not been drawn down as at 31 December 2010.

Compliance with covenants. As at 31 December 2010 and during the year then ended, there were covenants that the Bank should have complied with. The Bank is subject to certain covenants related primarily to its borrowings. Non-compliance with such covenants may result in negative consequences for the Bank including, growth in the cost of borrowings and declaration of default. As at 31 December 2010 the Bank was in compliance with all covenants imposed by international financial institutions, and local regulators.

Credit related commitments. The primary purpose of these instruments is to ensure that funds are available to a customer as required. Guarantees and standby letters of credit, which represent irrevocable assurances that the Bank will make payments in the event that a customer cannot meet its obligations to third parties, carry the same credit risk as loans. Documentary and commercial letters of credit, which are written undertakings by the Bank on behalf of a customer authorising a third party to draw drafts on the Bank up to a stipulated amount under specific terms and conditions, are collateralised by the underlying shipments of goods to which they relate or cash deposits and therefore carry less risk than a direct borrowing.

Commitments to extend credit represent unused portions of authorisations to extend credit in the form of loans, guarantees or letters of credit. With respect to credit risk on commitments to extend credit, the Bank is potentially exposed to loss in an amount equal to the total unused commitments. However, the likely amount of loss is less than the total unused commitments since most commitments to extend credit are contingent upon customers maintaining specific credit standards. The Bank monitors the term to maturity of credit related commitments because longer-term commitments generally have a greater degree of credit risk than shorter-term commitments. Outstanding credit related commitments and their fair values are as follows:

27 Contingencies and Commitments (continued)

<i>In thousands of Azerbaijani Manats</i>	31 December 2010	31 December 2009
Guarantees issued	748	482
Total credit related commitments	748	482

The credit related commitments were denominated in Azerbaijani Manats at 31 December 2010. The future undiscounted cash flows from credit related commitments are equal to AZN 10 thousand (31 December 2009: AZN 15 thousand) as at 31 December 2010.

28 Fair Value of Financial Instruments

(a) Fair values of financial instruments carried at amortised cost.

At 31 December 2010, fair values of financial instruments carried at amortised cost approximated to their carrying values.

Fair value is the amount at which a financial instrument could be exchanged in a current transaction between willing parties, other than in a forced sale or liquidation, and is best evidenced by an active quoted market price. Where quoted market prices are not available, the Bank used valuation techniques. Certain valuation techniques required assumptions that were not supported by observable market data.

The fair value of unquoted fixed interest rate instruments was estimated 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. Discount rates used depend on currency, maturity of the instrument and credit risk of the counterparty and were as follows:

	31 December 2010	31 December 2009
Due from other banks		
Short-term placements with other banks	9% to 10% p.a.	7% to 14% p.a.
Loans and advances to customers		
Loans to customers – SME and micro loans	12% to 36% p.a.	16% to 36% p.a.
Loans to customers – Retail loans to salaried individuals	12% to 39% p.a.	12% to 39% p.a.
Customer accounts		
- Customer accounts	1% to 20% p.a.	2% to 20% p.a.
Other borrowed funds		
- Term borrowings from companies/government agencies	3.5% to 12% p.a.	8% to 12% p.a.
Subordinated debt		
- Subordinated debt	11% p.a.	11% p.a.

29 Presentation of Financial Instruments by Measurement Category

For the purposes of measurement, IAS 39, *Financial Instruments: Recognition and Measurement*, classifies financial assets into the following categories: (a) loans and receivables; (b) available-for-sale financial assets; (c) financial assets held to maturity and (d) financial assets at fair value through profit or loss ("FVTPL"). Financial assets at fair value through profit or loss have two subcategories: (i) assets designated as such upon initial recognition, and (ii) those classified as held for trading.

29 Presentation of Financial Instruments by Measurement Category (continued)

The following table provides a reconciliation of classes of financial assets with these measurement categories as of 31 December 2010:

	Loans and receivables	Investment securities available for sale (through equity)	Total
<i>In thousands of Azerbaijani Manats</i>			
ASSETS			
Cash and cash equivalents	57,805	-	57,805
Mandatory cash balances with the CBAR	371	-	371
Investments securities available for sale	-	40	40
Due from other banks			
- Short-term placements with other banks	7,023	-	7,023
Loans and advances to customers			
- Micro loans	138,741	-	138,741
- SME loans	105,362	-	105,362
- Retail loans to salaried individuals	16,840	-	16,840
- Staff loans	5,242	-	5,242
Other financial assets	527	-	527
TOTAL FINANCIAL ASSETS	331,911	40	331,951
NON-FINANCIAL ASSETS	34,072	-	34,072
TOTAL ASSETS	365,983	40	366,023

The following table provides a reconciliation of financial assets with the measurement categories defined in IAS 39, *Financial Instruments: Recognition and Measurement*, as of 31 December 2009:

	Loans and receivables	Investment Securities Available for Sale (through equity)	Held to maturity	Total
<i>In thousands of Azerbaijani Manats</i>				
ASSETS				
Cash and cash equivalents	46,567	-	-	46,567
Mandatory reserves with CBAR	253	-	-	253
Investment securities available for sale	-	40	-	40
Due from other banks				
- Short-term placements with other banks with original maturities of more than three months	9,828	-	-	9,828
Loans and advances to customers				
- Micro loans	122,264	-	-	122,264
- SME loans	95,176	-	-	95,176
- Retail loans to salaried individuals	11,321	-	-	11,321
- Staff loans	4,920	-	-	4,920
Other financial assets	289	-	-	289
TOTAL FINANCIAL ASSETS	290,618	40	-	290,658
NON-FINANCIAL ASSETS	10,114	-	-	10,114
TOTAL ASSETS	300,732	40	-	300,772

30 Related Party Transactions

Parties are generally considered to be related if the parties are under common control or one party has the ability to control the other party or can exercise significant influence over the other party in making financial or operational decisions. In considering each possible related party relationship, attention is directed to the substance of the relationship, not merely the legal form.

At 31 December 2010, the outstanding balances with related parties were as follows:

<i>In thousands of Azerbaijani Manats</i>	Shareholders	Entities under joint control	Key management personnel
Gross amount of loans and advances to customers	-	-	128
Current accounts	-	-	58
Term deposits	-	-	288
Other borrowed funds	53,041	-	-

At 31 December 2009, the outstanding balances with related parties were as follows:

<i>In thousands of Azerbaijani Manats</i>	Shareholders	Entities under joint control	Key management personnel
Gross amount of loans and advances to customers	-	-	263
Due to banks	-	3,003	-
Current accounts	-	-	32
Term deposits	-	-	298
Other borrowed funds	58,020	-	-

The income and expense items with related parties for the year ended 31 December 2010 were as follows:

<i>In thousands of Azerbaijani Manats</i>	Shareholders	Key management personnel
Interest income	-	22
Interest expense	4,229	23
Payment for management and software support	1,410	-

The income and expense items with related parties for the year ended 31 December 2009 were as follows:

<i>In thousands of Azerbaijani Manats</i>	Shareholders	Key management personnel
Interest income	-	31
Interest expense	3,020	33
Payment for management and software support	1,012	-

30 Related Party Transactions (continued)

Key management compensation is presented below:

<i>In thousands of Azerbaijani Manats</i>	31 December 2010		31 December 2009	
	Expense	Accrued liability	Expense	Accrued liability
<i>Short-term benefits:</i>				
- Salaries	762	222	482	92
Total	762	222	482	92

31 Events After the End of the Reporting Period

Subsequent to the end of the reporting period, according to the decision of the General Assembly of Shareholders held on 15 December 2010 the Bank increased its share capital from AZN 41,800 thousand to AZN 67,800 thousand, by utilising AZN 26,000 thousand of its statutory taxable profit for the year ended 31 December 2010. The nominal value of the shares increased from AZN 2.09 to 3.39. There was no change in the distribution or number of shares. The new share certificates were issued on 3 March 2011 and registered by the State Securities Committee on 11 March 2011.

The bank has subsequently repaid AZN 18,389 of the principal amount thousand and AZN 5,071 thousand interest totalling AZN 23,460 thousand on its Other Borrowed Funds.

On 24 December 2010, the Bank signed a term facility agreement with Nederlandse Financierings-Maatschappij Voor Ontwikkelingslanden N.V. (FMO) in the amount of USD 20,000 thousand. On 28 March 2011, the Bank received the first tranche of USD 10,000 thousand under this agreement. Principal amounts and interests are to be repaid, in four equal semi-annual installments starting from 9 June 2012 and semi-annually starting from 9 June 2011, respectively. The facility bears market interest rate.