



«F.N. AUDIT SERVICE LTD»

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Att: Mr. Bahman Askerov/Direktor
CC: Mr. Babek Shahbazov/Financial Manager

Date: 19 March, 2007

Our Ref: 9177/YT

Norwegian Microcredit LLC.
4 J. Jabbarly Street,
Baku, Azerbaijan

**MANAGEMENT REPORT ON THE RESULTS OF THE AUDIT OF THE FINANCIAL
STATEMENTS FOR THE YEAR 2006**

Dear Sirs,

According to the agreement between "F.N.Audit Servis" LTD. and Norwegian Microcredit LLC (Normicro), we have completed an audit of the financial statements of Normicro for the year 2006. Our findings are based on the information and documents provided to us by Normicro's representatives and comply with provisions of the International Accounting Standards. All the documents and information provided for our review is wholly the responsibility of Normicro.

Below are our comments for your consideration:

1. Terms of Reference

Our audit covered the following aspects of financial activities of Normicro:

- Accounting and Internal Control Systems, including internal accounting and controls procedures, documents, packages etc.
- Credit Manual and Portfolio Related policies
- Loan Portfolio and Management Information Systems, Credit transactions, including calculation of credits interests, balances, repayment schedules, credit agreements, collection of fees, principal amounts of credits, file documentations, etc.;

- Loan Loss provisions, including creation of general and special reserves;
- Cash & Bank transactions, including credit and general administration transactions, bank reconciliations etc.
- Debt - recording and classification of loans received, interest paid, etc.
- Grants - classification and use of grants received, recording etc.
- Equity, including share capital and retained earnings;
- Revenues and expenses - correctness of recording, timing, attribution, etc.
- Statutory compliance - taxes, social contributions and other statutory requirements.
- Opening balances - all the opening balances as of January 1, 2006 for the purpose of International Standards on Auditing.

2. Accounting and Internal Control Systems

During the audit we reviewed the accounting and internal control systems operating within the Organization. The systems demonstrated reliability of the information produced by them.

3. Credit Manual and Portfolio Related Policies

During the audit of credit manual and portfolio related policies we have determined that the subject manual and policies meet the requirements of CGAP standards, IAS and government rules with regards to maintenance of credit portfolio.

4. Loan Portfolio and Management Information Systems, Credit Transactions

Accounting of loan portfolio, as well as other transactions was kept using the Management Information Systems (MIS) software. The software is specially designed for credit organizations and allows to account, analyze and report properly and in a timely manner on all transactions and requirements related to customer loans, interest accruals and payments, personal information on customers, loans status, loans securities etc. The audit procedures performed by "F.N.Audit Servis" allows us to conclude that the MIS provides reliable information related to loan transactions.

Our audit of credit transactions was conducted on a sample basis. Representative sample of credits was tested in Baku, Sumgayit, Agsu and Khachmaz branches. As a result, no material mistakes were revealed in recording of credits issued to customers, credits repayments, interests calculated and received from customers, recording of fees, fines etc., filing of documents etc.

5. Loan Loss Provisions

Rules of the National bank of the Azerbaijan Republic were applied by Normicro for creation of general and special reserves. Even though the subject rules are not obligatory for non-bank credit organization, we consider the rates provided by them adequate to the level of risk borne by Normicro and would recommend to sustain risk reserves at the percentages recommended by those Rules. Considering that Normicro started provisions for general group of loans only in the year 2005 balances of the loans which were issued to clients prior to this year were not covered by the general provision.

6. Cash and Bank Transactions

During the audit of cash and bank transactions we have not revealed any material mistakes.

7. Debt (Credits Received)

During the audit of debt of the Norwegian Microcredit LLC we did not reveal any material misstatements or mistakes.

8. Grants

During the audit of the Grants we did not reveal any material misstatements or mistakes. Usage of grants received by Normicro corresponds with the purposes and classifications stated in grant agreements.

9. Equity

During the audit of equity we did not reveal any material misstatements or mistakes.

10. Revenues and Expenses

Revenues and Expenses related to credit transactions were recorded and accounted for in US Dollars, which is the primary currency credits issued to customers. All the administrative expenses were incurred in manats and transferred to US Dollars at the rate applicable at the reporting date for the purpose of the including them into the financial statements in accordance with the IAS.

11. Summary

We would like to summarize the main issues discussed in the current Report as follows:

1. We would recommend to transfer the transactions made in manats into US Dollars at the rates applicable at the dates when those transactions were made for the purpose of presentation of financial statements of the Organization in USD in accordance with IAS.

2. We would recommend to obtain recommendations of the Tax Ministry on the VAT issue. Payment of balances of Profit tax and Social Contributions to the relevant authorities is advisable.

Sincerely Yours,

Fuad E. Aliyev
Managing Partner



NORWEGIAN MICROCREDIT LLC

**FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER,
2006 and 2005 and INDEPENDENT AUDIT REPORT**



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INDEPENDENT AUDIT REPORT

To the Management of Norwegian Microcredit LLC:

We have audited the accompanying balance sheet of Norwegian Microcredit LLC as of 31 December 2006 and the related statements of income, equity and cash flows for the year end. These financial statements are the responsibility of the Norwegian Microcredit LLC's management. 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 plan and perform the audit to obtain reasonable assurance about whether the financial statements and accompanying notes are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the financial statements give a true and fair view of the financial position of Norwegian Microcredit LLC as of 31 December 2006 and of the results of its operations and its cash flows for the year ended in accordance with International Accounting Standards.

March 19, 2007



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BALANCE SHEET as of 31 December 2006, 2005

(In US Dollars)

F.N.AUDIT SERVICE

CONFIDENTIAL

	NOTES	2006	2005
ASSETS			
<u>Non-Current assets</u>			
Property, plant and equipment	2c, 6, 10	87,877.28	76,918
Intangible Assets	2c, 6, 10	1,025.00	1,080
<u>Total Non-current assets</u>		<u>88,902.28</u>	<u>77,998</u>
<u>Current assets</u>			
Loans, net of allowances for losses	2b, 4	2,485,305.10	1,561,040
Other current assets	5	1,089.86	1,785
Cash and cash equivalents	3	25,415.77	109,643
<u>Total current assets</u>		<u>2,511,810.73</u>	<u>1,672,468</u>
TOTAL ASSETS		2,600,713.01	1,750,467

The notes on pages 9-16 form an integral part of these financial statements. Independent Auditor's Report is on page 3..

BALANCE SHEET as of 31 December, 2006
(In US Dollars)

	Note	2006	2005
EQUITY AND LIABILITIES			
<u>Equity & Resources</u>			
Share capital	9	5,823.96	5,525
Retained earnings	12	577,530.08	403,383
Grants received	9	861,952.43	801,036
<u>Total Equity & Resources</u>		<u>1,445,306.47</u>	<u>1,209,944</u>
<u>Non-current liabilities</u>			
Long-term credits	7	1,010,705.76	288,450
<u>Current liabilities</u>			
Short-term credits	7	37,296.30	75,000
Profit Tax	13	12,473.36	75,895
Social Protection Fund	13	85,376.50	80,837
Other current liabilities	8	5,037.44	4,135
Deferred Income	15	4,517.17	16,206
<u>Total current liabilities</u>		<u>144,700.78</u>	<u>252,073</u>

Total Liabilities	1,155,406.54	540,523
TOTAL EQUITY AND LIABILITIES	2,600,713.01	1,750,467

The notes on pages 9-16 form an integral part of these financial statements. Independent Auditor's Report is on page 3.

**INCOME STATEMENT for the year ended 31 December, 2006
(In US Dollars)**

Indicator	Note	2006	2005
<u>Interest Income</u>	10		
Interest on loans		<u>649,192.46</u>	522,078
<u>Total Interest Income</u>		<u>649,192.46</u>	<u>522,078</u>
<u>Interest Expense</u>			
Interest on credits		34,272.91	22,305
Interest on deposits			
<u>Total Interest Expense</u>		<u>34,272.91</u>	<u>22,305</u>
Net Interest Income		614,919.55	499,773
Provision for loan losses	4	24,196.53	29,196
Net interest income after provision for loan losses	10	590,723.02	470,577
Fee and commission income	10,14	71,171.06	52,906
Other operational income		10,007.08	915
Grant income	9,10	17,527.12	14,215
<u>Non-interest expense</u>			
Salaries and benefits		261,659.75	196,722
Expenses related to immovable property		26,092.48	21,662
Office rent		25,786.65	21,563
Exchange Loss	2e	35,215.39	64,578
Other expenses	11	121,144.56	57,389
<u>Total non-interest expense</u>		<u>469,898.83(434,683.44+35,215.39)</u>	<u>361,913</u>
Net Operational Income before tax		202,002.33(590,723.02+71,171.06+10,007.08-469,898.83)	176,699
Profit Tax	10	44,440.51	42,408
NET INCOME AFTER	2d, 10, 12	157,561.82	134,291

TAX

The notes on pages 9-16 form an integral part of these financial statements. Independent Auditor's Report is on page 3

STATEMENT OF CHANGES IN EQUITY as of 31 December, 2006 and 2005 (In US Dollars)

	Note	Share Capital	Retained Earnings	Grants Received	Total Equity and Resources
Balance 01.01.2005		5,175	253,999	713,654	972,828
Additions in 2005			132,241	39,215	171,456
Changes arisen from re-evaluation of currency in 2005	2e	350	17,143	48,167	65,660
Balance 01.01.2006		5,525	403,383	801,036	1,209,944
Additions in 2006	9,12		152,297.88	17,527.12	169,825
Changes arisen from re-evaluation of currency in 2006	2e	298.96	21,849.20	43,389.31	65,537.47
Balance 01.01.2007		5,823.96	577,530.08	861,952.43	1,445,306.47

The notes on pages 9-16 form an integral part of these financial statements. Independent Auditor's Report is on page 3.

CASH FLOW STATEMENT as at 31 December 2006, 2005 (In US Dollars)

Indicator	Note	2006	2005
Cash flow from operations (excluding grants)			
Net Operational Income -	2d, 12	152,297.88	132,241
Adjustments to reconcile net income with funds provided from operations:			
Increase in value of equity due to change in exchange rate US\$:AZM	2e	18998.51	17,493
Depreciation of fixed assets-	2c, 6	25,315.74	20,975
Amortization of Intangible Assets-	2c, 6	113.88	120
Changes in assets and liabilities:		(23879.96)	0
decrease (increase)in other current assets	5	792.52	1,044

Increase in Profit tax, SPF and other current liabilities-	8, 13c, 13d	(68,438.60)	62,519
Total funds provided from operating activities-		105199.97	234,392
Cash flows from investment activities			
Net increase in loan portfolio	4	(839710.81)	(311,872)
Purchase of fixed assets-	6	(32109.24)	(27,989)
Total cash used in investment activities		(871820.05)	(339,861)
Cash flows from financing activities			
Increase in short-term debt-	7	(79,062.43)	24,777
Increase in long-term-	7	743,928.16	89,021
Increase in donations and grants	9	17,527.12	87,382
Net cash flows from financing activities		682,392.85	201,180
NET INCREASE IN CASH	3	(84,227.23)	95,711
CASH AND CASH EQUIVALENTS AT THE BEGINNING OF THE YEAR	3	109,643	13,932
CASH AND CASH EQUIVALENTS AT THE END OF THE YEAR		25,415.77	109,643

The notes on pages 9-16 form an integral part of these financial statements. Independent Auditor's Report is on page 3.

1. Organization and basis of presentation

Norwegian Microcredits LLC (Normicro or the Organization), was incorporated in Azerbaijan in 2002 by a 100% owner of Normicro. In November 2006, Kolibri Kapital has taken over 100% shares of Norwegian Refugees Council.

The organization operates 3 branch offices in the Azerbaijan Republic, i.e. Baku, Khachmaz and Beylaqan branches. In its turn Khachmaz branch office operates 3 sub-offices in Khachmaz, Sumqait and Agsu cities. Normicro's primary source of revenue is derived from providing loans to refugees, internally displaced persons and other low-income groups of people.

2. Summary of significant accounting policies

The accounting and reporting policies adopted by Norwegian Microcredit LLC are in accordance with International Accounting Standards and CGAP standards. Accounting of loan and other accounting transactions is kept using the Management Information Systems (MIS) software specially designed for credit organizations, which allows to ensure reliability of the information provided.

a. Use of Estimates

The preparation of financial statements in conformity with international accounting standards requires management to make estimates and assumptions that affect reported assets and liabilities as well as reported income and expenses for each year. A material estimate that is particularly susceptible to significant change relates to the determination of provisions for loan losses.

b. Loans, loan loss allowance and interest

Since the year 2005 the Organization has changed its policy and started creating provisions for possible loan losses. As a risk portfolio to the year 2006, the % of working balances was created accordingly. The Organization estimates amounts of possible losses on loans at the reporting date to determine the provisions. There are no national regulations provided for the microfinance institutions with regards to provisions for possible losses. The Organization bases its provision for losses on the rates provided in the rules of National Bank of the Azerbaijan Republic for banks. The following percentages are applied to the outstanding balances of various categories:

Loan Status	Allowance (%)
30-59 days overdue-	30%
60-179 days overdue	60%
More than 180 days overdue-	100%

The Organization also maintains a general provision against the loan portfolio as a whole.

Interest on loans is accrued on the principal amount of loans outstanding. The Organization accrues interest on its loans as it is collected from the loan customers in cash.

c. Non-Current Assets

Fixed Assets include tangible and intangible assets and are shown at cost less accumulated depreciation and amortization. Depreciation is calculated using the reduced balance method at the rates of

depreciation provided by the Tax Code of the Azerbaijan Republic. Amortization of intangible assets is calculated using the straight line method at the rate of 10% per annum.

d. Income and Expense Recognition

Income and expenses are recognized on an accrual basis.

e. Currency

The US Dollar is the reporting currency. The books and records in the Organization are maintained in Azerbaijani Manats (AZN, although significant volume of operations, i.e. loan granting and repayments, receipt of interest is conducted in US Dollars. Payment of operating expenses is conducted in AZN.

Transfer of the results of transactions denominated in AZN is made in accordance with IAS 21 *The Effects of Changes in Foreign Exchange Rates*. Exchange rates used are official rates of the National Bank of the Azerbaijan Republic, which is an average of the market rates. Gains or losses originated on such transactions are included in the Profit and Loss account.

The exchange rate as of December 31, 2006 and 2005 were AZN 0.8714 and AZN 0.9186 to USD 1 respectively.

3. Cash and cash equivalents

Cash and cash equivalent balances as of December 31, 2006 and 2005 are as follows:
(In US Dollars)

Type of cash	2006	2005
Cash on hand	16,817.67	15,065
Cash in bank	8,598.10	94,578
Total Cash	25,415.77	109,643

4. Loan and Loan Loss Allowance

The amount of outstanding loan before reduction for possible losses as of December 31, 2006 and 2005 are USD 2,528,965.73 and 1,1590,236 respectively.

Prior to the year 2005 and 2006 the Organization made provisions for possible loan losses. Reserves for possible loan risks were created in 2005 and the balance of risk reserves as of 31st December, 2006 is as follows:

(In US Dollars)

Type of reserve	Balance
Special reserves for loans overdue for more than 30 days	18,521.88
General reserve for outstanding loans	25,138.75
Total Loan Loss Reserve	43,660.63

The maturity analyses of the loan are as follows:

(In US Dollars)

	2006
Due less than 30 days	2,509,158.00
Due within 30-59 days	1,673.22
Due within 60-179 days	3,102.63
Due 180 and more days	15,031.88
Total Loan Balance	2,528,965.73

**5. Other current assets
(In US Dollars)**

Type of asset	Balance	
	31.12.2006	31.12.2005
Taxes	0	1,579
Prepayments	907.05	207
Total	907.05	1,785

**6. Non-current assets
(In US Dollars)**

	Machinery & Equipment	Vehicles	Other assets	Intangibl e Assets	Total Fixed Assets
Original Cost as of 31.12.2004	38,173.57	64,515.69	8,414.95	1,191.88	112,296.09
Additions in 2005	8,068	11,609	1,299	120	21,096
Disposals in 2005					
Change in USD value due to change in exchange rate	1,268	2,329	279	7	3,883
1)Original Cost as of 31.12.2005	47,509.57	78,453.69	9,992.95	1,318.88	137,275.09
2)Depreciation as of 31.12.2005	20,345.58-	35,335.81	3,388.83	238.42	59,308.64-
3)Charge for the year 2006	4,477.27	22,106.69	2,561.85	0-	29,145.81-
4)Change in USD value due to change in exchange rate	2,573.38-	4,249.50	541.29	71.45-	7,435.62-
5)Depreciation as of 31.12.2006	28,422.88	50,850.25	5,315.93	365.22	84,954.28-
6)NBV as of 31.12.2005	27,163.99	43,117.87	6,604.12	1,080.47	77,966.45-
7)NBV as of 31.12.2006	26,137.34	53,959.63	7,780.16	1,025.11	88,902.24-

7. Debt

Debt as of December 31, 2006 and 2005 consisted of the following:

(In US Dollars)

Name of the party providing the loan	Date of loan	Final due date	Annual Interest %	Balance at 31.12.05	Additionally received (Repaid) during the year 2006	Change due to change in the exchange rate	Balance at 31.12.06
Long-term loans							
SFDI	08.11.02	30.04.08	0%	53,070	(37,296.30)	2,874.46	18,648.16
SFDI	03.03.06	03.09.15	9.5%	0	157,057.60		157,057.60
Kolibri Kapital	26.09.05	26.09.08	9%	200,000	0	0	200,000
Kolibri Kapital	22.06.06	22.06.08	10%	0	40,000	0	40,000
Kolibri Kapital	16.10.06		10%	0	95,000	0	95,000
MicroCredit Enterprises	01.12.06	30.11.08	10%	0	500,000	0	500,000
Total Long-term loans				253,070	754,761.3	2,874.46	1,010,705.76
Short-term loans							
SFDI	08.11.02	30.04.08	0%	35,380		1,916.30	37,296.30
Kolibri Kapital	23.12.05	23.12.06	9%	75,000	(75,000)		0
Total short-term loans				110,380	(75,000)	1,916.30	37,296.30

8. Other current liabilities

(In US Dollars)

Type of liability	Balance, 31.12.2006	Balance 31.12.2005
Various Taxes	5037.44	4135
Sundry creditors	0	0
Salaries	0	0
Total Current Liabilities	5037.44	4135

9. Related Parties Transactions, Share Capital, Grants..

The Organization's Share Capital is fully contributed by the Norwegian Refugees Council and constitutes AZN 5075.

Norwegian Microcredits LLC receives grants from Norwegian Refugees Council and AMFA. In the year 2006 capital grant in amount of USD 0 and equipment grant in amount of USD 7050.80 were received. The above grants were shown as direct additions to equity and the corresponding asset account.

Also, during the year 2006 the Organizations received funds to subsidize operating and administrative expenses in amount of USD 10476.32 which was recorded in the Income Statement as grant income.

10. Segment reporting of business operations
(In US Dollars)

Segment of Business	Baku Branch	Khachmaz Branch	Beylaqan Branch	Total
Interest Income	270,644.94	203,126.11	175,421.41	649,192.46
Net Interest Income after Provision for loan losses	259,120.17	161,789.49	169,813.36	590,723.02
Fee and commission income	25,161.01	26,967.67	19,042.38	71,171.06
Other Operational Income	63.04	0	704.04	10,007.08
Segment Result	114130.97	64999.13	63402.85	242532.92
Grant Income				17,527.12
Unallocated expenses				(40530.62)
Income Taxes				(44440.51)
Net Profit				157,561.82
Non-current Assets	25,237.81	17,991.34	27,659.42	70,888.57

11. Other Expenses

(In US Dollars)

Type of Expense	2006	2005
Minor Equipment	968.53	498
Office expenses	9,260.08	7,964
Utilities	2,186.19	1,714
Telephone & Internet	18,568.63	12,887
AMFA membership feep	785.64	786
Fuel	12,991.16	8,943
Vehicles Insurance	3,613.31	2,609
Transport expenses	6,968.53	7,945
Audit fee	24,346.14	2,641
Business trips	1,153.77	3,657
Bank fees	13,980.46	1,105
Trainings	9,632.01	3,676
Staff insurance	1,138.04	1,046
Other miscellaneous expenses	15,552.07	1,918
Total Other Expenses	121,144.56	57,389

12. Statement of recognized gains and losses
(In US Dollars)

	2006	2005
Non tax-deductible administration cost-		
	5,263.94	2,050
Net loss not recognized in the income statement	(5,263.94)	(2,050)
Net profit for the period	157,561.82	134,291
Total recognized gains and losses	152,297.88	132,241

13. Commitments and contingencies

a. Environment of Azerbaijan

Azerbaijan still continues to undergo substantial political, economic and social changes. With an emerging market economy, Azerbaijan does not possess a well-developed business and regulatory infrastructure that would generally exist in a more mature market economy. Furthermore, the Azerbaijan Government has not yet fully implemented the reforms necessary to create banking, judicial, taxation and regulatory systems that usually exist in more developed markets. As a result, operations in Azerbaijan involve risks that are not typically associated with those in developed markets. Simultaneously, the mentioned risks are the tendency to reduction due to economic and social changes. Although in recent years inflation has not been significant, certain risks exist in the current environment with results that include, but are not limited to a currency that is not freely convertible outside of the country, certain currency controls and young debt and equity markets characterized by low liquidity levels.

b. VAT

According to the Tax Code of the Azerbaijan Republic, an activity of Norwegian Microcredits LLC is exempt of Value Added Tax. However, in December 2002 the Organization was registered as a VAT payer by the Tax Ministry and since that moment VAT paid to various suppliers was debited to VAT account and then offset with other taxes due to the Tax Ministry. Due to not signing with Norwegian Refugees Council granted agreement for the year 2006 and according to Norwegian Microcredits LLC statement to the Tax authorities' dtd 10 February 2006, the VAT registration was postponed. The total VAT paid for the year 2006 was USD 1709.5

c. Social Contributions

Since the year 2005 Norwegian Microcredits LLC is exempt of social contributions on salaries paid to employees in accordance with the Letter # 03/03-482 dated 04.04.05 of the State Social Protection Fund of the Azerbaijan Republic. Employees of the Organization are liable for both personal income tax and social contributions on their income.

The balance due to Social Protection Fund as of December 31, 2006 is USD 85,376.60.. This balance is a result of non-payment of social contributions for several years due to absence of clear legislation with regards to social liabilities of the Organization. In the year 2007 the accumulated debt to the Social protection Fund will be paid off.

d. Profit Tax

The balance of Profit Tax as of December 31, 2006 is USD 12,473.36. This balance is accumulated during the recent years due to absence of clear legislation with regards to corporate taxation for type of organizations as Normicro is. During the year 2007 the profit tax liability will be paid off.

**14. Fee and Commission Income
(In US Dollars)**

	2006	2005
Application fee	10,424.69	9,975
Service fee	40,982.41	29,852
Credit risk fee	18,026.79	12,179
Penalties	1,737.17	900
Total	71,171.06	52,906

15. Deferred Income

Deferred Income in amount of USD 4,517.17 represents an operating grant received from the Norwegian Refugees Council, will be write off for expenses and profits partially during forthcoming financial periods.

16. Write off

According to prepared credit provisions, write off was in amount of 10779.36 USD from 12 people.