

NORWEGIAN MICROCREDIT LLC

**FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER,
2005 and 2004 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 2005 and the related statements of income, equity and cash flows for the year then ended. 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 2005 and of the results of its operations and its cash flows for the year then ended in accordance with International Accounting Standards.

Central Asia Business Consultants

April 24, 2006



NORWEGIAN MICROCREDIT LLC

BALANCE SHEET as of 31 December 2005, 2004

(In US Dollars)

	NOTES	2005	2004
ASSETS			
<u>Non-Current assets</u>			
Property, plant and equipment	2c, 6, 10	76,918	69,979
Intangible Assets	2c, 6, 10	1,080	1,125
<u>Total Non-current assets</u>		<u>77,998</u>	<u>71,104</u>
<u>Current assets</u>			
Loans, net of allowances for losses	2b, 4	1,561,040	1,249,168
Other current assets	5	1,785	2,829
Cash and cash equivalents	3	109,643	13,932
<u>Total current assets</u>		<u>1,672,468</u>	<u>1,265,929</u>
TOTAL ASSETS		1,750,467	1,337,033

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

NORWEGIAN MICROCREDIT LLC

BALANCE SHEET as of 31 December, 2005

(In US Dollars)

	Note	2005	2004
EQUITY AND LIABILITIES			
<u>Equity & Resources</u>			
Share capital	9	5,525	5,175
Retained earnings	12	403,383	253,999
Grants received	9	801,036	713,654
<u>Total Equity & Resources</u>		<u>1,209,944</u>	<u>972,828</u>
<u>Non-current liabilities</u>			
Long-term credits	7	288,450	199,429
<u>Current liabilities</u>			
Short-term credits	7	75,000	50,223
Profit Tax	13	75,895	38,576
Social Protection Fund	13	80,837	75,282
Other current liabilities	8	4,135	696
Deferred Income	15	16,206	
<u>Total current liabilities</u>		<u>252,073</u>	<u>164,777</u>
Total Liabilities		540,523	364,206
TOTAL EQUITY AND LIABILITIES		1,750,467	1,337,033

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NORWEGIAN MICROCREDIT LLC

INCOME STATEMENT for the year ended 31 December, 2005

(In US Dollars)

Indicator	Note	2005	2004
<u>Interest Income</u>	10		
Interest on loans		522,078	365,544
<u>Total Interest Income</u>		<u>522,078</u>	<u>365,544</u>
<u>Interest Expense</u>			
Interest on credits		22,305	5,000
<u>Total Interest Expense</u>		<u>22,305</u>	<u>5,000</u>
Net Interest Income		499,773	360,544
Provision for loan losses	4	29,196	10,814
Net interest income after provision for loan losses	10	470,577	349,730
Fee and commission income	10,14	52,906	41,574
Other operational income		915	1,127
Grant income	9,10	14,215	
<u>Non-interest expense</u>			
Salaries and benefits		196,722	203,252
Expenses related to immovable property		21,662	21,385
Office rent		21,563	18,660
Exchange Loss	2e	64,578	3,168
Other expenses	11	57,389	42,472
<u>Total non-interest expense</u>		<u>361,913</u>	<u>288,937</u>
Net Operational Income before tax		176,699	103,492
Profit Tax	10	42,408	24,838
NET INCOME AFTER TAX	2d, 10, 12	134,291	78,654

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NORWEGIAN MICROCREDIT LLC

STATEMENT OF CHANGES IN EQUITY as of 31 December, 2005 and 2004

(In US Dollars)

	Note	Share Capital	Retained Earnings	Grants Received	Total Equity and Resources
Balance 01.01.2004		5,154	181,049	600,908	787,111
Additions in 2004			72,211	110,295	182,506
Changes arisen from re-evaluation of currency in 2004	2e	21	739	2,451	3,211
Balance 01.01.2005		5,175	253,999	713,654	972,828
Additions in 2005	9, 12		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

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NORWEGIAN MICROCREDIT LLC**CASH FLOW STATEMENT as at 31 December 2005, 2004****(In US Dollars)**

Indicator	Note	2005	2004
Cash flow from operations (excluding grants)			
Net Operational Income	2d, 12	132,241	72,211
Adjustments to reconcile net income with funds provided from operations:			
Increase in value of equity due to change in exchange rate US\$:AZM	2e	17,493	761
Depreciation of fixed assets	2c, 6	20,975	20,527
Amortization of Intangible Assets	2c, 6	120	109
Changes in assets and liabilities:			
decrease (increase)in other current assets	5	1,044	(900)
Increase in Profit tax, SPF and other current liabilities	8, 13c, 13d	62,519	61,320
Total funds provided from operating activities		234,392	154,028
Cash flows from investment activities			
Net increase in loan portfolio	4	(311,872)	(304,353)
Purchase of fixed assets	6	(27,989)	(21,896)
Total cash used in investment activities		(339,861)	(326,249)
Cash flows from financing activities			
Increase in short-term debt	7	24,777	205
Increase in long-term	7	89,021	51,422
Increase in donations and grants	9	87,382	112,746
Net cash flows from financing activities		201,180	164,373
NET INCREASE IN CASH	3	95,711	(7,848)
CASH AND CASH EQUIVALENTS AT THE BEGINNING OF THE YEAR	3	13,932	21,780
CASH AND CASH EQUIVALENTS AT THE END OF THE YEAR		109,643	13,932

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

NORWEGIAN MICROCREDIT LLC

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEARS 2005, 2004

1. Organization and basis of presentation

Norwegian Microcredits LLC (Normicro or the Organization) is a non-for-profit organization, is incorporated in Azerbaijan in 2002 by the Norwegian Refugees Council which is a 100% owner of Normicro.

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

By the year 2004 reserves for possible loan losses were not created. Since the year 2005 the Organization has changed its policy and started creating provisions for possible loan losses. In 2005 loans have been reduced by the allowance for loan losses. 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 aging 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

NORWEGIAN MICROCREDIT LLC

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEARS 2005, 2004

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 (AZM), 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 AZM.

Transfer of the results of transactions denominated in AZM 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, 2005 and 2004 were AZM 4593 and AZM 4903 to USD 1 respectively.

The translation of AZM-denominated assets and liabilities into USD as at December 31, 2005 and 2004 does not indicate the organization could realize or settle in USD the translated value of these assets and liabilities.

3. Cash and cash equivalents

Cash and cash equivalent balances as of December 31, 2005 and 2004 are as follows:

(In US Dollars)

Type of cash	2005	2004
Cash on hand	15,065	10,494
Cash in bank	94,578	3,438
Total Cash	109,643	13,932

4. Loan and Loan Loss Allowance

The amount of outstanding loan before reduction for possible losses as of December 31, 2004 and 2005 are USD 1,590,236 and 1,249,168 respectively.

Prior to the year 2005 the Organization did not make provisions for possible loan losses. Consequently, the balance of outstanding loans as of 31st December, 2004 is stated without reduction for risks provision. Reserves for possible loan risks were created in 2005 and the balance of risk reserves as of 31st December, 2005 is as follows:

NORWEGIAN MICROCREDIT LLC

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEARS 2005, 2004

(In US Dollars)

Type of reserve	Balance
Special reserves for loans overdue for more than 30 days	18,080
General reserve for outstanding loans	11,116
Total Loan Loss Reserve	29,196

The maturity analysis of the loan are as follows:

(In US Dollars)

	2005
Due less than 30 days	1,564,411
Due within 30-59 days	3,735
Due within 60-179 days	8,518
Due 180 and more days	13,572
Total Loan Balance	1,590,236

5. Other current assets

(In US Dollars)

Type of asset	31.12.2005	Balance	31.12.2004
Taxes	1,579		2,604
Prepayments	207		225
Total	1,785		2,829

NORWEGIAN MICROCREDIT LLC**NOTES TO THE FINANCIAL STATEMENTS FOR THE YEARS 2005, 2004****6. Non-current assets**

(In US Dollars)

	Machinery & Equipment	Vehicles	Other assets	Intangible Assets	Total Fixed Assets
Original Cost as of 31.12.2004	44,535	73,493	9,361	1,236	128,625
Additions in 2005	7,771	13,101	2,319		23,190
Disposals in 2005					
Change in USD value due to change in exchange rate	3,006	4,960	632	83	8,681
Original Cost as of 31.12.2005	55,312	91,554	12,312	1,319	160,496
Depreciation as of 31.12.2004	18,781	34,499	4,130	111	57,521
Charge for the year 2005	8,068	11,609	1,299	120	21,096
Change in USD value due to change in exchange rate	1,268	2,329	279	7	3,883
Depreciation as of 31.12.2005	28,117	48,437	5,708	238	82,500
NBV as of 31.12.2004	25,754	38,994	5,231	1,125	71,104
NBV as of 31.12.2005	27,196	43,118	6,604	1,080	77,998

NORWEGIAN MICROCREDIT LLC

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEARS 2005, 2004

7. Debt

Debt as of December 31, 2005 and 2004 consisted of the following:

(In US Dollars)

Name of the party providing the loan	Date of loan	Final due date	Annual Interest %	Balance at 31.12.04	Additionally received (Repaid) during the year 2005	Change due to change in the exchange rate	Balance at 31.12.05
Long-term loans							
SFIDP	08.11.02	30.06.08	0%	99,429	(17,690)	6,711	88,450
Kolibri Capital	15.11.04;16.02.05;08.09.05;23.12.05	09.08.08	9%	100,000	100,000		200,000
Total Long-term loans				199,429	82,310	6,711	288,450
Short-term loans							
Caucasia Credit LLC	18.12.03	30.12.05	5%	50,223	(50,223)		---
Kolibri Kapital	23.12.05	23.12.06	9%	----	75,000		75,000
Total short-term loans				50,223	24,777		75,000

8. Other current liabilities

(In US Dollars)

Type of liability	Balance, 31.12.2005	Balance 31.12.2004
Various Taxes	4,135	671
Sundry creditors		19
Salaries		6
Total Current Liabilities	4,135	696

9. Related Parties Transactions, Share Capital, Grants.

The Organization's Share Capital is fully contributed by the Norwegian Refugees Council and constitutes AZM 25,375,000.

NORWEGIAN MICROCREDIT LLC

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEARS 2005, 2004

Norwegian Microcredits LLC receives grants from Norwegian Refugees Council. In the year 2005 capital grant in amount of USD 21,732 (AZM 99,824,920) and equipment grant in amount of USD 17,484 (AZM 80,302,072) were received. The above grants were are shown as direct additions to equity and the corresponding asset account.

Also, during the year 2005 the Organizations received funds to subsidize operating and administrative expenses in amount of USD 14,215 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	221,964	147,250	152,863	522,077
Net Interest Income after Provision for loan losses	196,534	125,297	148,765	470,596
Fee and commission income	22,403	15,051	15,451	52,905
Other Operational Income	915			915
Segment Result	95,231	54,620	75,623	225,474
Grant Income				14,215
Unallocated expenses				(62,990)
Income Taxes				(42,408)
Net Profit				134,291
Non-current Assets	26,777	23,423	15,321	65,521
Unallocated non-current assets				12,477

NORWEGIAN MICROCREDIT LLC

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEARS 2005, 2004

11. Other Expenses

(In US Dollars)

Type of Expense	2005	2004
Minor Equipment	498	750
Office expenses	7,964	5,656
Utilities	1,714	839
Telephone & Internet	12,887	11,773
AMFA membership fee	786	
Fuel	8,943	7,941
Vehicles Insurance	2,609	2,646
Transport expenses	7,945	5,551
Audit fee	2,641	2,503
Business trips	3,657	2,924
Bank fees	1,105	850
Trainings	3,676	
Staff insurance	1,046	
Other miscellaneous expenses	1,918	1,042
Total Other Expenses	57,389	42,472

12. Statement of recognized gains and losses

(In US Dollars)

	2005	2004
Non tax-deductible administration cost	2,050	6,443
Net loss not recognized in the income statement	(2,050)	(6,443)
Net profit for the period	134,291	78,654
Total recognized gains and losses	132,241	72,211

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

NORWEGIAN MICROCREDIT LLC

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEARS 2005, 2004

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. 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, activities of Norwegian Microcredits LLC is exempt of Value Added Tax. However, in March 2003 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. Considering that VAT registration of the Organization was not in consistency with the Tax Code, there is a remote possibility that decision on VAT registration may be recalled by the Tax Ministry and VAT offset with other taxes for the whole period of registration then should be repaid to the Tax Ministry. The total VAT paid for the years 2003-2005 was USD 10,442 (AZM 47,961,650).

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, 2005 is USD 80,837. 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 2006 the accumulated debt to the Social protection Fund will be paid off.

d. Profit Tax

The balance of Profit Tax as of December 31, 2005 is USD 75,895. 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 2006 the profit tax liability will be paid off.

14. Fee and Commission Income

(In US Dollars)

	2005	2004
Application fee	9,975	8,638
Service fee	29,852	21,592
Credit risk fee	12,179	10,924
Penalties	900	420
Total	52,906	41,574

15. Deferred Income

NORWEGIAN MICROCREDIT LLC

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEARS 2005, 2004

Deferred Income in amount of USD 16,206 represents an operating grant received from the Norwegian Refugees Council. The grant is aimed to finance operational expenses in the year 2006.