

NBCO Azeri Star Microfinance LLC

Financial Statements
for the Year Ended 31 December 2010
and Independent Auditor's Report

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Independent Auditor's Report

To the Shareholders and the Supervisory Council of NBCO Azeri Star Microfinance LLC

We have audited the accompanying financial statements of NBCO Azeri Star Microfinance LLC, which comprise the statement of financial position as at 31 December 2010, and the statement of comprehensive income, statement of cash flows and statement of changes in equity for the year then ended, and a summary of significant accounting policies and other explanatory notes.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with International Financial Reporting Standards, and for such internal control as management determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express an opinion on these financial statements based on our audit.

The financial statements for the year ended 31 December 2009 were audited by another auditor whose report dated 31 March 2010 expressed an unqualified opinion.

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 NBCO Azeri Star Microfinance LLC as at 31 December 2010, and its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards.

28 June 2011

Statement of Management's Responsibilities for the Preparation and Approval of the Financial Statements for the Year Ended 31 December 2010

The following statement, which should be read in conjunction with the independent auditor's responsibilities stated in the independent auditor's report set out on page 3, is made with a view to distinguishing the respective responsibilities of the management and those of the independent auditor in relation to the financial statements of NBCO Azeri Star Microfinance Limited Liability Company ("the Company").

Management is responsible for the preparation of the financial statements that present fairly the financial position of the Company as at 31 December 2010, the results of its operations, cash flows and changes in equity for the year then ended, in accordance with International Financial Reporting Standards ("IFRS").

In preparing the financial statements, management is responsible for:

- Selecting suitable accounting principles and applying them consistently;
- Making judgments and estimates that are reasonable and prudent;
- Stating whether IFRS have been followed, subject to any material departures disclosed and explained in the financial statements; and
- Preparing the financial statements on a going concern basis, unless it is inappropriate to presume that the Company will continue in business for the foreseeable future.

Management is also responsible for:

- Designing, implementing and maintaining an effective and sound system of internal controls throughout the Company;
- Maintaining proper accounting records that disclose, with reasonable accuracy at any time, the financial position of the Company, and which enable them to ensure that the financial statements of the Company comply with IFRS;
- Maintaining statutory accounting records in compliance with legislation and accounting standards of the Republic of Azerbaijan;
- Taking such steps as are reasonably available to them to safeguard the assets of the Company; and
- Detecting and preventing fraud and other irregularities.

On behalf of the Company's management the financial statements for the year ended 31 December 2010 were authorised for issue on 28 June 2011 by:

Rufat Abas
Chief Executive Officer

Rovshan Mammadov
Chief Accountant

NBCO Azeri Star Microfinance LLC
Baku, Azerbaijan

NBCO Azeri Star Microfinance LLC
Statement of Financial Position as at 31 December 2010
in Azerbaijani manats, unless otherwise indicated

	Note	2010	2009
Assets			
Cash and cash equivalents	6	18,672	370,256
Loans to customers	7	1,802,695	2,112,016
Property and equipment	8	38,377	50,187
Deferred income tax assets	9	10,764	-
Receivable from the Ministry of Taxes	9	107,116	-
Other assets	10	3,937	9,162
Total assets		1,981,561	2,541,621
Liabilities and equity			
Liabilities			
Borrowings	11	918,254	1,296,333
Current income tax liabilities	9	27,834	16,617
Deferred income tax liabilities	9	-	2,389
Other liabilities	12	14,218	16,535
Total liabilities		960,306	1,331,874
Equity			
Share capital	13	32,229	32,229
Accumulated grants	14	348,964	588,964
Retained earnings		640,062	588,554
Total equity		1,021,255	1,209,747
Total liabilities and equity		1,981,561	2,541,621

Rufat Abas
Chief Executive Officer

Rovshan Mammadov
Chief Accountant

28 June 2011

The notes set out on pages 9 to 33 are an integral part of these financial statements.

NBCO Azeri Star Microfinance LLC
Statement of Comprehensive Income for the Year Ended 31 December 2010
in Azerbaijani manats, unless otherwise indicated

	Note	2010	2009
Interest income	15	1,135,263	1,107,383
Interest expense	15	(184,511)	(143,007)
Net interest income		950,752	964,376
(Provision)/recovery of provision for impairment of loans to	7	(25,160)	26,984
Net interest income after loan impairment charges		925,592	991,360
Operating expenses	16	(687,354)	(769,336)
Other income		3	3,647
Profit before income taxes		238,241	225,671
Income tax expense for the year	9	(38,200)	(53,562)
Additional current income tax charge	9	(148,533)	-
Net profit for the year		51,508	172,109
Donations made	14	(240,000)	-
Total comprehensive income for the year		(188,492)	172,109

Rufat Abas
Chief Executive Officer

Rovshan Mammadov
Chief Accountant

28 June 2011

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NBCO Azeri Star Microfinance LLC
Statement of Cash Flows for the Year Ended 31 December 2010
in Azerbaijani manats, unless otherwise indicated

	Note	2010	2009
Cash flows from operating activities			
Profit before income taxes		238,241	225,671
Adjustments for:			
(Provision)/recovery of provision for impairment of loans to customers	7	25,160	(27,026)
Depreciation charge	8	16,734	29,711
<i>Cash flows from operating activities before changes in operating assets and liabilities</i>		<i>280,135</i>	<i>228,356</i>
<i>Changes in operating assets and liabilities</i>			
<i>(Increase)/decrease in operating assets:</i>			
Loans to customers	7	284,160	(179,424)
Receivable from the Ministry of Taxes	9	(107,116)	-
Other assets	10	5,225	(9,162)
<i>Increase/(decrease) in operating liabilities:</i>			
Accrued interest on borrowings	11	(8,677)	6,599
Other liabilities	12	(2,317)	-
<i>Cash inflow from operating activities before taxation and donations made</i>		<i>451,410</i>	<i>46,369</i>
Current income tax paid	9	(188,669)	(85,579)
Donations made	14	(240,000)	-
Net cash inflow/(outflow) from operating activities		22,741	(39,210)
Cash flow from investment activities			
Purchases of property and equipment	8	(4,924)	(45,515)
Net cash outflow from investing activities		(4,924)	(45,515)
Cash flows from financing activities			
Borrowings received	11	-	676,720
Borrowings repaid	11	(369,401)	(257,932)
Net cash (outflow)/inflow from financing activities		(369,401)	418,788
Net (decrease)/increase in cash and cash equivalents		(351,584)	334,063
Cash and cash equivalents at the beginning of the year	6	370,256	36,193
Cash and cash equivalents at the end of the year	6	18,672	370,256

Rufat Abas
Chief Executive Officer

Rovshan Mammadov
Chief Accountant

28 June 2011

NBCO Azeri Star Microfinance LLC
Statement of Changes in Equity for the Year Ended 31 December 2010
in Azerbaijani manats, unless otherwise indicated

	<u>Share capital</u>	<u>Accumulated grants</u>	<u>Retained earnings</u>	<u>Total equity</u>
31 December 2008	32,229	588,964	416,445	1,037,638
Net profit for the year	-	-	172,109	172,109
31 December 2009	32,229	588,964	588,554	1,209,747
Net profit for the year	-	-	51,508	51,508
Donations made	-	(240,000)	-	(240,000)
31 December 2010	32,229	348,964	640,062	1,021,255

Rufat Abas
Chief Executive Officer

Rovshan Mammadov
Chief Accountant

28 June 2011

The notes set out on pages 9 to 33 are an integral part of these financial statements.

1. Principal Activities of the Company

Non-banking Credit Organization "Azeri Star Microfinance" LLC ("the Company") was established by Save the Children Federation, Inc on 18 July 2002 and passed the state registration 6 June 2003. The Company commenced its operations in March 2006 under lending license issued by the Central Bank of the Republic of Azerbaijan dated 13 July 2005. The Company has three branches in Barda, Ganja and Goychay and the Head Office in Barda. The territories of Azerbaijan covered by the Company's activities include Agdam, Agdash, Agjabedi, Barda, Dashkasan, Ganja, Goranboy, Goychay, Goygol, Mingachevir, Samukh, Tartar, Ujar and Yevlah.

The main objectives of the Company are:

- Supporting development of micro, small and medium sized enterprises, included those engaged in production and agricultural activities;
- Creating new employment opportunities in family and other types of enterprises;
- Providing equal access to financial resources for both men and women.

The legal address of the Company is 9A/1 Gen. Akim Abbasov Street, Baku, Azerbaijan. The Head Office is located at 45 Baku Street, Barda, Azerbaijan.

Save the Children Federation, Inc., a US corporation registered at 54 Wilton Road, Westport, Connecticut 06880, United States of America, is the founder, the sole owner and the ultimate controlling party of the Company.

The average annual number of the Company's employees in 2010 was 48 (2009: 45).

2. Operating Environment of the Company

General

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

Although recently there have been positive economic signs in Azerbaijan, the long-term prospects for the Azerbaijani economy remain uncertain. National economy is dependent of export of hydrocarbon resources. As a result, the Company's assets and operations could be at risk resulting from any adverse changes in the political and business environment.

Financial market transactions

The international financial crisis has resulted in, among other things, global liquidity crunch which led to contraction of the international and domestic capital market, lower liquidity levels across the Azerbaijani banking sector and very high uncertainty in the domestic and foreign equity markets. The uncertainties in the global financial market have also led to bank failures and bank rescues in the United States of America, Western Europe, Russia and other countries, however its impact on financial system of Azerbaijan has been relatively limited. Currently, it is impossible to fully assess the influence of the ongoing crisis or avoid its impact.

Since 2008 investors have been re-evaluating their exposure to risks, which resulted in reduced or closed limits on transactions conducted in Azerbaijan, thereby adding to volatility. Such circumstances can affect the ability of the Company to obtain new borrowings at terms and conditions similar to those applied to earlier transactions.

Borrowers and debtors of the Company may also be affected by the repercussions of the financial crisis, which can in turn impact their ability to meet their financial obligations to the Company. To the extent that information is available, management has adequately reflected revised estimates of expected future cash flows in their impairment assessments. These financial statements do not include the adjustments reflecting the impact on the Company's financial position of further deterioration in the liquidity on the financial markets and the increased volatility in the currency and equity markets.

Inflation

In 2010 inflation in Azerbaijan was significant, although less than in previous years. The official inflation indices for the last two years are given in the table below:

Year ended	Inflation for the period
31 December 2010	5.7%
31 December 2009	1.5%

Currency transactions

National currency of Azerbaijan - manat - is the main currency used within the country. Foreign currencies, in particular the US dollar ("USD"), play a significant role in measuring economic parameters of many business transactions in Azerbaijan. The table below shows the exchange rates of US dollar relative to manat:

	2010	2009
1 US dollar - as at 31 December	0.7979	0.8031

3. Basis of Presentation

General principles

These financial statements of the Company are prepared in accordance with International Financial Reporting Standards ("IFRS"). The Company maintains its accounting records in accordance with the applicable legislation of the Republic of Azerbaijan. These financial statements have been prepared on the basis of those accounting records and adjusted as necessary in order to comply, in all material respects, with IFRS.

Functional and presentation currency

These financial statements are presented in Azerbaijani manats ("AZN") being the Company's functional and presentation currency.

Estimates and assumptions

The preparation of the financial statements requires the use of estimates and assumptions that affect the reported amounts of assets and liabilities, disclosure of contingent assets and liabilities as at the date of the financial statements preparation, and the reported amounts of revenues and expenses during the reporting period. Issues that require best estimate and are most significant for the financial statements are disclosed in Notes 7, 8, 9.

Going concern

These financial statements reflect the Company management's current assessment of the impact of the Azerbaijani business environment on the operations and the financial position of the Company. The future economic direction of Azerbaijan is largely dependent upon the effectiveness of measures undertaken by the Azerbaijani Government and other factors, including regulatory and political developments which are beyond the Company's control. The Company's management cannot predict what impact these factors can have on the Company's financial position in future. The accompanying financial statements do not include the adjustments associated with this risk.

For prompt management of liquidity risk the Company regularly monitors external factors, which could influence the Company's liquidity level, and forecasts cash flows. For the medium- and long-term liquidity risk management the Company analyses maturity mismatches of assets and liabilities. To reduce its risk exposure the Company sets liquidity gap limits. The set limits are periodically reviewed to reflect the changes in external and internal environment.

To maintain the required liquidity level the Company can attract additional funds from external lending market. Diversification of liquidity sources allows to minimise the Company's dependence on any source and ensure full satisfaction of its liabilities. A sufficient current liquidity cushion accumulated by the Company and the available sources of additional fund-raising allow the Company to continue its operations as a going concern on a long-term basis.

Prior year errors

In the reporting period the Company corrected balances for current income tax payable and other liabilities in the statement of financial position as at 31 December 2009, that resulted in increase in amounts of both elements by AZN 16,617 and AZN 16,139 respectively.

Changes in Accounting Policies

The accounting policies adopted are generally consistent with those of the previous financial year. Listed below are those amended standards and interpretations which are or in the future could be relevant to the Company's operations:

- IAS 1 "Presentation of Financial Statements" (effective for annual periods beginning on or after 1 January 2010). The main amendment is the change in classification of the liability component of a convertible instrument as current or non-current.
- IAS 7 "Statement of Cash Flows" (effective for annual periods beginning on or after 1 January 2010). The revised Standard (paragraph 16) requires that only expenditures that result in a recognised asset can be classified as a cash flow from investing activities.
- IAS 17 "Leases" (effective for annual periods beginning on or after 1 January 2010). The classification of the land and building elements as finance or operating lease should be made separately for each element and should follow the general lease classification guidance. For classification of land all factors provided for other lease contracts should be considered.
- IAS 36 "Impairment of Assets" (effective for annual periods beginning on or after 1 January 2010). According to the revised Standard, each cash-generating unit or group of units to which goodwill is allocated shall not be larger than an operating segment before aggregation.
- IAS 39 "Financial Instruments: Recognition and Measurement" (effective for annual periods beginning on or after 1 January 2010). The key areas of amendments included treatment of loan prepayment penalties as closely related embedded derivatives, scope exemption for business combination contracts and cash flow hedge accounting.
- IFRS 5 "Non-current Assets Held for Sale and Discontinued Operations" (effective for annual periods beginning on or after 1 January 2010). The scope of IFRS 5 has been clarified to make it clear that only the disclosures specified in IFRS 5 are applicable to non-current assets (or disposal groups) classified as held for sale, and to discontinued operations.
- IFRIC 19 "Extinguishing Financial Liabilities with Equity Instruments" (effective for annual periods beginning on or after 1 July 2010). This IFRIC provides guidance on treating settlement of a financial liability through the issue of an entity's own equity to the creditor.

IFRSs and IFRIC interpretations not yet effective

The Company has not applied the following IFRSs and Interpretations of the International Financial Reporting Interpretations Committee (IFRIC) that have been issued but are not yet effective:

- Amendments to IFRS 1 "Limited Exemption from Comparative IFRS 7 Disclosures for First-time Adopters" (effective for annual periods beginning on or after 1 July 2010).
- Amendments to IFRS 7 "Disclosures - Transfers of Financial Assets" (effective for annual periods beginning on or after 1 July 2011). These Amendments increase the disclosure requirements for transactions involving transfers of financial assets.
- IFRS 9 (as amended in 2010) "Financial Instruments" (effective for annual periods beginning on or after 1 January 2013). This Standard issued in November 2009 and amended in October 2010 introduces new requirements for the classification and measurement of financial assets and financial liabilities and for derecognition.
- IAS 24 (revised in 2009) "Related Party Disclosures" (effective for annual periods beginning on or after 1 January 2011). This revised Standard modifies the definition of a related party and simplifies disclosures for government-related entities.
- Amendments to IAS 32 "Classification of Rights Issues" (effective for annual periods beginning on or after 1 February 2010). The Amendments address the classification of certain rights issues denominated in a foreign currency as either an equity instrument or as a financial liability.
- Amendments to IFRIC 14 "Prepayments of a Minimum Funding Requirement" (effective for annual periods beginning on or after 1 January 2011).

The Management anticipates that IFRS 9 that will be adopted in the Company's financial statements for the annual period beginning 1 January 2013 and that the application of the new Standard will have a significant impact on amounts reported in respect of the Company's financial assets and financial liabilities. However, it is not practicable to provide a reasonable estimate of that effect until a detailed review has been completed.

Management believes that the application of other new and revised IFRSs will not have a material impact on the financial statements.

4. Summary of Significant Accounting Policies

Cash and cash equivalents

Cash and cash equivalents are assets, which can be converted into cash within a day and consist of cash on hand and current bank account balances of the Company, and other short-term highly liquid investments with original maturities of three months or less. Amounts, which relate to funds that are of a restricted nature, are excluded from cash and cash equivalents.

Financial assets

The Company classifies its financial assets in the following categories:

- loans and receivables (this category includes loans to customers and receivables);
- financial assets available for sale.

The Company determines the classification of its financial assets at initial recognition. Classification of financial assets at initial recognition depends on the purpose for which they were acquired and their characteristics.

Initial recognition of financial instruments

The Company recognizes financial assets and financial liabilities in its statement of financial position when it becomes a party to the contractual obligation of the financial instrument. Regular way purchases and sales of the financial assets and liabilities are recognized using settlement date accounting.

All financial assets are initially recognized at fair value plus transaction costs that are directly attributable to acquisition or issue of the financial instrument.

Fair value measurement

The fair value of financial instruments traded on the active market as at the reporting date is determined based on the market or dealers' quotations including transaction costs.

If a quoted market price is not available, the fair value of financial assets and financial liabilities recorded in the statement of financial position is estimated on the basis of market quotations for similar financial instruments or using various valuation techniques, including mathematical models. Where mathematical models are used, inputs are based on observable market data or judgment.

Judgment is based on such considerations as the time value of money, credit risk level, volatility of the instrument, market risk level and other applicable factors.

Derecognition of financial assets

A financial asset (or, where applicable, a part of a financial asset, or part of a group of similar financial assets) is derecognized where:

- the rights to receive cash flows from the asset have expired;
- the Company has transferred its rights to receive cash flows from the asset, or retained the right to receive cash flows from the asset, but has assumed an obligation to pay them in full without material delay to a third party; and
- the Company either has transferred substantially all the risks and rewards of the asset, or has neither transferred nor retained substantially all the risks and rewards of the asset, but has transferred control of the asset. If the transferee has no practical ability to sell the asset in its entirety to an unrelated third party without needing to impose additional restrictions on the transfer, the entity has retained control.

Where the Company has transferred its rights to receive cash flows from an asset and has neither transferred nor retained substantially all the risks and rewards of the asset nor transferred control of the asset, the asset is recognized to the extent of the Company's continuing involvement in the asset. Continuing involvement that takes the form of a guarantee over the transferred asset is measured at the lower of the original carrying amount of the asset and the maximum amount of consideration that the Company could be required to repay.

Loans to customers

This category includes non-derivative financial assets with fixed or determinable payments that are not quoted in an active market, other than:

- those that the entity intends to sell immediately or in the near term, which shall be classified as held for trading;
- those that the entity upon initial recognition designates as available for sale;

- those for which the holder may not recover substantially all of its initial investment, other than because of credit deterioration, which shall be classified as available for sale.

Loans to customers are initially recorded at cost, which is the fair value of the consideration given. Subsequently, they are carried at amortized cost using the effective interest method less provision for impairment losses.

Loans to customers are recorded when cash is advanced to borrowers.

Loans to customers originated at interest rates different from market rates are remeasured at origination to their fair values, being future interest payments and principal repayment(s) discounted at market interest rates for similar loans. The difference between the fair value and the nominal value at origination is credited or charged to the statement of comprehensive income as gains /losses on origination of assets at rates above/below market. Subsequently, the carrying amount of such loans is adjusted for amortization and the related gains/losses are recorded within the statement of comprehensive income using the effective interest method.

Financial assets available for sale

Financial assets available for sale are non-derivative financial assets. This category includes investment securities which the Company 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. The Company classifies investments as available for sale at the time of purchase.

Financial assets available for sale are initially recognized at fair value plus transaction costs that are directly attributable to acquisition or issue of the financial asset. After initial recognition financial assets are measured at cost.

Dividends received on equity investments available for sale are recorded in the statement of comprehensive income as other operating income when the Company's right to receive dividends is established and dividends are likely to be received.

Impairment of financial assets

The Company assesses on each closing date whether there is any objective evidence that the value of a financial asset item or group of items has been impaired. Impairment losses are recognized in the statement of comprehensive income as they are incurred as a result of one or more events that occurred after the initial recognition of the asset (a "loss event") and has 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 Company determines that no objective evidence of impairment exists for an individually assessed financial asset, it includes the asset in a group of financial assets with similar credit risk characteristics and collectively assesses them for impairment.

Impairment of loans to customers

For loans to customers carried at amortized cost, the Company first assesses whether objective evidence of impairment exists individually for financial assets that are individually significant or collectively for financial assets that are not individually significant.

Objective evidence that loans to customers are impaired includes observable data about the following events in respect of individually significant financial assets:

- default in any payments due;
- significant financial difficulty of the borrower supported by financial information at the Company's disposal;
- it becoming probable that the borrower will enter bankruptcy or other financial reorganization;
- worsening national or local economic environment affecting the borrower;
- breach of contract, such as a default or delinquency in interest or principal payments;
- the lender, for economic or legal reasons relating to the borrower's financial difficulty, granting to the borrower a concession that the lender would not otherwise consider.

Assets that are individually assessed for impairment and for which an impairment loss is recognized are not included in a collective assessment of impairment.

If the Company determines that no objective evidence of impairment exists for an individually assessed financial asset, it includes the asset in a group of financial assets with similar credit risk characteristics and collectively assesses them for impairment.

For the purpose of a collective evaluation of impairment, financial assets are grouped on the basis of similar credit risk characteristics such as asset type, industry, geographical location, collateral type, payment status and other relevant factors. The characteristics chosen are relevant to the estimation of future cash flows for groups of such assets by being indicative of the borrowers' ability to pay all amounts due according to the contractual terms of the assets being evaluated.

The main criterion used for determining objective evidence of loss from impairment of due from other banks and loans to customers representing collectively measured financial assets is availability of observable data indicating that there is a measurable decrease in the estimated future cash flows from a group of financial assets since the initial recognition of those assets, although the decrease cannot yet be identified with the individual financial assets in the group.

Such information may include adverse changes in the payment status of borrowers in the group (for example, an increased number of delayed payments), national or local economic conditions that correlate with defaults on the assets in the group (for example, an increase in the unemployment rate in the geographical area of the borrowers, a decrease in property prices in the relevant area, a decrease in oil prices, or adverse changes in industry conditions that affect the borrowers in the group).

If there is objective evidence that an impairment loss has been incurred, the amount of the loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows. The carrying amount of the asset is reduced through the use of the provision account and the amount of the loss is recognized in the statement of comprehensive income.

The present value of the estimated future cash flows is discounted at the financial asset's original effective interest rate. If a loan has variable interest rate, the discount rate for measuring any impairment loss is the current effective interest rate. The calculation of the present value of the estimated future cash flows of a collateralized financial asset reflects the cash flows that may result from foreclosure less costs for obtaining and selling the collateral.

Loans that have not been individually assessed are then included in the group of loans that are collectively assessed for impairment. The collectively assessed loans are grouped based on similar credit risk characteristics and on their past-due status and assessed accordingly. The collectively assessment methodology strives to ensure the provision for impairment reflects the loss events that have occurred, but have not yet been identified on an individual loan basis.

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 recognized (such as improvement in the debtor's financial position), the previously recognized impairment loss is reversed by adjusting the allowance account in the statement of comprehensive income.

Non-performing loans are written off by the Supervisory Council in accordance with applicable legislation after confirming that all policy-required collection efforts have been diligently pursued by management.

In case of a write-off of the uncollectible loan and relating interest, the Company shall take necessary and adequate steps, envisaged by law, custom of business turnover or agreement, to collect this outstanding loan.

Impairment of financial assets available for sale

The Company assesses at each reporting date whether there is objective evidence that an investment or a group of investments available for sale is impaired.

In case of equity investments classified as available for sale, objective evidence would include a significant or prolonged decline in the fair value of the equity security below its cost. This determination of what is significant and/or prolonged requires judgment. The Company also assesses other factors such as volatility of price per share. Cumulative impairment loss measured as a difference between the acquisition cost and the current fair value, less any impairment loss on that asset previously recognized through the profit and loss accounts, is transferred from other comprehensive income to the profit and loss accounts.

Impairment losses on equity instruments are not reversed through the profit and loss account: increases in the fair value after impairment are recognized directly in other comprehensive income.

Financial liabilities

Financial liabilities are classified as financial liabilities carried at amortized cost.

Initially, a financial liability shall be measured by the Company at its fair value plus transaction costs that are directly attributable to the acquisition or issue of the financial liability.

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

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

Financial liabilities carried at amortized cost

Financial liabilities carried at amortized cost payables to suppliers, taxes payable, and borrowed funds. Borrowed funds include regular and subordinated loans received by the Company and are recorded as cash is advanced to the Company.

Offsetting of financial instruments

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

Property and equipment

Property and equipment are stated at cost less accumulated depreciation and impairment provision.

At each reporting date the Company assesses whether there is any indication of impairment of property and equipment. If such indication exists, the Company 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. Where the carrying amount of premises and equipment is greater than their estimated recoverable amount, it is written down to their recoverable amount and the difference is charged as impairment loss to the statement of comprehensive income.

Gains and losses on disposal of premises and equipment are determined by reference to their carrying amount and recorded as operating expenses in the statement of comprehensive income.

Repairs and maintenance are charged to the statement of comprehensive income when the expense is incurred.

Depreciation

Depreciation of premises and equipment commences from the date the assets are ready for use. Depreciation is charged on a straight line basis over the estimated useful lives of the assets:

- Furniture and fixtures - 5 years;
- Computers equipment - 4 years;
- Motor vehicles - 4 years.

The residual value of an asset is the estimated amount that the Company 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 each reporting date.

Intangible assets acquired separately

Intangible assets with finite useful lives that are acquired separately are carried at cost less accumulated amortization and accumulated impairment losses. Amortization is recognized on a straight-line basis over their estimated useful lives. The estimated useful life and amortization method are reviewed at the end of each reporting period, with the effect of any changes in estimate being accounted for on a prospective basis. Intangible assets with indefinite useful lives that are acquired separately are carried at cost less accumulated impairment losses.

Operating lease - the Company as a lessee

Leases of property under which the risks and rewards of ownership are effectively retained with the lessor are classified as operating leases. Lease payments under operating lease are recognized as expenses on a straight-line basis over the lease term and included into operating expenses in the statement of comprehensive income.

Share capital

Share capital is recorded at its amount indicated in the Company's charter in accordance with statutory rules.

Dividends

The policy of the Company is reinvesting all retained earnings in increasing operations. No dividends are declared or distributed.

Contingent assets and liabilities

Contingent assets are not recognized in the statement of financial position but disclosed in the financial statements when an inflow of economic benefits is probable. Contingent liabilities are not recognized in the statement of financial position but disclosed in the financial statements unless the possibility of any outflow in settlement is remote.

Taxation

The income tax charge comprises current tax and deferred tax and is recorded in the statement of comprehensive income. Income tax expense is recorded in the financial statements in accordance with the applicable legislation of Azerbaijan. Current tax is calculated on the basis of the taxable profit for the year, using the tax rates enacted during the reporting period.

Current tax is the amount expected to be paid to or recovered from the taxation authorities in respect of taxable profits or losses for the current or prior periods. Tax amounts are based on estimates if financial statements are authorized prior to filing relevant tax returns.

Deferred income tax is provided using the balance sheet liability method for tax loss carryforwards and temporary differences arising between the tax bases of assets and liabilities and their carrying amounts for financial reporting purposes. Deferred tax balances are measured at tax rates enacted or substantively enacted at the reporting date which are expected to apply to the period when the temporary differences will reverse or the tax loss carryforwards will be utilized. Deferred tax assets and liabilities are offset if there is a legally enforceable right to set off current tax assets against current tax liabilities. Deferred tax assets for deductible temporary differences and tax loss carryforwards are recorded to the extent that it is probable that future taxable profit will be available against which the deductions can be utilized. Judgment is required to determine the amount of deferred tax assets that may be recognized in financial statements based on probable periods and amounts of future taxable profits and future tax planning strategies.

Azerbaijan also has various other taxes, which are assessed on the Company's activities. These taxes are recorded within operating expenses in the statement of comprehensive income.

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. The effective interest method is a method of calculating the amortized cost of a financial asset or a financial liability and of allocating the interest income or interest expense over the relevant period. The effective interest rate is the rate that exactly discounts estimated future cash payments or receipts through the expected life of the financial instrument to the net carrying amount of the financial asset or financial liability. When calculating the effective interest rate, the Company estimates cash flows considering all contractual terms of the financial instrument, but does not consider future credit losses. The calculation includes all commissions and fees paid or received by the parties to the contract that are an integral part of the effective interest rate, transaction costs, and all other premiums or discounts.

Fees, commissions and other income and expense items are recorded on an accrual basis after the service is provided. Loan origination fees for loans that are not yet provided, but are probable of being drawn down, are recognized within other assets and are subsequently taken into account in calculation of effective yield on the loan.

Employee benefits and social insurance contributions

The Company pays social security contributions in the territory of Azerbaijan. These contributions are recorded on an accrual basis. The Company does not have pension arrangements separate from the state pension system of Azerbaijan. Wages, salaries, contributions to the State Social Protection Fund, paid annual leaves and paid sick leaves, bonuses and non-monetary benefits are accrued as the Company's employees render the related service.

Foreign currency

Foreign currency transactions are translated into the functional currency at the Central Bank of the Republic of Azerbaijan exchange rate in effect at the transaction date. Monetary assets and liabilities denominated in foreign currencies are translated into the functional currency at the Central Bank's exchange rate ruling at the reporting date. Foreign exchange gains and losses resulting from revaluation of transactions in foreign currency are recorded in the statement of comprehensive income within foreign exchange translation gains less losses. Non-monetary items denominated in foreign currency and carried at cost are restated at the Central Bank's exchange rate in effect at the transaction date. Non-monetary items denominated in foreign currency and carried at fair value are restated at the exchange rate in effect at the date the fair value is determined.

Gains and losses on purchase and sale of foreign currency are determined as the difference between the selling price and the carrying amount at the date of the transaction.

5. Critical Accounting Estimates and Judgements

The Company makes certain estimates and assumptions regarding the future. Estimates and judgements are continually evaluated based on historical experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances. In the future, actual experience may differ from these estimates and assumptions. The estimates and assumptions that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year are discussed below.

Provision for impairment losses on loans to customers

The specific counterparty component of the total allowances for impairment applies to claims evaluated individually for impairment and is based upon management's best estimate of the present value of the cash flows that are expected to be received. In estimating these cash flows, management makes judgments about a counterparty's financial situation and the net realizable value of any underlying collateral. Each impaired asset is assessed on its merits, and the workout strategy and estimate of cash flows considered recoverable are independently approved by the Credit Risk function.

Collectively assessed impairment allowances cover credit losses inherent in portfolios of claims with similar economic characteristics when there is objective evidence to suggest that they contain impaired claims, but the individual impaired items cannot yet be identified. A component of collectively assessed allowances is for country risks. In assessing the need for collective loan credit loss allowances, management considers factors such as credit quality, portfolio size, concentrations, and economic factors. In order to estimate the required allowance, assumptions are made to define the way inherent losses are modeled and to determine the required input parameters, based on historical experience and current economic conditions. The accuracy of the allowances depends on how well these estimated future cash flows for specific counterparty allowances are forecast and the model assumptions and parameters used in determining collective allowances.

Fair value of financial instruments

The Company determines the fair value of financial instruments that are not quoted, using valuation techniques. Those techniques are significantly affected by the assumptions used, including discount rates and estimates of future cash flows. In that regard, the derived fair value estimates cannot always be substantiated by comparison with independent markets and, in many cases, may not be capable of being realized immediately.

The methods and assumptions applied, and the valuation techniques used, are disclosed in note 20.

Useful lives of property and equipment

As described in the 4 above, the Company reviews the estimated useful lives of property, plant and equipment at the end of each reporting period.

Legal proceedings

In accordance with IFRSs the Company recognises a provision where there is a present obligation from a past event, a transfer of economic benefits is probable and the amount of costs of the transfer can be estimated reliably. In instances where the criteria are not met, a contingent liability may be disclosed in the notes to the financial statements. Obligations arising in respect of contingent liabilities that have been disclosed, or those which are not currently recognised or disclosed in the financial statements, could have a material effect on the Company's financial position. Application of these accounting principles to legal cases requires the Company's management to make determinations about various factual and legal matters beyond its control. The Company reviews outstanding legal cases following developments in the legal proceedings and at each reporting date, in order to assess the need for provisions and disclosures in its financial statements. Among the factors considered in making decisions on provisions are the nature of litigation, claim or assessment, the legal process and potential level of damages in the jurisdiction in which the litigation, claim or assessment has been brought, the progress of the case (including the progress after the date of the financial statements but before those statements are issued), the opinions or views of legal advisers, experience on similar cases and any decision of the Company's management as to how it will respond to the litigation, claim or assessment.

Income taxes

The Company is subject to income tax and significant judgement is required in determining the provision for income taxes. During the ordinary course of business, there are transactions and calculations for which the ultimate tax determination is uncertain. As a result, the Company recognizes tax liabilities based on estimates of whether additional taxes and interest will be due. These tax liabilities are recognised when, despite the Company's belief that its tax return positions are supportable, the Company believes that certain positions are likely to be challenged and may not be fully sustained upon review by tax authorities. The Company believes that its accruals for tax liabilities are adequate for all open audit years based on its assessment of many factors including past experience and interpretations of tax law. This assessment relies on estimates and assumptions and may involve a series of complex judgments about future events. To the extent that the final tax outcome of these matters is different than the amounts recorded, such differences will impact income tax expense in the period in which such determination is made.

6. Cash and Cash Equivalents

	2010	2009
Cash on hand	3,178	3,139
Cash balances with banks	15,494	367,117
Total cash and cash equivalents	18,672	370,256

7. Loans to Customers

Loans to customers comprise:

	2010	2009
Loans to customers - principal	1,796,397	2,080,415
Accrued interest on loans to customers	44,131	44,273
Less provision for impairment losses on loans to customers	(37,833)	(12,672)
Total loans to customers	1,802,695	2,112,016

As at 31 December 2010, accrued interest income on impaired loans to customers amounted to nil (2009: nil).

Movements in the provision for impairment of loans to customers during 2010 and 2009 are as follows:

	2010	2009
Provision for impairment losses on loans to customers as at 1 January	12,672	39,698
Provision/(recovery of provision) for impairment of loans to customers	25,160	(26,984)
Write-offs	-	(42)
Provision for impairment losses on loans to customers as at 31 December	37,833	12,672

Economic sector risk concentrations within the Company's loan portfolio are as follows:

	2010	2009
Livestock	714,884	899,758
Retail	662,079	753,991
Consumer	161,361	156,440
Services	208,780	202,583
Production	51,636	65,599
Agriculture	26,125	21,220
Other	15,663	25,097
Less provision for impairment losses on loans to customers	(37,833)	(12,672)
Total loans to customers	1,802,695	2,112,016

Azerbaijan regional concentrations within the Company's loan portfolio are as follows:

	2010	2009
Barda	878,176	1,006,633
Ganja	747,683	886,575
Goychay	214,669	231,480
Less provision for impairment losses on loans to customers	(37,833)	(12,672)
Total loans to customers	1,802,695	2,112,016

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Loan models concentrations within the Company's loan portfolio are as follows:

	2010	2009
Zirve	1,151,196	1,134,820
Individual	108,064	112,466
Business	487,356	751,605
Livestock	43,603	81,823
Employees	50,309	43,974
Less provision for impairment losses on loans to customers	(37,833)	(12,672)
Total loans to customers	1,802,695	2,112,016

The Company does not have any standalone borrower a group of related borrowers with the total amount of substantial nature to the whole loan portfolio.

The Company does not hold any collateral as a security for its loan assets.

8. Property and Equipment

	Furniture and fixtures	Computer equipment	Vehicles	Total
Cost				
31 December 2008	18,582	18,915	14,185	51,682
Additions	7,932	6,816	30,767	45,515
Disposal	-	-	(3,628)	(3,628)
31 December 2009	26,514	25,731	41,324	93,569
Additions	2,916	2,008	-	4,924
Disposal	-	-	-	-
31 December 2010	29,430	27,739	41,324	98,493
Accumulated depreciation				
31 December 2008	3,760	9,050	4,489	17,299
Charge for the year	6,006	6,936	16,769	29,711
Disposal	-	-	(3,628)	(3,628)
31 December 2009	9,766	15,986	17,630	43,382
Charge for the year	5,177	3,811	7,746	16,734
Disposal	-	-	-	-
31 December 2010	14,943	19,797	25,376	60,116
Net book value				
31 December 2009	16,748	9,745	23,694	50,187
31 December 2010	14,487	7,942	15,948	38,377

9. Income Taxes

Differences between IFRS and statutory taxation regulations of Azerbaijan give rise to certain temporary differences between the carrying value of certain assets and liabilities for financial reporting purposes and for the Company's profit tax purposes. Temporary differences as at 31 December 2010 and 2009 comprise:

	2010	2009
Deductible temporary differences		
Loans to customers	37,833	-
Borrowings	-	29,005
Property and equipment	9,006	4,105
Other liabilities	6,982	-
Total deductible temporary differences	53,821	33,110
Taxable temporary differences		
Loans to customers	-	44,273
Other assets	-	784
Total taxable temporary differences	-	45,057
Net deferred deductible/(taxable) temporary differences	53,821	(11,947)
Net deferred tax asset/(liability) at the statutory tax rate (20%)	10,764	(2,389)

Relationship between tax expenses and accounting profit for the years ended 31 December 2010 and 2009 are explained as follows:

	2010	2009
Profit before income taxes	238,241	225,672
Tax at the statutory tax rate (20%)	47,648	49,648
Tax effect of permanent differences	(9,448)	3,914
Income tax expense	38,200	53,562
Current income tax expense	51,353	50,302
Deferred income tax (recovery)/expense	(13,153)	3,260
Income tax expense	38,200	53,562
	2010	2009
Deferred income tax asset/(liability) as at 1 January	(2,389)	871
Deferred income tax recovery/(expense)	13,153	(3,260)
Deferred income tax asset/(liability) as at 31 December	10,764	(2,389)

Net deferred tax assets represent the amounts of income tax that may be offset against future income taxes and are reported as deferred tax assets in the statement of financial position.

The Tax Audit Department under the Taxes Ministry of the Republic of Azerbaijan did the onsite tax audit of the Company for the period covering August 2006 to July 2009. The tax inspectors proposed charging financial sanction to the Company totalling AZN 255,649 and this amount was withheld from the Company's bank account. The Company disagreed with the decision and on 12 July 2010 applied to Baku Administrative-Economic Court # 2, which on the 5 April 2011 partly satisfied the appeal and issued decision to return AZN 107,116 to the Company.

10. Other Assets

	2010	2009
Receivables on penalties	3,016	783
Prepayments	921	3,865
Prepayments for taxes other than income taxes	-	4,514
Total other assets	3,937	9,162

11. Borrowings

	2010	2009
Triple Jump	542,500	717,520
Microcredit Enterprise	239,370	240,930
Oiko credit	116,056	233,628
Qafqaz kredit	-	75,250
Accrued interest on borrowings	20,328	29,005
Total borrowings	918,254	1,296,333

12. Other Liabilities

	2010	2009
Payable to employees	14,218	-
Taxes payable other than income tax	-	396
Other	-	16,139
Total other liabilities	14,218	16,535

13. Share Capital

The total contributed share capital of the Company USD 33,000 USD (AZN 32,229) was contributed in two forms: USD 8,414 (AZN 8,248) in cash and USD 24,586 (AZN 23,981) in form of property and equipment transferred from the shareholder at its net book value at the date of contribution. Share capital consists of two equal shares.

14. Accumulated Grants

Accumulated grants represent cumulative donation received by the Company from its donors.

On the 9 March 2010 the Company signed agreements with NBCO "Avrasiya-kredit" LLC, NBCO "Dayag-kredit" LLC and NBCO "Komek-kredit" LLC, national microfinance institutions. Under terms and conditions of these agreements the Company committed to make one-off financial support of AZN 80,000 to each of these entities. Funds were actually transferred to recipients in March 2010.

15. Interest Income and Expense

	2010	2009
Interest income		
Interest income on loans to customers	1,135,263	1,107,383
Total interest income	1,135,263	1,107,383
Interest expense		
Triple Jump	128,528	63,816
Microcredit Enterprise	28,205	17,843
Oikocredit	24,020	35,493
Qafqaz Kredit	3,758	13,556
Blue Orchard	-	12,299
Total interest expense	184,511	143,007
Net interest income	950,752	964,376

16. Operating Expenses

	2010	2009
Salaries and related taxes	473,992	554,633
Rent expense	43,340	32,230
Payments to hired drivers	69,989	57,640
Depreciation charge	16,734	29,711
Professional services fees	20,770	15,596
Office expenses	14,614	16,702
Rating expenses	-	12,833
Travel expenses	18,343	10,755
Utilities	3,818	8,240
Membership dues	2,131	2,093
Vehicle costs	9,237	1,715
Bank charges	11,917	17,785
Training expenses	2,312	-
Net (gain)/loss on foreign exchange operations	(1,359)	6,309
Other expenses	1,516	3,094
Total operating expenses	687,354	769,336

17. Risk Management

Management of risk is fundamental to the Company's business and is an essential element of the Company's operations. The main financial risks inherent to the Company's operations are those related to credit, liquidity and market movements in interest and foreign exchange rates. A summary description of the Company's risk management policies in relation to those risks follows.

The Supervisory Board is ultimately responsible for identifying and controlling risks; however, there are separate independent bodies responsible for managing and monitoring risks.

Supervisory Council

The Supervisory Council is responsible for the overall risk management approach and for approving the risk strategies and principles. Twice a year the Supervisory Council examines reports related to risk issues presented by the Chief Accountant and follows measures undertaken by the management to resolve discovered issues. The Supervisory Council is also involved in discussion of findings discovered by external auditors.

Management Committee

The Management Committee has the responsibility to monitor the overall risk process within the Company. However, in the management the main responsible person for risk management is Chief Executive Officer, whereas Chief Accountant is responsible for the preparation of risk management report.

Audit Commission

The Audit Commission is in charge of the overall risk management approach.

Finance Department

Finance department is responsible for day to day management of assets and liabilities of the Company, computation and planning of liquidity position of the Company, redistribution of cash and cash equivalents between operating sites of the Company. Finance department controls application of limits and liquidity ratios, and liquidity risk optimization.

Internal Audit

Internal audit of the Company is performed by a compliance manager and the manager implements an independent review of risk management process, informs management of the Company about the revealed shortcomings and gives appropriate recommendations concerning improvement of risk management process.

Risk measurement and reporting systems

Choice of risk management method depends on risk factors which are observed to determine relative importance or probability of risk occurrence which may affect adversely financial position of the Company. Therefore the Company analyzes and measures not only each risk separately, but also determines the level of cumulative risks. Thus, for each kind of risk following methods of risk measurement are applied:

- interest rate risk - maturity and interest rate gap analysis of assets and liabilities,
- liquidity risk - gap analysis of payments in national and foreign currencies; analysis of liquidity ratios, determination of liquidity reserve;
- currency risk - gap analysis of payments in foreign currency; analysis of currency position;
- credit risk - analysis of a credit portfolio and credit risk ratios;
- operational risk - for all operations having impact on the Company's financial position systems assuring separation of activities (such as initiation, execution and control) necessary for the finalization of operations have been implemented;
- influence of financial crisis - analysis of regional and international process.

Risk measurement methods reflect expected loss which the Company will probably bear when performing its activities. Every month based on the analysis of separate risks Finance Department prepares conclusion concerning the current state of the risk and main factors deteriorating or improving it.

The risk management function within the Company is carried out in respect of financial risks (credit, market, currency, liquidity and interest rate), operational and legal risks. The primary objectives of the financial risk management function are to establish risk limits, and then ensure that exposure to risks stays within these limits. The assessment of exposure to risks also serves as a basis for optimal distribution of risk-adjusted capital, transaction pricing and business performance assessment. The operational and legal risk management functions are intended to ensure proper functioning of internal policies and procedures to minimise operational and legal risks.

Industry risk. Industry risk is a possibility of incurring losses that may worsen the Company's financial condition due to concentration of operations in specific economic sector.

Credit risk. The Company takes on exposure to credit risk which is the risk that a counterparty will be unable to pay amounts in full when due. The Company controls the credit risk it undertakes by placing limits on the amount of risk accepted in relation to one borrower, or group of related borrowers. Such risks are monitored by the Company on a regular basis, the limits being subject to an annual or more frequent review. Limits on the level of credit risk by product, borrower or group of borrowers are approved by the Company's Executive Board.

The exposure to any one borrower including banks and broker companies is further restricted by sub-limits covering on- and off-balance sheet exposures. Actual exposures are monitored against limits daily.

Exposure to credit risk is managed through regular analysis of the ability of borrowers and potential borrowers to meet interest and principal repayment obligations and by changing these lending limits where appropriate. Exposure to credit risk is also managed by obtaining property and securities collateral and corporate and personal guarantees.

The Company's maximum exposure to credit risk is primarily reflected in the carrying value of financial assets in the statement of financial position. The impact of possible netting of assets and liabilities to reduce potential credit exposure is not significant.

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 Company uses the same credit policies in making contingent obligations as it does for on-balance sheet financial instruments through established credit approvals, risk control limits and monitoring procedure.

The Company performs the loan maturity analysis and subsequent monitoring of overdue balances. Therefore, the management provides data on overdue maturities and other information on credit risk.

The Company is exposed to early redemption risk as a result of lending at fixed or variable interest rates. The financial result and the Company's equity for the current year and at the current reporting date would not greatly depend on the rate fluctuations in case of early redemption because such loans are carried at amortised cost whereas the amount to be early redeemed corresponds or nearly corresponds to the amortised cost of loans to customers.

Market risk. The Company takes on exposure to market risks. Market risks arise from open positions in interest rate, currency and equity products, all of which are exposed to general and specific market movements. The management sets acceptable risk limits and monitors them on a regular basis. However, the use of this approach does not prevent losses beyond these limits in the event of more significant market movements.

The objective of market risk management is to keep the exposure to market risk within the acceptable limits assuring optimal yields for accepted risk.

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

	Azerbaijan	OECD	Total
Assets			
Cash and cash equivalents	18,672	-	18,672
Loans to customers	1,802,695	-	1,802,695
Property and equipment	38,377	-	38,377
Deferred income tax assets	10,764	-	10,764
Receivable from the Ministry of Taxes	107,116	-	107,116
Other assets	3,937	-	3,937
Total assets	1,981,561	-	1,981,561
Liabilities			
Borrowings	-	918,254	918,254
Current income tax liabilities	27,834	-	27,834
Other liabilities	14,218	-	14,218
Total liabilities	42,052	918,254	960,306
Net balance sheet position	1,939,509	(918,254)	1,021,255

The geographical analysis of the Company's assets and liabilities as at 31 December 2009 is set out below:

	Azerbaijan	OECD	Total
Assets			
Cash and cash equivalents	370,256	-	370,256
Loans to customers	2,112,016	-	2,112,016
Property and equipment	50,187	-	50,187
Deferred income tax assets	-	-	-
Receivable from the Ministry of Taxes	-	-	-
Other assets	9,162	-	9,162
Total assets	2,541,621	-	2,541,621
Liabilities			
Borrowings	76,325	1,220,008	1,296,333
Current income tax liabilities	16,617	-	16,617
Deferred income tax liabilities	2,389	-	2,389
Other liabilities	16,535	-	16,535
Total liabilities	111,866	1,220,008	1,331,874
Net balance sheet position	2,429,755	(1,220,008)	1,209,747

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Currency risk. The Company takes on exposure to effects of fluctuations in the foreign currency exchange rates on its financial position and cash flows. The management defines limits on the level of exposure by currency and in total, which are monitored periodically.

The table below summarises the Company's exposure to foreign currency exchange rate risk as at 31 December 2010.

	AZN	USD	Total
Assets			
Cash and cash equivalents	18,672	-	18,672
Loans to customers	1,802,695	-	1,802,695
Property and equipment	38,377	-	38,377
Deferred income tax assets	10,764	-	10,764
Receivable from the Ministry of Taxes	107,116	-	107,116
Other assets	3,937	-	3,937
Total assets	1,981,561	-	1,981,561
Liabilities			
Borrowings	559,360	358,894	918,254
Current income tax liabilities	27,834	-	27,834
Deferred income tax liabilities	-	-	-
Other liabilities	14,218	-	14,218
Total liabilities	601,412	358,894	960,306
Net balance sheet position	1,380,149	(358,894)	1,021,255

As at 31 December 2009, the Company had the following positions in currencies:

	AZN	USD	Total
Assets			
Cash and cash equivalents	370,256	-	370,256
Loans to customers	2,112,016	-	2,112,016
Property and equipment	50,187	-	50,187
Deferred income tax assets	-	-	-
Receivable from the Ministry of Taxes	-	-	-
Other assets	9,162	-	9,162
Total assets	2,541,621	-	2,541,621
Liabilities			
Borrowings	816,309	480,024	1,296,333
Current income tax liabilities	16,617	-	16,617
Deferred income tax liabilities	2,389	-	2,389
Other liabilities	16,535	-	16,535
Total liabilities	851,850	480,024	1,331,874
Net balance sheet position	1,689,771	(480,024)	1,209,747

The Company issued loans and bears expenses in currencies other than its functional currency. Depending on the revenue stream of the borrower, the appreciation of the currencies against the US dollar may adversely affect the borrowers' repayment ability and therefore increases the likelihood of future loan losses.

The table below shows the change in the financial result and comprehensive income due to possible fluctuations of exchange rates used as at the reporting date if all other conditions remain unchanged. Reasonably expected exchange rate changes for each currency were projected on the basis of maximal exchange rate fluctuations in December 2010 and 2009.

	2010		2009	
	USD appreciated by 10%	USD depreciated by 10%	USD appreciated by 10%	USD depreciated by 10%
Impact on profit or loss	(35,889)	35,889	(48,002)	48,002
Impact on equity	(35,889)	35,889	(48,002)	48,002

The risk was calculated only for cash balances in currencies other than the Company's functional currency.

Liquidity risk. Liquidity risk is defined as the risk when the maturity of assets and liabilities does not match. The Company is exposed to risk via scheduled calls from lenders on its available cash resources. The Company does not accumulate cash resources to meet calls on all probable liabilities mentioned, as based on the existing practice, it is possible to forecast with a sufficient degree of certainty the required level of cash funds necessary to meet the above obligations.

The Company is keen on maintaining stable financing predominantly consisting of borrowings and also on investing funds in loan asset portfolios to be able to meet unexpected liquidity needs quickly and unhampered.

To manage its liquidity, the Company is required to analyse the level of liquid assets needed to settle the liabilities on their maturity by providing access to various sources of financing, drawing up plans to solve the problems with financing and exercising control over compliance of the liquidity ratios with the laws and regulations.

The management receives information about their financial assets and liabilities and promptly manages the Company's resources with regard for the asset and liabilities management decisions, ensures solvency and liquidity of the Company by optimising cash flows and payment calendar for efficient use of cash funds.

The Management regularly monitors the liquidity position and performs periodic liquidity forecasts under a several of scenarios covering both normal and more severe market conditions.

The table below shows the liabilities as at 31 December 2010 by their remaining contractual maturity. The amounts in the table represent contractual undiscounted cash flows. These undiscounted cash flows differ from the amounts recorded in the statement of financial position which are based on discounted cash flows.

In those cases when the amount to be paid is not fixed, the amount in the table is determined on the basis of conditions prevailing at the reporting date. Foreign currency payments are translated using the spot exchange rates effective at the reporting date.

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The table below shows the undiscounted maturity analysis of financial assets and financial liabilities as at 31 December 2010:

	On demand and less than 1 month	From 1 month to 3 months	From 3 months to 1 year	From 1 year to 5 years	Total
Financial assets					
Cash and cash equivalents	3,937	-	-	-	3,937
Loans to customers	363,965	609,712	1,160,738	76,112	2,210,527
Receivable from the Ministry of Taxes	-	-	107,116	-	107,116
Other assets	-	-	3,937	-	3,937
Total financial assets	367,902	609,712	1,271,791	76,112	2,325,517
Liabilities					
Borrowings	-	50,707	515,308	572,920	1,138,935
Current income tax liabilities	-	27,834	-	-	27,834
Other liabilities	-	-	14,218	-	14,218
Total liabilities	-	78,541	529,526	572,920	1,180,987
Net liquidity gap	367,902	531,171	742,265	(496,808)	1,144,530
Cumulative liquidity gap	367,902	899,073	1,641,338	1,144,530	

The table below shows the undiscounted maturity analysis of financial assets and financial liabilities as at 31 December 2009:

	On demand and less than 1 month	From 1 month to 3 months	From 3 months to 1 year	From 1 year to 5 years	Total
Assets					
Cash and cash equivalents	370,256	-	-	-	370,256
Loans to customers	458,047	759,318	1,372,492	29,375	2,619,232
Other assets	-	-	9,162	-	9,162
Total assets	828,303	759,318	1,381,654	29,375	2,998,650
Liabilities					
Borrowings	40,696	93,829	425,524	1,117,210	1,677,259
Current income tax liabilities	-	16,617	-	-	16,617
Other liabilities	-	-	16,535	-	16,535
Total liabilities	40,696	110,446	442,059	1,117,210	1,710,411
Net liquidity gap	787,607	648,872	939,595	(1,087,835)	1,288,239
Cumulative liquidity gap	787,607	1,436,479	2,376,074	1,288,239	

In the opinion of the Company's management, the matching and/or controlled mismatching of the maturities and interest rates of assets and liabilities is fundamental for successful management of the Company. It is unusual for the lending institutions 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 Company and its exposure to changes in interest and exchange rates.

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Interest rate risk. The Company takes on exposure to the effects of fluctuations in 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.

The Company is exposed to interest rate risk, principally as a result of lending at fixed interest rates, in amounts and for periods, which differ from those of term borrowings at fixed interest rates. In practice, interest rates are generally fixed. Also, interest rates fixed contractually on both assets and liabilities are usually renegotiated to reflect current market conditions.

The Management sets limits on the level of mismatch of interest rate re-pricing that may be undertaken, which is monitored regularly. In the absence of any available hedging instruments, the Company normally seeks to match its interest rate positions.

The table below summarises the Company's exposure to interest rate risks as at 31 December 2010. Included in the table are the Company's financial assets and liabilities at carrying amounts, categorised by the earlier of contractual re-pricing or maturity dates.

	On demand and less than 1 month	From 1 month to 3 months	From 3 months to 1 year	From 1 year to 5 years	Non- interest bearing	Total
Financial assets						
Cash and cash equivalents	18,672	-	-	-	-	18,672
Loans to customers	325,520	482,074	959,206	35,895	-	1,802,695
Property and equipment	-	-	-	-	38,377	38,377
Deferred income tax	-	-	-	10,764	-	10,764
Receivable from the Ministry of Taxes	-	-	107,116	-	-	107,116
Other assets	-	-	3,937	-	-	3,937
Total assets	344,192	482,074	1,070,259	46,659	38,377	1,981,561
Liabilities						
Borrowings	-	49,056	434,718	434,480	-	918,254
Current income tax liabilities	-	27,834	-	-	-	27,834
Deferred income tax liabilities	-	-	-	-	-	-
Other liabilities	-	-	14,218	-	-	14,218
Total liabilities	-	76,890	448,936	434,480	-	960,306
Net interest sensitivity gap	344,192	405,184	621,323	(387,821)	38,377	1,021,255
Cumulative interest sensitivity gap	344,192	749,376	1,370,699	982,878	1,021,255	

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The table below summarises the Company's exposure to interest rate risks as at 31 December 2009.

	On demand and less than 1 month	From 1 month to 3 months	From 3 months to 1 year	From 1 year to 5 years	Non- interest bearing	Total
Assets						
Cash and cash equivalents	370,256	-	-	-	-	370,256
Loans to customers	368,408	600,083	1,119,541	23,984	-	2,112,016
Property and equipment	-	-	-	-	50,187	50,187
Deferred income tax assets	-	-	-	-	-	-
Other assets	-	-	9,162	-	-	9,162
Total assets	738,664	600,083	1,128,703	23,984	50,187	2,541,621
Liabilities						
Borrowings	39,755	50,704	305,631	900,243	-	1,296,333
Current income tax liabilities	-	16,617	-	-	-	16,617
Deferred income tax liabilities	-	-	-	2,389	-	2,389
Other liabilities	-	-	16,535	-	-	16,535
Total liabilities	39,755	67,321	322,166	902,632	-	1,331,874
Net interest sensitivity gap	698,909	532,762	806,537	(878,648)	50,187	1,209,747
Cumulative interest sensitivity gap	698,909	1,231,671	2,038,208	1,159,560	1,209,747	

The Company monitors financial instrument interest rates. The table below shows the interest rates on the basis of reports that were analysed by the Company's key managers as at 31 December 2010 and 2009:

	2010		2009	
	AZN	USD	AZN	USD
Assets				
Loans to customers	18-48%	-	18-48%	-
Liabilities				
Borrowings	14%	10-11%	14-15%	10-11%

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

The following table presents a sensitivity analysis of interest rate risk, which has been determined based on "reasonably possible changes in the risk variable". The level of these changes is determined by management.

	2010		2009	
	Interest rate increase by 1%	Interest rate decrease by 1%	Interest rate increase by 1%	Interest rate decrease by 1%
Assets				
Loans to customers	18,898	(18,898)	20,804	(20,804)
Liabilities				
Borrowings	(14,193)	14,193	(29,346)	29,346
Net impact on profit before income taxes	4,705	(4,705)	(8,542)	8,542
Net impact on equity	4,705	(4,705)	(8,542)	8,542

18. Capital Management

Management's focus in respect of the Company's capital management has the following objectives: ensuring the Company's ability to operate as a going concern and maintain balances and ratios in order to comply with covenants of lenders and regulatory requirements. This is exercised daily in respect of the projected and actual data and on the basis of monthly reports with the corresponding calculations that are approved by the Chief Executive Officer and Chief Accountant of the Company.

19. Contingent Liabilities

Legal issues. In the ordinary course of business, the Company is subject to legal actions and complaints. Management believes that the ultimate liability arising from such actions or complaints will not have a material adverse effect on the financial condition or the results of future operations of the Company and accordingly no provision has been made as in the management's opinion the possibility of material losses is low.

Tax legislation. Azerbaijani tax legislation is 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 Company may be challenged by the relevant authorities. Recent events in Azerbaijan have shown that the tax authorities may be taking a more assertive position in their interpretation of the legislation and assessments and it is possible that transactions and activities that have not been challenged in the past may be challenged. As a result, significant additional taxes, penalties and interest may be assessed. Fiscal periods remain open to review by the tax authorities in respect of taxes for three calendar years preceding the year of the review. Under certain circumstances reviews may cover longer periods.

As at 31 December 2010, the management believes that its interpretation of the relevant legislation is appropriate and the Company's tax, currency and customs positions will be sustained by controlling bodies.

Operating lease commitments. The Company did not enter any non-cancellable lease arrangements.

Credit related commitments. The Company does not provide its customers with credit line facilities.

20. Fair Value of Financial Instruments

The fair value is defined as the amount at which the instrument could be exchanged in a current transaction between knowledgeable willing parties on arm's length conditions, other than in a forced or liquidation sale. Quoted financial instruments in active markets provide the best evidence of fair value. As no readily available market exists for major part of the Company's financial instruments, the fair value shall be estimated based on current economic conditions and the specific risks attributable to the instrument. The estimates presented herein are not necessarily indicative of the amounts the Company could realise in a market exchange from the sale of its full holdings of a particular instrument.

Management believes that carrying values of the Company's financial assets and liabilities approximate their fair values.

The Company uses the following methods and assumptions to estimate the fair value of the following financial instruments:

Loans to customers. Loans to customers are reported net of impairment provisions. The estimated fair value of loans to customers represents the discounted amount of estimated future cash flows expected to be received. To determine fair value, expected cash flows are discounted at current market rates. The management believes that the fair values of loans to customers as at 31 December 2010 and 31 December 2009 do not materially differ from respective carrying amounts. This is primarily due to the existing practice to renegotiate interest rates to reflect current market conditions. So, interest on most balances is accrued at rates approximating market interest rates.

Borrowings. The fair value of fixed interest bearing financial liabilities carried at amortised cost is determined by comparing the market interest rates at initial recognition of these instruments with current market rates on similar financial instruments. The estimated fair value of fixed interest liabilities is based on discounted cash flows using interest rates for debt instruments with similar credit risk and maturity.

The fair value of variable rate borrowings without market quotations is based on discounted cash flows using interest rates for debt instruments with similar maturity. The estimated fair value of other borrowed funds approximates their carrying value as these instruments do not have market quotations and are attracted at floating interest rate.

21. Reconciliation of Categories of Financial Instruments to Statement of Financial Position

In accordance with IAS 39 “Financial Instruments: Recognition and Measurement” the Company classifies its financial assets in the following categories: 1) loans and receivables; 2) financial assets available for sale. In the reporting periods the Company classified all its financial assets as loans and receivables and all its financial liabilities as measured at amortised cost.

22. Related Party Transactions

For the purposes of these financial statements, parties are considered to be related if one party has the ability to control or exercise significant influence over the other party in making financial or operational decisions as defined by IAS 24 “Related Party Disclosures”. In considering each possible related party relationship, attention is directed to the economic substance of the relationship, not merely the legal form.

In the normal course of business the Company enters into transactions with its major shareholder, directors, and other related parties. These transactions include settlements, issuance of loans, trade finance and foreign currency transactions. According to the Company’s policy the terms of related party transactions are equivalent to those that prevail in arm’s length transactions.

The outstanding balances at the year end and income and expenses with related parties were as follows:

	2010		2009	
	Key management personnel	Total	Key management personnel	Total
Balances				
Loans to customers	8,737	8,737	16,615	16,615
Income				
Interest income	308	308	2,143	2,143
Expenses				
Salaries and related taxes	100,870	100,870	128,169	128,169

23. Subsequent Events

On 22 February 2011 the Company received a loan in the amount of AZN 400,000 from Grameen Credit Agricole Microfinance Foundation under the loan agreement signed on 24 December 2010. The loan bears annual interest of 11.4% and will be repaid in five equal semi-annual instalments with the first repayment scheduled for 15 October 2011. The funds will be intended solely to finance micro-credit loans.