



**AUDITORS' REPORT**

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**To the shareholders of X.A.C Co., LTD.**

We have audited the accompanying balance sheet of X.A.C Co., LTD as of 31 December 2000, and the related profit and loss accounts, statements of changes in equity and cash flows for the then year ended. These financial statements are the responsibility of the company'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 issued by the International Federation of Accountants and laws or regulations of Mongolia. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether then financial statements 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 and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in material respects, the financial position of the XAC Co., LTD as of December 31, 2000 and of the results of its operations and its cash flows for the year then ended in accordance with International Accounting Standards issued by the International Accounting Standards Committee and related laws and regulations which are effective in Mongolia.

Ulaanbaatar, Mongolia  
February 8, 2001

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Itgelt Audit LLC

**X.A.C CO., LTD**  
**BALANCE SHEET**  
**AS OF DECEMBER 31, 1999 AND 2000**  
**(In Mongolian Togrogs)**

	Note	December 31,1999	December 31, 2000
<b><u>Assets</u></b>			
<b>Current assets</b>			
Cash and cash equivalents	4	192,569,752.12	339,227,861.80
Loan and advance	5	258,773,639.00	944,316,366.75
Provision for loan losses	5	(5,098,946.74)	(11,155,968.73)
Other real estate owned	6	270,000.00	966,686.00
Provision for loss – OREO	6	(270,000.00)	(180,066.86)
Other current assets	7	14,167,701.14	46,756,783.57
<b>Total current assets</b>		<b>460,412,145.52</b>	<b>1,319,931,662.53</b>
<b>Non current assets</b>			
Fixed assets	8	52,044,300.00	162,620,474.30
Accumulated depreciation	8	(14,387,924.62)	(39,058,897.74)
Intangible asset		852,788.00	852,788.00
<b>Total Non Current Assets</b>		<b>38,509,163.38</b>	<b>124,414,364.56</b>
<b>Total assets</b>		<b>498,921,308.90</b>	<b>1,444,346,027.09</b>

	Note	December 31,1999	December 31, 2000
<b><u>Liabilities</u></b>			
Accounts payable	9,10	2,398,981.04	40,926,130.35
Social Insurance payable		1,738,313.27	582,208.20
Other tax payable		456,898.78	1,243,349.67
Income taxes payable		1,600,054.29	2,358,900.00
Deferred tax		1,732,444.03	3,114,118.24
Long term loan	10	-	438,800,000.00
Financing of UNDP	11	254,820,911.16	690,419,396.58
<b>Total liabilities</b>		<b>262,747,602.57</b>	<b>1,177,444,103.04</b>
<b>Equity</b>			
Share capital	12	180,000,000.00	180,000,000.00
Retained earnings –Previous year		44,174,019.79	53,523,168.14
Retained earnings –Current year		11,999,686.54	33,378,755.91
<b>Total equity</b>		<b>236,173,706.33</b>	<b>266,901,924.05</b>
<b>Total liabilities and equity</b>		<b>498,921,308.90</b>	<b>1,444,346,027.09</b>

**X.A.C CO., LTD**  
**PROFIT AND LOSS ACCOUNTS**  
**FOR THE YEAR ENDED DECEMBER 31, 1999 AND 2000**  
**(In Mongolian Togrogs)**

	Note	1999	2000
Net interest revenue	13	63,675,439.66	341,125,619.16
Commissions and fees		1,101,100.00	8,754,590.00
Gain (loss) on foreign currency revaluation and trading	13	(431,934.23)	2,314,626.38
Other revenue	13	1,307,978.77	4,797,234.72
<b>Total operating revenue</b>		<b>65,652,584.20</b>	<b>356,992,070.26</b>
Operating expenses	14	(46,714,908.90)	(303,038,425.36)
<b>Income before Provision for loan losses</b>		<b>18,937,675.30</b>	<b>53,953,644.90</b>
Expenses on provisions for loan losses	5	(2,642,790.44)	(7,263,088.99)
Profit before tax expense		16,294,884.86	46,690,555.91
Income tax expenses:	15		
Tax for the period		(2,562,754.29)	(13,311,800.00)
Deferred tax		(1,732,444.03)	-
<b>Net profit</b>		<b>11,999,686.54</b>	<b>33,378,755.91</b>

**STATEMENT OF CHANGES IN EQUITY**  
**FOR THE YEAR ENDED DECEMBER 31, 1999 AND 2000**  
**(In Mongolian Togrog)**

	Share		Retained earnings	UNDP's financing
	Unit	MNT		
Balance as of 31 August 1999	6,000	60,000,000.00	44,174,019.79	228,611,911.16
Additional Shares	12,000	120,000,000.00	-	-
Financing	-	-	-	150,000,000.00
Expenditure for share purchase	-	-	-	(120,000,000.00)
Transferred to payable account	-	-	-	(3,791,000.00)
Net profit for the last period	-	-	11,999,686.54	-
Balance as of 31 December 1999	18,000	180,000,000.00	56,173,706.33	254,820,911.16
Bonus for results of the year 1999	-	-	(2,650,538.19)	-
Adjusted balance as of 31 December 1999	18,000	180,000,000.00	53,523,168.14	254,820,911.16
Received financing for current year	-	-	-	502,662,485.42
Transferred to MSM	-	-	-	(67,064,000.00)
Net profit for the current period	-	-	33,378,755.91	-
<b>Balance as of December 31,2000</b>	<b>18,000</b>	<b>180,000,000.00</b>	<b>86,901,924.05</b>	<b>690,419,396.58</b>

**X.A.C CO., LTD**  
**STATEMENTS OF CASH FLOWS**  
**FOR THE YEAR ENDED DECEMBER 31, 2000**  
**(In Mongolian Togrogs)**

	Sub Total	Total
<i>Cash flows from operating activities:</i>		
Profit before tax	46,690,555.91	
<i>Adjustments for:</i>		
Interest revenue	(348,424,152.16)	
Interest expenses	7,298,533.00	
Provisions for loan losses expenses	7,263,088.99	
Losses on Disposal fixed assets	201,226.52	
Depreciation expenses	24,854,769.60	
	<u>(308,806,534.05)</u>	
Operating income before working capital changes	(262,115,978.14)	
<i>Working capital changes</i>		
Increase in loan and advance	(685,542,727.75)	
Increase in Other real state owned	(696,686.00)	
Increase in other current assets	(12,813,876.11)	
Increase in current liabilities	30,917,295.13	
	<u>(668,135,994.73)</u>	
Operating transactions		
Loan written-off in provision for loan losses	(1,206,067.00)	
Adjustments of provision for OREO losses	(89,933.14)	
Interest received	328,648,945.84	
Interest paid	(58,333.00)	
Income tax paid	(11,171,200.00)	
	<u>316,123,412.70</u>	
<b>Net Cash flows from operating activities</b>		<b>(614,128,560.17)</b>
<i>Cash flows from Investing activities:</i>		
Purchase of fixed assets	(110,961,277.38)	
<b>Net cash flows from Investing activities</b>		<b>(110,961,277.38)</b>
<i>Cash flows from financing activities:</i>		
Long term loan received	438,800,000.00	
Increase in financing fund	435,598,485.42	
Bonus for result of the year 1999 paid	(2,650,538.19)	
<b>Net cash flows from financing activities</b>		<b>871,747,947.23</b>
<b>Total net cash flows</b>		<b>146,658,109.68</b>
Cash and cash equivalents, beginning balance	192,569,752.12	
Cash and cash equivalents, ending balance	339,227,861.80	

**X.A.C CO., LTD**  
**NOTES TO THE FINANCIAL STATEMENTS**  
AS OF DECEMBER 31, 1999 AND 2000.  
(In Mongolian Togrogs )

**1. ORGANIZATION AND OPERATION**

The agreement between the Government of Mongolia and UNDP was made to finance and implement the three-year “MicroStart” project, for the purpose of establishing micro finance market and decreasing the poverty. The project was started in August 1998.

It was decided according to the Working plan approved by UNDP that ACIDI-VOCA, organization in the USA, would implement the project jointly with up to 4 selected NGO’s operating in Mongolia.

The X.A.C, a second tier organization was established in September 1998 for the purpose of project sustainability, and training, advising, controlling and providing financing to the participating organizations and their project implementation units.

During the trial period ended on September 1999, the company was providing small loans with the purpose of improving a living standards of low income families, and financial services to the small businesses, with the cooperation of non governmental organizations providing social oriented services such as Mongolian Women Federation (MWF) and Liberal Women’s Brain Pool (LEOS).

In 23 August 1999, the shareholder’s meeting was held and the articles of incorporation of XAC Co., Ltd was approved and the non governmental organizations including MWF, LEOS and Local Governance Development Fund (LGDF), National Association of Mongolian Agricultural Cooperators (NAMAC) and Rotary Club of Ulaanbaatar, Mongolian Open Society (Soros fund) were approved as a shareholders of XAC Co., Ltd. These six non-governmental organizations own same shares of stock in the capital of the company.

On 16 September 1999, the XAC Co., Ltd was granted the license in accordance with the ‘ ‘ Rule on granting and controlling the license of some banking operations to the banking and non bank financial institutions ‘ ‘, approved by the Bank of Mongolia.

The XAC Co., LTD has branches in Sainshand and Airag soum of Dornogobi aimag, Ondorkhaan soum of Khentii aimag, Chilgeltei, Bayanzurkh, Songinokhairkhan, Sukhbaatar, Khan-Uul districts of Ulaanbaatar capital city, Darkhan soum of Darkhan-Uul aimag, Arvaiheer soum of Ovorhangai aimag, Sukhbaatar soum of Selenge aimag, Choir soum of Gobisumber aimag and unit for Development loan subject to Center office.

Loans are of 5 types in their designated purpose: Working capital loan, Investment loan, Development loan, Being necessities loan and Employee loan.

## 2. ACCOUNTING BASIS

The Financial statements have been prepared on the accrual basis in accordance with International Accounting Standards. The accounting methodologies used by the Management of the company are guided by the Accounting methodologies for non-bank financial institutions, approved by Bank of Mongolia, and Accounting methodologies for business entities, approved by the Ministry of Finance.

## 3. SIGNIFICANT ACCOUNTING POLICIES

The financial statements of XAC Co., Ltd for the year ended December 31, 1999 and 2000, have been prepared on historical cost assumption using the following accounting policies:

(a) Interest revenue and expense

Interest revenues and expenses are accrued on straight-line basis.

(b) Commissions and fees

Service commissions and fees are recorded as revenue when they are paid in cash.

(c) Penalty income

The penalty of 0.2 percent per day is levied on past due loan principle when the loan repayment schedule is violated, and revenue is recognized when the cash is received.

(d) Loan

The net amount of loans outstanding reported on the balance sheet subtracts the loss provision from the gross amount.

Interest on loans made is accrued on the outstanding principles at the balance sheet date.

Interests on loans are calculated at the date of repayment based on the outstanding principle amount of the loan, using simple interest method.

The provision for probable loan loss is determined in accordance with the rules and procedures issued by the management.

Loans are classified in accordance with the rules on loan classification approved by the Bank of Mongolia.

Percentages of loan loss provisions for each loan categories as follow:

Loan categorization	Company's policy	Policy of the Bank of Mongolia		
Standard loan				
Standard loan		1%		1%
*Restructured loan	Prolonged terms	25%		1%
Non-performing loan				
Past due loan	1-30 days overdue	1%	1-90 days overdue	1%
Sub-standard loan	31-60 days overdue	25%	91-180 days overdue	25%
Doubtful loan	61-90 days overdue	50%	181-360 days overdue	50%
Bad loan	>90 days overdue	100%	>360 days overdue	100%

### 3. SIGNIFICANT ACCOUNTING POLICIES (cont'd)

\*In the event where the principles or interest payments become past due, the terms of loans are renegotiated and appropriate changes are made in the loan agreement or contract, resulting in reclassifying these loans to the “Restructured Loan” category.

#### (e) Other Real Estate Owned (OREO)

The assets received in due of repayment of loan is recorded as the Other Real Estate Owned, being valued at the lower of market value of asset or sum total of principle amount of loan and loan interest amount.

Other real estate owned is reported on the balance sheet at the accounting cost and probable loss reserve.

Provision for Probable OREO loss is determined using same percentage used for Provision for loan loss.

#### (f) Operating lease

The company’s lease agreement is an operating lease in its nature. Operating lease expenses are recognized in the profit and loss account for the current year.

#### (g) Foreign currency translation and revaluation.

Transactions in foreign currencies are recorded at Mongolian Togrog using the exchange rate declared by Bank of Mongolia on date of transaction.

Cash, receivable and debt in foreign currencies are translated to Mongolian Togrogs, using the exchange rate on the balance sheet date declared by the Bank of Mongolia.

Cash accounts in foreign currencies are revalued each time when the exchange rates are changed, and resulting differences are recognized as foreign currency revaluation gain or loss. Gain or loss resulted from foreign currency trading is recognized as gain or loss on foreign currency trading.

#### (h) Tangible fixed assets

Building, vehicles, office equipment and computers and technical equipment are reported at their historical cost and accumulated depreciation.

Assets are depreciated over a useful life of assets, using the straight-line method of depreciation.

Useful lives are as follows:

	Under company’s policy	According to Mongolian tax law
Building	20 years	40 years
Vehicle	5 years	10 years
Office equipment	5 years	10 years
Computers and related technical equipment	3 years	10 years

### 3. SIGNIFICANT ACCOUNTING POLICIES (cont'd)

#### (i) UNDP Grants - due to donors

The Financing received to utilize for operating expenses, assets and loan fund of the MicroStart project is initially recorded in "UNDP grants- due to donors" liability account and written off to the 'Retained earnings', equity account for the amount of actual expenditure.

### 4. CASH AND CASH EQUIVALENTS

Balances of cash and cash equivalent accounts as of December 31, 1999 and 2000 are given below. Exchange rates on these dates were 1,072.37 and 1,097.00 Togrog, respectively.

	1999	2000
Petty cash fund	28,430.00	-
Cash on hand-Togrog	24,417,002.00	5,864,391.00
Cash on hand- USDollar	5,361.85	2,451,531.72
Cash in bank – Togrog	16,525,410.72	21,254,414.65
Cash in bank – USDollar	2,099,593.23	11,316,608.11
Domestic currency deposit	-	680,322.00
Foreign currency deposit	149,493,954.32	297,660,594.32
	192,569,752.12	339,227,861.80

### 5. LOAN AND PROVISIONS FOR LOAN LOSS

a) The balances of loans categorized according to the purposes, as of December 31, 1999 and 2000 are as follows:

	1999	2000
Working capital loan	249,204,252.00	718,710,891.00
Investment loan	9,569,387.00	186,811,734.00
Being necessities loan	-	7,794,666.00
Development loan	-	22,505,000.00
Employee loan	-	8,494,075.75
Loan before provision for loan loss	258,773,639.00	944,316,366.75
Provision for Loan loss (i)	(5,098,946.74)	(11,155,968.73)
Total Net Loan	253,674,692.26	933,160,398.02

i. Change in Provision for loan loss as follows.

	1999	2000
Beginning balance	2,856,451.30	5,098,946.74
Additional provision	2,837,790.44	7,263,088.99
Loans written off against the provision	(595,295.00)	(1,206,067.00)
Ending balance	5,098,946.74	11,155,968.73

## **5. LOAN AND PROVISIONS FOR LOAN LOSS**

b) The balances of loan and related provision as of December 31, 1999 and 2000 as follows:

Classification	As of 31 December, 1999		As of 31 December, 2000	
	Loan	Provision	Loan	Provision
Standard loan	252,440,042.00	(2,524,400.42)	938,889,025.75	(9,388,890.26)
Restructured loan	402,250.00	(318,440.25)	1,715,373.00	(428,843.25)
Past due loan	2,939,407.00	(29,394.07)	1,515,097.00	(15,150.97)
Sub-standard loan	505,000.00	(126,250.00)	242,835.00	(60,708.75)
Doubtful loan	772,956.00	(386,478.00)	1,383,321.00	(691,660.50)
Bad loan	1,713,984.00	(1,713,984.00)	570,715.00	(570,715.00)
	258,773,639.00	(5,098,946.74)	944,316,366.75	(11,155,968.73)

## **6. OTHER REAL ESTATE OWNED**

The balances of OREO as of December 31, 1999 and 2000 as follows:

	As of 31 December, 1999		As of 31 December, 2000	
	OREO	Provision	OREO	Provision
Standard OREO	-		756,686	(7,566.86)
Doubtful OREO	-		75,000	(37,500)
Bad OREO	270,000	(270,000)	135,000	(135,000)
	270,000	(270,000)	966,686	(180,066.86)

## **7. OTHER CURRENT ASSETS**

The balances as of December 31, 1999 and 2000 as follows:

	1999	2000
Interest receivable	8,424,258.14	28,199,464.46
Collateral	108,000.00	544,000.00
Prepayments to Individuals	-	1,375,704.28
Prepayments	3,257,626.00	7,161,472.66
Employee advances	65,600.00	-
Supplies	866,336.50	2,929,650.67
Low valuable and fast depreciable items	1,445,880.50	6,546,491.50
	14,167,701.14	46,756,783.57

## 8. FIXED ASSETS

The statement of fixed asset's movement, from December 31, 1999 to December 31, 2000 as follow:

	Dec 31, 1999	Additions	Disposals	Dec 31, 2000
<b>Building</b>				
Initial cost	-	35,663,565.00	-	35,663,565.00
Accumulated depreciation	-	(153,751.41)	-	(153,751.41)
Net book value	-	35,509,813.59	-	35,509,813.59
<b>Vehicle</b>				
Initial cost	-	10,260,000.00	-	10,260,000.00
Accumulated depreciation	-	(684,000.00)	-	(684,000.00)
Net book value	-	9,576,000.00	-	9,576,000.00
<b>Office equipment</b>				
Initial cost	16,872,311.00	16,096,359.50	463,773.00	32,504,897.50
Accumulated depreciation	(2,697,909.76)	(4,923,896.66)	(189,581.83)	(7,432,224.59)
Net book value	14,174,401.24	11,172,462.84	274,191.17	25,072,672.91
<b>Computer &amp; tech. Equipment</b>				
Initial cost	35,171,989.00	48,683,785.80	-	83,855,774.80
Accumulated depreciation	(11,690,014.86)	(19,098,906.88)	-	(30,788,921.74)
Net book value	23,481,974.14	29,584,878.92	-	53,066,853.06
Fixed assets' financing	-	336,237.00	-	336,237.00
<b>Total</b>				
Initial cost	<b>52,044,300.00</b>	<b>111,039,947.30</b>	<b>463,773.00</b>	<b>162,620,474.30</b>
Accumulated depreciation	<b>(14,387,924.62)</b>	<b>(24,860,554.95)</b>	<b>(189,581.83)</b>	<b>(39,058,897.74)</b>
Net book value	<b>37,656,375.38</b>	<b>86,179,392.35</b>	<b>274,191.17</b>	<b>123,561,576.56</b>

Depreciation expense recorded for the current year was 24,854,770Togrog.

## 9. ACCOUNTS PAYABLE

The balances of payables as of 31 December, 1999 and 2000, as follows:

	Dec 31, 1999	Dec 31, 2000
Accounts payable	557,894.04	9,035,295.70
Accrued payable	318,287.00	607,500.00
Interest payable	-	7,240,200.00
Payable to MSM	1,522,800.00	24,043,134.65
	2,398,981.04	40,926,130.35

## 10. LONG TERM LOAN

XAS Co., LTD borrowed 400,000 USD for the purpose of financing growth of the activities as stipulated in the business plan under the Convertible Loan Agreement made between XAS Co., LTD and Stichting TRIODOS-DOEN. As reflected in the terms of the agreement, the loan must be repaid within two years since the disbursement or before 1 January 2003.

The interest rate of the loan is on 3-months LIBOR+2.8% p.a. The rate is fixed for three months on the 1 of January, April, July and October for the next three months. Interest is payable quarterly in USD at the end of each three-months starting January 1, 2001.

6,600USD or 7,240,200 togros is reported in the financial statements as of December 31, 2000 as interest payables.

## **11. UNDP GRANTS – DUE TO DONORS**

The balance of UNDP grants as of 31 December, 1999 and 2000, as follows:

	1999	2000
Beginning balance	228,611,911.16	254,820,911.16
Increase:		
Financing received	146,209,000.00	502,662,485.42
Accumulated total	374,820,911.16	757,483,396.58
Decrease :		
Distributed to owners	(120,000,000.00)	-
Expenditures for operation	(-)	(67,064,000.00)
Total expenditures	(120,000,000.00)	(67,064,000.00)
Ending balance	254,820,911.16	690,419,396.58

## **12. SHARE CAPITAL**

XAC Co., LTD declared 60,000 shares of stock with a par value of 10,000 togrog. The number of shares outstanding as of 31 December 2000 is 18,000 shares of stock with a par value of 10.000.

## **13. REVENUE**

The revenue for the years ended on December 31, 1999 and 2000, as follows:

### a) Net interest revenue

	Year ended 31/12/99	Year ended 31/12/2000
Interest revenue		
Interest on loan	62,022,041.00	329,965,559.06
Interest on bank account	589,687.52	506,356.92
Interest on deposit account	1,088,316.14	17,952,236.18
	63,700,044.66	348,424,152.16
Discount on interest and interest expense	(24,605.00)	(7,298,533.00)
Net interest revenue	63,675,439.66	341,125,619.16

### b) Net loss on foreign exchange and trading

	Year ended 31/12/99	Year ended 31/12/2000
Gain on foreign currency revaluation	414,700.08	3,501,208.03
Loss on foreign currency revaluation	(574,794.17)	(1,284,450.85)
Net gain (loss) on foreign currency revaluation	<b>(160,094.09)</b>	<b>2,216,757.18</b>
Gain on foreign currency trading	-	212,900.00
Loss on foreign currency trading	(271,840.14)	(115,030.80)
Net gain (loss) on foreign currency trading	<b>(271,840.14)</b>	<b>97,869.20</b>
Total net gain (loss)	<b>(431,934.23)</b>	<b>2,314,626.38</b>

## **13. REVENUE (Continued)**

c) Other revenue

	Year ended 31/12/99	Year ended 31/12/2000
Penalty revenue	698,264.00	2,294,584.00
Other revenue	609,714.77	2,502,650.72
	1,307,978.77	4,797,234.72

**14. OPERATING EXPENSES**

	Year ended 31/12/99	Year ended 31/12/2000
Salaries	14,327,850.66	101,454,522.06
Social insurance	3,900,132.40	22,129,724.71
Compensation and remuneration	6,218,860.30	14,517,636.00
Loan approval committee's fee	2,512,688.00	12,190,545.33
Stationary	1,910,707.50	10,709,532.08
Rent and utilities	4,475,539.00	22,856,877.50
Depreciation expenses	4,799,502.55	24,854,769.60
Communication	1,801,576.97	12,358,885.36
Business travel	1,187,390.00	22,104,322.91
Fuel and transportation	1,295,209.00	10,329,439.00
Training of customers	363,185.00	1,856,165.00
Training of Employees	-	2,415,294.00
Entertainment	631,606.00	9,324,247.00
Advertisement	-	2,920,495.80
Maintenance of fixed assets	-	7,535,023.02
Press subscriptions	-	314,516.00
Sanitary expenses	-	757,029.00
Financial charges	-	8,111,661.66
Audit fees	-	3,195,600.00
Insurance expenses	-	1,274,000.00
Automations	-	4,969,660.00
Labor safeties and janitorial	-	1,050,552.50
Other expenses	3,290,661.52	5,807,926.83
Total operating expenses	46,714,908.90	303,038,425.36

**15. INCOME TAX**

As stated in the Income tax law of Mongolia, 15% tax is levied on taxable income up to 100 million Togrog. For taxable income above 100 million, 15 million Togrog plus 40 % tax on the amount in excess of 100 million is to be levied.

For the income tax computation made by XAS Co., LTD with Tax authority, 13,311.8 thousand togros are being levied for income tax.

**16. POST BALANCE SHEET EVENT**

XAS Co., LTD is planning to operate through 25 branches in the end of 2004 and Managerial Representation Counsel has decided to open the new branches in Erdenet city of Orkhon aimag, Arkhangai, Dornod aimags and in Zavkhan, Khovd aimags of Western areas in 2001.