

**XacBank LLC**

Financial Statements for the year ended  
31 December 2004

**XacBank LLC**  
**Corporate information**

**Banking Licence No. 24** dated 27 December 2001, issued by the Bank of Mongolia.

<b>Board of Directors</b>	Chuluun Ganbold Stephen Mitchell Chuluun Ganhuyag Jambaldorj Erdenechimeg Tsend Enhtuya Ser-Od Jargalsaihan Nyamaa Tumenbayar Ganhuyag Munhbat Tuvdendorj Galbaatar Steve Zimmerman James Anderson	Chairman Vice Chairman Director Director Director Director Director Director Director Director Director Non-voting Director
<b>Executive Committee</b>	Chuluun Ganbold Chuluun Ganhuyag Nyamaa Tumenbayar Steve Zimmerman James Anderson	Chairman Member Member Member Non-voting Member
<b>Audit Committee</b>	Stephen Mitchell James Anderson Ser-Od Jargalsaihan Jambaldorj Erdenechimeg	Chairman Non-voting Vice-chairman Member Member
<b>Risk Management and Lending Committee</b>	James Anderson Chuluun Ganhuyag Tsend Enhtuya Tuvdendorj Galbaatar Ganhuyag Munhbat	Non-voting Chairman Member Member Member Member
<b>Executive Officers</b>	Chuluun Ganhuyag Gira Delgermaa Dugersuren Bat-Ochir Bayanjargal Delgerjargal Lhagvasuren Soronzonbold	Chief Executive Officer Chief Operations Officer Chief Financial Officer Chief Credit Officer Strategic Planning & Marketing Division, Director
	Ganzorig Zul Galbadrah Tsogbadrah Chuluun Gantulga	Administration Division, Director Branch Banking Division, Director Operations Division, Director
<b>Registered office</b>	XacBank Building Prime Minister Amar's Street Sukhbaatar District, Ulaanbaatar Mongolia	
<b>Auditors</b>	KPMG Kuala Lumpur, Malaysia	

**XacBank LLC**  
**Corporate information**

### **Board of Directors' responsibility statement**

The Bank's Board of Directors is responsible for the preparation of the financial statements.

The financial statements of XacBank LLC have been prepared to comply with International Financial Reporting Standards. The Board of Directors is responsible for ensuring that these financial statements present fairly the state of affairs of the Bank as at 31 December 2004 and the results and cash flows for the year then ended on that date.

The Board of Directors have responsibility for ensuring that the Bank keeps proper accounting records which disclose with reasonable accuracy the financial position of the Bank and which enable them to ensure that the financial statements comply with the requirements set out in note 2(a) thereto.

The Board of Directors also have a general responsibility for taking such steps as are reasonably open to them to safeguard the assets of the Bank and to prevent and detect fraud and other irregularities.

The Board of Directors consider that, in preparing the financial statements on pages 4 to 38, they have used appropriate policies, consistently applied and supported by reasonable and prudent judgement and estimates, and that all applicable accounting standards have been followed.

Signed in accordance with a resolution of the Board of Directors:

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Chuluun Ganhuyag  
Executive Director

Ulaanbaatar, Mongolia

31 March 2005

## **Report of the auditors to the members of XacBank LLC**

We have audited the financial statements of XacBank LLC on pages 4 to 38. The preparation of the financial statements is the responsibility of the Bank's Board of Directors.

It is our responsibility to form an independent opinion, based on our audit, on the financial statements and to report our opinion to you, as a body, and for no other purpose. We do not assume responsibility towards any other person for the content of this report.

We conducted our audit in accordance with International Standards on Auditing. These standards require that we plan and perform the audit to obtain all the information and explanations which we consider necessary to provide us with evidence to give reasonable assurance that the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence relevant to the amounts and disclosures in the financial statements. An audit also includes an assessment of the accounting principles used and significant estimates made by the Directors as well as evaluating the overall adequacy of the presentation of information in the financial statements. We believe our audit provides a reasonable basis for our opinion.

In our opinion, except for the non-compliance with International Accounting Standard (“IAS”) 39 and IAS 30 with respect to general provision as disclosed in Note 2(a), the financial statements on pages 4 to 38 present fairly, in all material respects, the state of affairs of XacBank as at 31 December 2004 and the results and cash flows for the year then ended on that date in accordance with International Financial Reporting Standards.

KPMG

Ulaanbaatar, Mongolia

31 March 2005

**XacBank LLC**  
**Balance sheet at 31 December 2004**

	Note	2004 MNT'000	2003 MNT'000
<b>ASSETS</b>			
Cash on hand	3	1,052,516	637,419
Balances with other banks	3	4,204,447	1,143,765
Balances with the Bank of Mongolia	3	1,392,439	1,121,497
Investment securities - Available for sale	4	965,169	1,946,792
Loans and advances - Net	5	20,044,996	10,840,446
Property, plant and equipment	6	2,437,507	1,386,299
Other assets	7	1,501,697	727,184
		<hr/>	<hr/>
<b>TOTAL ASSETS</b>		<b>31,598,771</b>	<b>17,803,402</b>
<hr/>			
<b>LIABILITIES AND SHAREHOLDERS' EQUITY</b>			
<b>Liabilities</b>			
Deposits from customers	8	15,696,429	10,012,172
Loans from local financial institutions	9	3,581,350	1,680,000
Loans from foreign financial institutions	10	5,108,025	1,197,200
Loans from government agencies	11	1,648,899	856,245
Taxation		30,903	45,709
Deferred grants	12	41,235	88,365
Other liabilities	13	632,078	803,862
		<hr/>	<hr/>
<b>Total liabilities</b>		<b>26,738,919</b>	<b>14,683,553</b>
<hr/>			
<b>Shareholders' equity</b>			
Share capital	14	4,205,530	3,004,000
Other reserves		22,415	9,436
Retained earnings		631,907	106,413
		<hr/>	<hr/>
<b>Total shareholders' equity</b>		<b>4,859,852</b>	<b>3,119,849</b>
<hr/>			
<b>TOTAL LIABILITIES AND SHAREHOLDERS' EQUITY</b>		<b>31,598,771</b>	<b>17,803,402</b>
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Chuluun Ganhuyag  
*Executive Director*

Dugersuren Bat-Ochir  
*Finance and Accounting Division Director*

*The notes set out on pages 5 to 38 form an integral part of these financial statements*

**XacBank LLC**  
**Statement of income for the year ended 31 December 2004**

	Note	2004 MNT'000	2003 MNT'000
Interest income	15	5,936,418	3,715,511
Interest expense	16	(1,974,577)	(1,168,688)
<b>Net interest income</b>		<b>3,961,841</b>	<b>2,546,823</b>
Net fees and commissions income	17	384,895	212,495
Net foreign exchange gains/(losses)		15,216	(451)
Other operating income	18	108,658	151,930
<b>Net non-interest income</b>		<b>508,769</b>	<b>363,974</b>
<b>Operating income</b>		<b>4,470,610</b>	<b>2,910,797</b>
General and administrative expenses	19	(2,985,140)	(2,284,411)
Impairment losses	20	(274,891)	(123,164)
Grant income		132,269	241,187
Other expenses		(132,269)	(241,187)
<b>Profit from operations</b>		<b>1,210,579</b>	<b>503,222</b>
Corporate income tax	22	(423,085)	(226,343)
<b>Net profit after tax</b>		<b>787,494</b>	<b>276,879</b>

Chuluun Ganhuyag  
*Executive Director*

Dugersuren Bat-Ochir  
*Finance and Accounting Division Director*

*The notes set out on pages 6 to 38 form an integral part of these financial statements*

**XacBank LLC**  
**Statement of changes in equity for the year ended 31 December 2004**

		← <i>Non-distributable</i> →			<i>Distributable</i>	
	<b>Note</b>	<b>Share capital MNT'000</b>	<b>Share premium MNT'000</b>	<b>General reserves MNT'000</b>	<b>Retained earnings/ (accumulated losses) MNT'000</b>	<b>Total MNT'000</b>
Balance at 1 January 2003		3,004,000	-	9,436	(170,466)	2,842,970
Net profit for the year		-	-	-	276,879	276,879
<hr/>						
Balance at 1 January 2004		3,004,000	-	9,436	106,413	3,119,849
Issue of share capital	14	940,000	8,551	-	-	948,551
Capitalisation of retained profits	21	261,530	-	-	(261,530)	-
Dividend paid	21		-	-	(470)	(470)
Increase during the year		-	-	4,428	-	4,428
Net profit for the year		-	-	-	787,494	787,494
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Balance at 31 December 2004		4,205,530	8,551	13,864	631,907	4,859,852

Note 14

*The notes set out on pages 7 to 38 form an integral part of these financial statements*

**XacBank LLC**  
**Statement of cash flows for the year ended 31 December 2004**

	Note	2004 MNT'000	2003 MNT'000
<b>CASH FLOWS FROM OPERATING ACTIVITIES</b>			
<b>Profit before tax</b>		<b>1,210,579</b>	<b>503,222</b>
<i>Adjustments for</i>			
Depreciation		220,958	168,555
Gain on disposal of property, plant and equipment		(4,364)	(5,324)
		<hr/>	<hr/>
<b>Operating profit before changes in operating assets and liabilities</b>		<b>1,427,173</b>	<b>666,453</b>
Increase in loans and advances		(9,204,550)	(5,439,278)
Decrease in amount due from the holding company		-	101,868
Increase in other assets		(772,999)	(204,012)
Increase in deposits from customers		5,684,257	3,832,159
(Decrease) / increase in other liabilities		(171,784)	637,072
		<hr/>	<hr/>
		<b>(3,037,903)</b>	<b>(405,738)</b>
Corporate income tax paid		(437,891)	(136,577)
		<hr/>	<hr/>
<b>Net cash flows used in operating activities</b>		<b>(3,475,794)</b>	<b>(542,315)</b>
<b>CASH FLOWS FROM INVESTING ACTIVITIES</b>			
Net acquisition / (disposal) of investment securities			
– available for sale		981,623	(1,048,732)
Purchase of property and equipment		(1,311,278)	(457,317)
Proceeds from disposals of property, plant and equipment		41,962	21,247
		<hr/>	<hr/>
<b>Net cash flows used in investing activities</b>		<b>(287,693)</b>	<b>(1,484,802)</b>

*The notes set out on pages 8 to 38 form an integral part of these financial statements*

**XacBank LLC****Statement of cash flows for the year ended 31 December 2004 (continued)**

	Note	2004 MNT'000	2003 MNT'000
<b>CASH FLOWS FROM FINANCING ACTIVITIES</b>			
Proceeds from the issue of shares		948,551	-
Increase in general reserves		4,428	-
Increase in loans from local financial institutions		1,901,350	1,000,000
Increase in loans from foreign financial institutions		3,910,825	44,075
Increase in loans from government agencies		792,654	611,245
Decrease in deferred grants		(47,130)	(4,824)
Dividends paid	i)	(470)	-
		<hr/>	<hr/>
<b>Net cash flows generated from financing activities</b>		<b>7,510,208</b>	<b>1,650,496</b>
		<hr/>	<hr/>
<b>Net cash flows generated from / (used in) the year</b>		<b>3,746,721</b>	<b>(376,621)</b>
<b>Cash and cash equivalents at the beginning of the year</b>		<b>2,902,681</b>	<b>3,279,302</b>
		<hr/>	<hr/>
<b>Cash and cash equivalents at the end of the year</b>	<b>3</b>	<b>6,649,402</b>	<b>2,902,681</b>
		<hr/>	<hr/>

**Note:**

- i) During the year, the bank declared an interim dividend of MNT262,000,000 of which MNT261,530,000 was capitalised as share capital and the remaining MNT470,000 was paid in cash.

*The notes set out on pages 9 to 38 form an integral part of these financial statements*

## **XacBank LLC**

### **Notes to the financial statements for the year ended 31 December 2004**

These notes form an integral part of and should be read in conjunction with the accompanying financial statements.

#### **1. Corporate information and principal activities**

X.A.C. Co., Ltd. commenced operations in 1999 as a non-bank financial institution. The company first started its operation by rendering five types of loan services. In October 2001, this company entered into a merger agreement with Goviin Ekhlel Co., Ltd., another non-bank financial institution, to form XAC-GE, a holding company, which owns a majority stake in XacBank LLC. The shareholders of the holding company are:

- Mercy Corps
- Open Society Forum
- Mongolian Women's Federation
- Liberal Women's Intellectual Pool
- National Association of Mongolian Agricultural Cooperatives
- Rotary Club of Ulaanbaatar
- Local Governance Development Foundation
- Tuushin LLC
- Monnis

The principal activities of XacBank LLC ("the Bank"), which is incorporated as a commercial bank under the Mongolian Banking Law, are to provide a wide range of banking products and services, including deposit taking, lending, international and domestic payment services, foreign exchange dealing, securities trading, financial and investment consulting, under Banking Licence No. 24 issued by the Bank of Mongolia on 27 December 2001 (referred to as "the Banking Licence").

The Bank has been and continues to be predominantly involved in providing micro financing to the general public to develop retail and small and medium enterprises.

As at 31 December 2004 the Company had 506 employees (2003: 413 employees).

The financial statements were authorised for issue by the Board of Directors on 31 March 2005.

## **XacBank LLC**

### **Notes to the financial statements for the year ended 31 December 2004 (continued)**

## **2. Summary of significant accounting policies**

The following significant accounting policies have been adopted by the Bank in the preparation of these financial statements.

### **(a) Statement of compliance**

The financial statements have been prepared in accordance with International Financial Reporting Standards ("IFRS") issued and adopted by the International Accounting Standards Board ("IASB"), and interpretations issued by the Standing Interpretations Committee of the IASB except as follows:

As required by the Bank of Mongolia's 'Regulations On Asset Classification And Provisioning' ("BoM's regulations"), the Bank had maintained a 1% general provision for all its performing loans, movement of which are charged to the Income Statement, amounting to approximately MNT201 million (2003: MNT108 million) as at 31 December 2004. This however represents a non-compliance with the following International Financial Reporting Standards:

- a) International Accounting Standard 39 - Financial Instruments: Recognition and Measurement ("IAS 39") which does not allow for the recognition of an impairment loss through an establishment of an allowance for future losses charged to the Income Statement; and
- b) International Accounting Standard 30 - Disclosures in the Financial Statements of Banks and Similar Financial Institutions ("IAS 30") which requires any general provision to be treated as an appropriation of retained earnings.

Had the Bank complied with the above and not maintained the general provision, its profit from operations would increase by MNT93 million (2003: MNT53 million) to MNT1,303 million (2003: MNT556 million).

### **(b) Basis of financial statement preparation**

The financial statements are presented in Mongolian Tugrug ("MNT"), rounded to the nearest thousand. MNT is the Bank's measurement currency. The financial statements are prepared on the historical cost basis, except for the following financial assets and liabilities which are stated at fair value: investments held for trading and investments available-for-sale. The accounting policies have been consistently applied by the Bank and are consistent with those used in the previous year.

**XacBank LLC**

**Notes to the financial statements for the year ended 31 December 2004 (continued)**

**(c) Foreign currency transactions**

Transactions in foreign currencies are translated at the foreign exchange rate ruling at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies, which are stated at historical cost, are translated at the foreign exchange rate ruling at that date. Foreign exchange differences arising on translation are recognised in the income statement. Non-monetary assets and liabilities denominated in foreign currencies, which are stated at historical cost, are translated at the foreign exchange rate ruling at the date of the transaction. Non-monetary assets and liabilities denominated in foreign currencies, which are stated at fair value, are translated into MNT at foreign exchange rates ruling at the dates that the values were determined.

**(d) Financial instruments**

**(i) Classification**

*Trading instruments* are those that the Bank principally holds for the purposes of short-term trading and liquidity management.

*Originated loans and receivables* are loans and receivables created by the Bank providing money to a debtor other than those created with the intention of short-term trading. Originated loans and receivables comprise loans and advances to banks and customers.

*Held-to-maturity assets* are financial assets with fixed or determinable payments and fixed maturity that the Bank has the intent and ability to hold to maturity.

*Available-for-sale assets* are financial assets that are not held for trading purposes, originated by the Bank, or held to maturity.

**(ii) Initial recognition**

Financial instruments are measured initially at cost, including transaction costs, when purchased or originated by the Bank.

**(iii) Subsequent measurement**

Subsequent to initial recognition, all trading instruments and all available-for-sale assets are measured at fair market value, except that any instrument that does not have a quoted market price in an active market and whose fair market value cannot be reliably measured is stated at cost, including transaction costs, less impairment losses.

All non-trading financial liabilities, originated loans and receivables and held-to-maturity assets are measured at amortised cost less impairment losses. Amortised cost is calculated on the effective interest rate method. Premiums and discounts, including initial transaction costs, are included in the carrying amount of the related instrument and amortised based on the effective interest rate of the instrument.

## **XacBank LLC**

### **Notes to the financial statements for the year ended 31 December 2004 (continued)**

#### **(e) Cash and cash equivalents**

Cash and cash equivalents for cash flow purpose comprises cash on hand, balances with other banks and balances with the Bank of Mongolia.

#### **(f) Loans and advances**

Loans and advances originated by the Bank are classified as originated loans and receivables. Loans and advances are reported net of allowances to reflect the estimated recoverable amounts (refer to accounting policy (i)).

#### **(g) Property, plant and equipment**

##### **(i) Cost**

Property, plant and equipment are stated at cost less accumulated depreciation and impairment losses. The initial cost of an item of property, plant and equipment comprises its purchase price, including import duties, non-refundable purchase taxes and any directly attributable costs of bringing the asset to its working condition and location for its intended use. Expenditure incurred after property, plant and equipment have been put into operation, such as repairs and maintenance and overhaul costs, are normally charged to income in the year in which the costs are incurred. In situations where it can be clearly demonstrated that the expenditure has resulted in an increase in the future economic benefits expected to be obtained from the use of an item of property, plant and equipment beyond its originally assessed standard of performance, the expenditure is capitalised as an additional cost of property, plant and equipment.

##### **(ii) Depreciation**

Depreciation is charged to the statement of income on a straight-line basis over the estimated useful lives of property, plant and equipment. The estimated useful lives are as follows:

■ buildings	40 years
■ motor vehicles	10 years
■ office equipment	10 years
■ computers	5 years

#### **(h) Construction in progress**

Construction in progress represents the cost of construction of new buildings and premises, which have not been fully completed or installed. No depreciation is provided for construction in progress during the period of construction.

## **XacBank LLC**

### **Notes to the financial statements for the year ended 31 December 2004 (continued)**

#### **(i) Impairment**

The carrying amounts of the Bank's assets are reviewed at each balance sheet date to determine whether there is objective evidence of impairment. If such an indication exists, the asset's recoverable amount is estimated.

##### ***(i) Originated loans and advances***

Loans and advances are presented net of specific and general allowances for uncollectability. Specific allowances are made against the carrying amount of loans and advances that are identified as being potentially impaired, based on regular reviews of outstanding balances, to reduce these loans and advances to their recoverable amount. General allowances are maintained to reduce the carrying amount of portfolios of similar loans and advances to their estimated recoverable amounts at the balance sheet date. Increases in the allowance account are recognised in the statement of income. When a loan is known to be uncollectible, all the necessary legal procedures have been completed and the final loss has been determined, the loan is written off directly.

If in a subsequent period the amount of impairment loss decreases and the decrease can be linked objectively to an event occurring after the write down, the write-down or allowance is reversed through the statement of income.

##### ***(ii) Assets other than loans and advances***

The recoverable amount is the greater of the asset's net selling price and value in use. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset. For an asset that does not generate cash inflows largely independent of those from other assets, the recoverable amount is determined for the cash-generating unit to which the asset belongs. An impairment loss is recognised whenever the carrying amount of an asset or its cash-generating unit exceeds its recoverable amount. Impairment losses are recognised in the statement of income.

An impairment loss is reversed if there has been a change in the estimates used to determine the recoverable amount. An impairment loss is reversed only to the extent that the asset's carrying amount does not exceed the carrying amount that would have been determined, net of depreciation or amortisation, if no impairment loss had been recognised. All reversals of impairment are recognised in the statement of income.

#### **(j) Non-trading financial liabilities**

Non-trading financial liabilities include deposits from customers and from other financial institutions, interest-bearing borrowings and other amounts payable. Non-trading financial liabilities are initially stated at cost. Subsequent to the initial recognition, they are stated at amortised cost with any difference between cost and redemption value being recognised in the statement of income over the period of the instrument on an effective interest basis.

**XacBank LLC**

**Notes to the financial statements for the year ended 31 December 2004 (continued)**

**(k) Grants**

Grants are recognised initially in the balance sheet as deferred grants when there is reasonable assurance that they will be receivable and that the Bank will comply with the conditions attaching to them. Grants that compensate the Bank for expenses incurred are recognised as revenue in the statement of income on a systematic basis in the same period in which the expenses are incurred. Grants that compensate the Bank for the cost of an asset are recognised in the statement of income on a systematic basis over the useful life of the asset.

**(l) Provisions**

A provision is recognised in the balance sheet when the Bank has a legal or constructive obligation as a result of a past event, and it is probable that an outflow of economic benefits will be required to settle the obligation. If the effect is material, provisions are determined by discounting the expected future cash flows at a pre-tax rate that reflects current market assessment of the time value of money and, where appropriate, the risk specific to the liability.

**(m) Revenue**

**(i) Interest income**

Interest income and expense is recognised in the statement of income as it accrues, taking into account the effective yield of the asset. Interest income and expense include the amortisation of any discount or premium or other differences between the carrying amount of an interest bearing instrument and its amount at maturity calculated on an effective interest rate basis. The recognition of interest income is suspended when the recoverability of principal or interest becomes doubtful. In accordance with the requirement of the Bank of Mongolia, interest is suspended when payment are in arrears for three months (non performing loans). On the commencement of the suspension, related interest receivable is written off. Subsequent to the suspension, interest income is recognised on a cash basis. Interest income recognition will resume on an accrual basis when the uncertainties surrounding the recoverability are removed.

**(ii) Fee income and commission**

Fee and commission income is charged to customers for the financial services provided. Fee and commission income is recognised when the corresponding service is provided.

**(iii) Rental income**

Rental income from leased property is recognised in the income statement on a straight-line basis over the term of the lease. Lease incentives granted are recognised as an integral part of the total rental income.

**XacBank LLC**

**Notes to the financial statements for the year ended 31 December 2004 (continued)**

**(n) Operating lease payments**

Payments made under operating leases are recognised in the income statement on a straight-line basis over the term of the lease. Lease incentives received are recognised in the income statement as an integral part of the total lease expense.

**(o) Income tax**

Income tax on the profit or loss for the year comprises current and deferred tax. Income tax is recognised in the statement of income except to the extent that it relates to items recognised directly to equity, in which case it is recognised in equity.

Current tax is the expected tax payable on the taxable income for the year, using the tax rates approved at balance sheet date and any adjustment to tax payable in respect of previous years.

Deferred tax is provided using the balance sheet liability method providing for temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes. Deferred tax is not provided for temporary differences arising on the initial recognition of assets or liabilities that affect neither accounting nor taxable profit. The amount of deferred tax provided is based on the expected manner of realisation or settlement of the carrying amount of assets and liabilities, using the tax rates approved at balance sheet date. Deferred tax assets are recognised in the financial statements only to the extent that it is probable that future taxable profits will be available against which the asset can be utilised. Deferred tax assets are reduced to the extent that it is no longer probable that the related tax benefit will be realised.

**(p) Employee benefits**

**(i) *Defined contribution plan***

Employee benefits include statutory social insurance payments to the State Social Insurance Scheme. Contributions to this defined contribution plan are recognised as an expense in the statement of income as incurred.

**(ii) *Equity compensation benefits***

The Employee Stock Ownership Plan allows the Bank's staff to acquire shares of the Bank from XAC-GE. No compensation cost or obligation is recognised when options are granted. When shares are purchased, the holding company records the proceeds and share discount in respect of the options exercised and shares will be transferred from the holding company to the employees. No change is made to the Bank's total share capital and no compensation cost is recognised by the Bank.

**XacBank LLC****Notes to the financial statements for the year ended 31 December 2004 (continued)****3. Cash and cash equivalents**

	<b>2004</b> <b>MNT'000</b>	<b>2003</b> <b>MNT'000</b>
Cash on hand	1,052,516	637,419
Balances with other banks	4,204,447	1,143,765
Balances with the Bank of Mongolia	1,392,439	1,121,497
	<hr/>	<hr/>
Total cash and cash equivalents	6,649,402	2,902,681
	<hr/> <hr/>	<hr/> <hr/>

Balances are maintained with the Bank of Mongolia in accordance with the Bank of Mongolia's requirements and bear no interest. Balances are determined based on average deposits and liabilities balances.

**4. Investment securities – available for sale**

	<b>2004</b> <b>MNT'000</b>	<b>2003</b> <b>MNT'000</b>
Bank of Mongolia bills	366,714	1,946,792
Other debt securities	604,500	-
	<hr/>	<hr/>
	971,214	1,946,792
	<hr/>	<hr/>
Impairment losses	(6,045)	-
	<hr/>	<hr/>
	965,169	1,946,792
	<hr/> <hr/>	<hr/> <hr/>

**XacBank LLC****Notes to the financial statements for the year ended 31 December 2004 (continued)****5. Loans and advances**

	<b>2004</b> <b>MNT'000</b>	<b>2003</b> <b>MNT'000</b>
Loans and advances to customers	19,819,550	10,753,582
Loans to staff	463,307	203,732
Loans to executive officers	30,700	54,901
	<hr/>	<hr/>
	20,313,557	11,012,215
Allowance for loan impairment	(268,561)	(171,769)
	<hr/>	<hr/>
<b>Net loans and advances</b>	<b>20,044,996</b>	<b>10,840,446</b>

Included in the gross balance of loans and advances is an amount of non-performing loans of MNT210 million (2003: MNT247 million).

Movements in the allowance for loan losses during the year are as follows:

	<b>Specific</b> <b>allowances</b> <b>MNT'000</b>	<b>General</b> <b>allowances</b> <b>MNT'000</b>	<b>Total</b> <b>MNT'000</b>
<b>Allowance for loan losses</b>			
At 1 January 2003	15,199	54,600	69,799
Charge for the year	62,026	53,053	115,079
Written off	(13,109)	<hr/>	(13,109)
At 31 December 2003	64,116	107,653	171,769
Charge for the year	172,729	93,385	266,114
Written back	(2,188)	-	(2,188)
Written off	(167,134)	-	(167,134)
At 31 December 2004	<hr/> <b>67,523</b>	<hr/> <b>201,038</b>	<hr/> <b>268,561</b>

**XacBank LLC****Notes to the financial statements for the year ended 31 December 2004 (continued)****5. Loans and advances (continued)**

Loans and advances can be analysed by industry as follows:

	<b>2004</b>	<b>2003</b>
	<b>MNT'000</b>	<b>MNT'000</b>
Textile and production	1,722,440	771,066
Trading	9,726,531	5,188,031
Food processing	531,917	314,608
Services	1,554,131	717,099
Consumption	5,239,542	2,298,856
Others	1,044,989	1,463,922
Loans to staff	463,307	203,732
Loans to executive officers	30,700	54,901
	<hr/>	<hr/>
	20,313,557	11,012,215
	<hr/>	<hr/>

Others include borrowers in construction, mining and education.

**XacBank LLC****Notes to the financial statements for the year ended 31 December 2004 (continued)****6. Property, plant and equipment**

	<b>Buildings</b>	<b>Motor vehicles</b>	<b>Office equipment</b>	<b>Computers</b>	<b>Construction in progress</b>	<b>Total</b>
	<b>MNT'000</b>	<b>MNT'000</b>	<b>MNT'000</b>	<b>MNT'000</b>	<b>MNT'000</b>	<b>MNT'000</b>
<b>Cost</b>						
At 1 January 2004	451,459	348,355	260,151	644,785	36,000	1,740,750
Additions	514,852	252,206	130,519	179,881	233,820	1,311,278
Disposals	(22,704)	(21,257)	(2,961)	(1,049)	-	(47,971)
Transfer	-	-	(2,196)	-	-	(2,196)
At 31 December 2004	943,607	579,304	385,513	823,617	269,820	3,001,861
<b>Accumulated depreciation</b>						
At 1 January 2004	23,317	55,407	73,057	202,670	-	354,451
Charge for the year	15,695	41,782	3,859	159,622	-	220,958
Disposals	(2,223)	(7,393)	(490)	(267)	-	(10,373)
Transfer	-	-	(682)	-	-	(682)
At 31 December 2004	36,789	89,796	75,744	362,025	-	564,354
<b>Net book value</b>						
At 31 December 2004	906,818	489,508	309,769	461,592	269,820	2,437,507
At 31 December 2003	428,142	292,948	187,094	442,115	36,000	1,386,299
Depreciation charge for year ended 31 December 2003	11,472	27,280	43,960	85,843	-	168,555

During the year, certain office equipment were transferred to other assets.

**XacBank LLC****Notes to the financial statements for the year ended 31 December 2004 (continued)****7. Other assets**

	<b>2004</b> <b>MNT'000</b>	<b>2003</b> <b>MNT'000</b>
Foreclosed properties	-	32,698
Prepaid expenses	637,131	284,717
Supplies and low value assets	253,444	156,171
Accrued interest receivable	391,544	206,722
Other receivables	219,578	46,876
	<hr/>	<hr/>
	1,501,697	727,184
	<hr/>	<hr/>

Foreclosed properties and other receivables are presented net of impairment loss amounting to MNT1,500,000 and MNT4,738,000 respectively (2003: MNT330,000 and MNT1,227,000)

During the year, foreclosed properties and other receivables amounting to MNT98,000 and MNT141,000 respectively are written off against the impairment losses.

**8. Deposits from customers**

	<b>2004</b> <b>MNT'000</b>	<b>2003</b> <b>MNT'000</b>
Current accounts	1,364,484	880,022
Demand deposits	3,398,260	1,816,232
Time deposits	10,933,685	7,315,918
	<hr/>	<hr/>
	15,696,429	10,012,172
	<hr/>	<hr/>

Current accounts bear interest at a rate of 3.6% (2003: 3.6%) per annum applicable to individual balances more than MNT5 million. Demand deposits bear interest at a rate of approximately 6% (2003: 8.60%) per annum. Time deposits bear interest at rates ranging from 4.2% to 18% (2003: 3.60% to 18.00%) per annum.

**XacBank LLC****Notes to the financial statements for the year ended 31 December 2004 (continued)****9. Loans from local financial institutions**

	<b>2004</b>	<b>2003</b>
	<b>MNT'000</b>	<b>MNT'000</b>
Loan from Anod Bank	-	280,000
Loan from MongolPost Bank	1,600,000	400,000
Loan from Golomt Bank	1,800,000	1,000,000
Loan from UB City Bank	181,350	-
	<hr/>	<hr/>
	3,581,350	1,680,000
	<hr/>	<hr/>

The loans bear interest at rates ranging from 7% to 16% per annum and are repayable in 2005.

**10. Loans from foreign financial institutions**

	<b>2004</b>	<b>2003</b>
	<b>MNT'000</b>	<b>MNT'000</b>
Loan from Deutsche Bank Micro Credit Development Fund ("DBMCDF")	151,125	146,000
Loan from International Finance Corporation ("IFC")	483,600	467,200
Loan from Dexia Micro Credit Fund ("DMCF")	604,500	584,000
Loan from Credit Suisse Microfinance Fund ("CSMF")	604,500	-
Loan from Calvert Social Investment Foundation ("CSIF")	241,800	-
Loan from Microvest 1, LP	1,813,500	-
Loan from ASN-Novib Fonds	1,209,000	-
	<hr/>	<hr/>
	5,108,025	1,197,200
	<hr/>	<hr/>

The loan from the DBMCDF is in the form of subordinated debt issued by the Bank for a principal amount of USD125,000. The loan bears interest at a rate of 2% (2003: 2%) per annum and is repayable in August 2007.

The loan from IFC, amounting to USD400,000, bears interest at rate of LIBOR+3.5% (2003: LIBOR+3.5%). The loan is repayable in twelve semi-annual instalments commencing 15 January 2005.

The loan from DMCF is in the form of a promissory note issued by the Bank for a principal amount of USD500,000. The note bears interest at a rate of LIBOR+6% (2003: LIBOR+6%) per annum. The loan is repayable in four equal two-monthly instalments of USD125,000 each, commencing in February 2006.

**XacBank LLC****Notes to the financial statements for the year ended 31 December 2004 (continued)****10. Loans from foreign financial institutions (continued)**

The loan from CSMF is in the form of a promissory note issued by the Bank for a principal amount of USD500,000. The note bears interest at a rate of LIBOR+6% per annum. The loan is repayable in four equal two-monthly instalments of USD125,000 each, commencing in June 2005.

The loan from CSIF is in the form of a promissory note issued by the Bank for a principal amount of USD200,000. The note bears interest at a rate of 6% per annum and is repayable in January 2007.

The loan from Microvest, amounting to USD1,500,000, bears interest at a rate of LIBOR+5.21%. The loan is repayable in three equal instalments commencing March 2006.

The loan from ASN-Novib Fonds, amounting to USD1,000,000, bears interest at a rate of 9% per annum. The loan is repayable in three instalments commencing in May 2006.

These loans are to support further expansion of the Bank's micro-finance and small-medium enterprise lending activities and to strengthen the Bank's technical capability.

**11. Loans from government agencies**

	<b>2004</b>	<b>2003</b>
	<b>MNT'000</b>	<b>MNT'000</b>
Loan from Employment Generation Support Fund	500,000	445,000
Loan from Asian Development Bank (ADB)	493,169	260,956
Loan from United Nations Development Funds (UNDP)	150,289	150,289
Loan from Micro Finance Development Fund	237,711	-
Loan from International Foundation for Agricultural Development	267,730	-
	<hr/>	<hr/>
	1,648,899	856,245
	<hr/>	<hr/>

The objective of the loan from Employment Generation Support Fund is to channel funds to small business entities and individuals. The loan, which is in Mongolian Tugrug, bear interest at a rate of 6% (2003: 6%) per annum and is repayable on 23 May 2005.

The ADB loan was channelled through the Bank of Mongolia. The objective of the loan is to develop Mongolia's agricultural sector. The loan, which is in Mongolia Tugrug, bears interest of 5.5% (2003: 5.5%) per annum and is repayable from 19 May 2004.

## **XacBank LLC**

### **Notes to the financial statements for the year ended 31 December 2004 (continued)**

#### **11. Loans from government agencies (continued)**

The UNDP loan was channelled through the Bank of Mongolia. The objective of the loan is to develop Mongolia's credit and saving cooperatives. The loan, which is in Mongolian Tugrug, bears interest of 6% (2003: 6%) per annum and is repayable from 15 January 2006.

The objective of the loan from Micro Finance Development Fund is to support and improve the living standard in the rural areas. The loan, which is in Mongolian Tugrug, bears interest at a rate of 5% per annum and is repayable from September 2005 to June 2006.

The objective of the loan from International Foundation for Agricultural Development is to support and reduce the poverty in the rural areas. The loan, which amounted to USD1,823,380, is disbursed from March 2004 to June 2009. It bears interest at a rate of LIBOR + 3.5% per annum and is repayable in 10 equal semi-annual instalments commencing from January 2013.

#### **12. Deferred grants**

	<b>2004</b>	<b>2003</b>
	<b>MNT'000</b>	<b>MNT'000</b>
Grant from Consultative Group to Assist the Poorest ("CGAP")	30,732	46,557
Grant from International Finance Corporation ("IFC")	7,584	38,872
Others	2,919	2,936
	<hr/>	<hr/>
	41,235	88,365
	<hr/>	<hr/>

The CGAP grant was approved in 2001 with the objective of assisting the X.A.C. Co., Ltd in making a successful transition to a micro-finance bank. The grant allows the Bank to carry out the following activities:

- Develop internal systems that meet the requirements and needs of a micro-finance bank;
- Secure higher standard of external audit services; and
- Strengthen senior management and governance, in particular, financial management and banking skills.

The IFC grant was received during 2002 with the objective of providing funds for technical assistance in the following initiatives: technical advice, training for senior managers with an established micro-finance institution and participation by an international participant in the meetings of the Bank's Board of Directors and training for the Bank's Board members.

**XacBank LLC****Notes to the financial statements for the year ended 31 December 2004 (continued)****13. Other liabilities**

	<b>2004</b> <b>MNT'000</b>	<b>2003</b> <b>MNT'000</b>
Interest payable	353,232	299,941
Remittances payable	16,006	248,492
Other payables	262,840	255,429
	<hr/>	<hr/>
	632,078	803,862
	<hr/> <hr/>	<hr/> <hr/>

**14. Share capital**

<i>In number of shares</i>	<b>2004</b>	<b>2003</b>
In issue at 1 January	3,004,000	300,400
Issued for cash	940,000	-
Capitalisation of retained profits	261,530	-
	<hr/>	<hr/>
In issue at 31 December – fully paid	4,205,530	300,400
	<hr/> <hr/>	<hr/> <hr/>

During the year, the Bank's shares were split at a ratio of 1 common share of MNT10,000 each to 10 common shares of MNT1,000 each. The authorised share capital of the Bank had also increased from MNT4,000 million to MNT6,000 million, which consists of 6,000,000 common shares of MNT1,000 per share.

The Bank increased its share capital during the year as follows:

- (a) The issue of 940,000 common shares of MNT1,000 each for a total consideration of MNT948,551,000.
- (b) The issue of 261,530 common shares of MNT 1,000 each by the capitalisation of retained profits of MNT261,530,000.

The holders of ordinary shares are entitled to receive dividends as declared from time to time and are entitled to one vote per share at shareholders meetings of the Bank. All shares rank equally with regard to the Bank's residual assets.

As at 31 December 2004, 94% (2003: 96%) of the issued shares are owned by XAC-GE, the holding company, and 6% (2003: 4%) are owned by other shareholders.

**XacBank LLC****Notes to the financial statements for the year ended 31 December 2004 (continued)****15. Interest income**

	<b>2004</b>	<b>2003</b>
	<b>MNT'000</b>	<b>MNT'000</b>
Loans and advances	5,746,713	3,573,322
Balances with other banks	93,212	98,258
Investment securities	96,493	43,931
	<hr/>	<hr/>
	5,936,418	3,715,511
	<hr/> <hr/>	<hr/> <hr/>

**16. Interest expense**

	<b>2004</b>	<b>2003</b>
	<b>MNT'000</b>	<b>MNT'000</b>
Deposits from customers	1,456,743	973,179
Loans	517,834	195,509
	<hr/>	<hr/>
	1,974,577	1,168,688
	<hr/> <hr/>	<hr/> <hr/>

**17. Net fees and commissions income**

	<b>2004</b>	<b>2003</b>
	<b>MNT'000</b>	<b>MNT'000</b>
Fees and commissions income	400,065	218,398
Fees and commissions expenses	(15,170)	(5,903)
	<hr/>	<hr/>
	384,895	212,495
	<hr/> <hr/>	<hr/> <hr/>

Net fees and commissions income includes loan application fees, payment service fees, loan commissions and money transfer service fees.

**XacBank LLC****Notes to the financial statements for the year ended 31 December 2004 (continued)****18. Other operating income**

	<b>2004</b> <b>MNT'000</b>	<b>2003</b> <b>MNT'000</b>
Rental income	74,527	117,670
Other income	34,131	34,260
	<hr/>	<hr/>
	108,658	151,930
	<hr/> <hr/>	<hr/> <hr/>

Included in other income are gains from disposal of property and equipment, penalty income, etc.

**19. General and administrative expenses**

	<b>2004</b> <b>MNT'000</b>	<b>2003</b> <b>MNT'000</b>
Salaries, provision for staff welfare and bonus	1,210,368	922,244
Depreciation on property, plant and equipment	220,958	168,555
Travel	164,431	83,571
Rental	350,040	329,255
Representation	67,187	39,040
Fuel and maintenance of vehicles	121,740	77,367
Communication	134,274	111,341
Advertising	96,364	68,389
Maintenance of property, plant and equipment	11,748	12,797
Office supplies	114,297	96,744
Social insurance	231,390	177,003
Other	262,343	198,105
	<hr/>	<hr/>
	2,985,140	2,284,411
	<hr/> <hr/>	<hr/> <hr/>

**20. Impairment losses**

	<b>2004</b> <b>MNT'000</b>	<b>2003</b> <b>MNT'000</b>
Loans and advances (allowance for loan losses)	263,926	115,079
Other assets	4,920	8,085
Investment securities	6,045	-
	<hr/>	<hr/>
	274,891	123,164
	<hr/> <hr/>	<hr/> <hr/>

**XacBank LLC****Notes to the financial statements for the year ended 31 December 2004 (continued)****21.Dividend**

	<b>2004</b> <b>MNT'000</b>	<b>2003</b> <b>MNT'000</b>
Ordinary:		
Interim paid	262,000	228,403

During the year, an interim dividend amounting to MNT262,000,000 was declared of which MNT261,530,000 was capitalised as share capital and the remaining MNT470,000 was paid in cash.

A final dividend of MNT127,000,000 has been proposed subsequent to the year end and has not been accounted for in the financial statements.

**22. Corporate income tax****Recognised in the statement of income:**

	<b>2004</b> <b>MNT'000</b>	<b>2003</b> <b>MNT'000</b>
<i>Current tax expense</i>		
Current year	423,085	228,403
Over provided in prior years	-	(2,060)
Income tax expense in the statement of income	423,085	226,343

**Reconciliation of effective tax rate**

	<b>2004</b> <b>MNT'000</b>	<b>2003</b> <b>MNT'000</b>
Profit before tax	1,210,579	503,222
Tax at income tax rate of 15%	181,587	75,483
Tax effect of non-deductible expenses	48,278	16,835
Tax effect of tax exempt revenues	-	(576)
Under/(over) provided in prior years	-	(2,060)
Tax effect of progressive tax rate of 30% (2003: 40%) on the portion of taxable income exceeding MNT100 million	193,220	136,661
Income tax expense	423,085	226,343

The calculation of income tax is subject to the review and approval of the tax authorities.

According to Mongolian Tax Laws, the Company has an obligation to pay the Government Income Tax at the rate of 15% (2003: 15%) of the portion of taxable profits up to MNT100 million and 30% (2003: 40%) of the portion of taxable profits above MNT100 million.

## XacBank LLC

### Notes to the financial statements for the year ended 31 December 2004 (continued)

## 23. Employee benefits

### *Equity compensation benefits*

Under the Bank's Employee Stock Ownership Plan, shares are allocated to employees on the following conditions:

- Employment duration with the Bank and its predecessor companies must be at least one year;
- Performance rating in the most recent evaluation period; and
- No disciplinary action is pending or due.

The number of shares offered for sale and its price will be determined at the discretion of the Bank's Board. For 2004, the shares were offered at a price of 30% of the par value. The Plan enables employees to purchase shares in XacBank LLC already held by XAC-GE. The share capital of XacBank LLC is not affected by these transactions.

The shares are purchased within the financial year in which they are offered.

	<b>Movement of shares offered under the Plan (expressed in number of shares)</b>	
	<b>2004</b>	<b>2003</b>
Share offer vested during the year	166,100	10,160
Shares offered outstanding at 1 January	-	-
Shares offered during the year	166,100	10,160
Shares offered and purchased during the year	(67,729)	(8,030)
Shares offered and expired during the year	(98,371)	(2,130)
Shares offered outstanding at 31 December	-	-

The Bank does not bear or incur any cost in connection with these transactions.

**XacBank LLC****Notes to the financial statements for the year ended 31 December 2004 (continued)****24. Significant transactions with related parties**

The Bank has a controlling related party relationship with XAC-GE, the holding company.

The Bank also has a related party relationship with the shareholders of XAC-GE (see note 1), and with its directors and executive officers.

As at 31 December 2004, executive officers held 10,298 (2003: 3,200) voting shares of the Bank.

During the year the Bank had the following transactions with related parties:

	<b>2004</b> <b>MNT'000</b>	<b>2003</b> <b>MNT'000</b>
Loans to executive officers	30,700 =====	54,901 =====

Total remuneration of directors and executive officers included in general and administrative expenses:

	<b>2004</b> <b>MNT'000</b>	<b>2003</b> <b>MNT'000</b>
Directors	52,832	3,050
Executive officers	76,542	80,264
	<hr/> 129,374	<hr/> 83,314
	<hr/> <hr/>	<hr/> <hr/>

**XacBank LLC****Notes to the financial statements for the year ended 31 December 2004 (continued)****25. Capital adequacy**

The Bank of Mongolia requires banks to maintain a minimum capital adequacy ratio of 10%, compiled on the basis of total equity and total assets as adjusted for their risk. As at 31 December 2004, the Bank's core capital ratio and risk weighted capital ratio are 19% (2003: 24%) and 19% (2003: 24%) respectively.

Components of Tier I and Tier II capital:

	<b>2004</b>	<b>2003</b>
	<b>MNT'000</b>	<b>MNT'000</b>
<b>Tier I capital</b>		
Share capital	4,205,530	3,004,000
Share premium	8,551	-
General reserve	13,864	9,436
Retained earnings	631,907	106,413
	<hr/>	<hr/>
Total capital	4,859,852	3,119,849
<b>Tier II capital</b>	-	-
	<hr/>	<hr/>
Total Tier I and Tier II capital	4,859,852	3,119,849

Breakdown of risk weighted assets as follows:

	<b>2004</b>	<b>2003</b>
	<b>MNT'000</b>	<b>MNT'000</b>
<b>Risk weighted factor (%)</b>		
0	2,813,955	3,705,708
10	-	-
20	4,204,447	1,143,765
50	-	-
100	25,116,231	12,953,929
	<hr/>	<hr/>
Total	31,604,816	17,803,402

## **26. Risk management disclosure**

This section provides details of the Bank's exposure to risk and describes the methods used by management to control risk. Because of the Bank's activities, which are predominantly non-trading, assets structure consists mainly of loans and advances, and their financing, which is mainly from deposits from customers. The most important types of financial risk to which the Bank is exposed are credit risk, liquidity risk, interest rate risk and, to a less extent, foreign currency risk.

Below is a discussion of these risks and the approach taken to manage them:

### **(i) Credit risk**

The Bank's primary exposure to credit risk arises through its loans and advances. The amount of credit risk exposure in this regard is represented by the carrying amounts of the assets on the balance sheet.

The Bank structures the level of credit risk it undertakes by placing limits on the amount of risk acceptable to one individual borrower or a group of borrowers and to an industry sector. Exposure to credit risk is managed through regular analysis of the ability of the borrowers and potential borrowers to meet interest and capital repayment obligations. Credit limit is changed when needed. Exposure to credit risk is also managed by obtaining collateral and corporate and personal guarantees.

The major concentration of credit risk arises by industry sector in relation to the Bank's loans and advances to customers. See note 5 for analysis of total loans and advances to customers by industry sector. The Bank has no significant exposure to any individual borrower.

### **(ii) Liquidity risk**

Liquidity risk arises in the general funding of the Bank's activities and in the management of its positions. It includes both risk of being unable to fund assets at appropriate maturities and rates and risk of being unable to liquidate an asset at a reasonable price in an appropriate time frame.

The Bank has access to a diverse funding base. Funds are raised using a broad range of instruments including deposits, interest-bearing borrowings from local and overseas financial institutions and share capital. This enhances funding flexibility and limits dependence on any source of funds or any fund provider. The Bank continually assesses liquidity risk by identifying and monitoring changes in funding required to meet business goals and targets set in terms of the overall strategy.

In addition, the Bank holds a portfolio of liquid assets as part of its liquidity risk management policy.

**XacBank LLC****Notes to the financial statements for the year ended 31 December 2004 (continued)****26. Risk management disclosure (continued)**

The following table provides an analysis of the financial assets and liabilities of the Bank into relevant maturity groupings based on the remaining periods to repayment:

*As at 31 December 2004*

	<b>Less than three months MNT'000</b>	<b>Three to six months MNT'000</b>	<b>Six months to one year MNT'000</b>	<b>One to five years MNT'000</b>	<b>Over five years MNT'000</b>	<b>Total MNT'000</b>
<b>Financial assets</b>						
Cash on hand	1,052,516	-	-	-	-	1,052,516
Balances with other banks	2,995,447	-	1,209,000	-	-	4,204,447
Balances with the Bank of Mongolia	1,392,439	-	-	-	-	1,392,439
Investment securities	366,714	-	598,455	-	-	965,169
Loans and advances	8,423,303	6,284,705	4,332,179	1,004,809	-	20,044,996
Other assets	1,050,109	432,979	16,628	1,981	-	1,501,697
	<b>15,280,528</b>	<b>6,717,684</b>	<b>6,156,262</b>	<b>1,006,790</b>	<b>-</b>	<b>29,161,264</b>
<b>Financial liabilities</b>						
Deposits from customers	7,993,024	1,613,958	2,851,687	1,051,469	2,186,291	15,696,429
Loans from local financial institutions	981,350	800,000	1,800,000	-	-	3,581,350
Loans from foreign financial institutions	779,805	1,233,180	1,662,375	1,432,665	-	5,108,025
Loans from government agencies	153,825	627,493	406,170	193,681	267,730	1,648,899
Other liabilities	332,301	66,303	233,474	-	-	632,078
	<b>10,240,305</b>	<b>4,340,934</b>	<b>6,953,706</b>	<b>2,677,815</b>	<b>2,454,021</b>	<b>26,666,781</b>
Net financial assets/(liabilities)	<b>5,040,223</b>	<b>2,376,750</b>	<b>(797,444)</b>	<b>(1,671,025)</b>	<b>(2,454,021)</b>	<b>2,494,483</b>
Cumulative total	<b>5,040,223</b>	<b>7,416,973</b>	<b>6,619,529</b>	<b>4,948,504</b>	<b>2,494,483</b>	

**XacBank LLC****Notes to the financial statements for the year ended 31 December 2004 (continued)****26. Risk management disclosure (continued)***As at 31 December 2003*

	<b>Less than three months MNT'000</b>	<b>Three to six months MNT'000</b>	<b>Six months to one year MNT'000</b>	<b>One to five years MNT'000</b>	<b>Over five years MNT'000</b>	<b>Total MNT'000</b>
<b>Financial assets</b>						
Cash on hand	637,419	-	-	-	-	637,419
Balances with other banks	63,365	350,400	-	730,000	-	1,143,765
Balances with the Bank of Mongolia	1,121,497	-	-	-	-	1,121,497
Investment securities	1,946,792	-	-	-	-	1,946,792
Loans and advances	1,314,462	2,726,718	5,911,499	887,767	-	10,840,446
Other assets	470,782	-	83,900	172,502	-	727,184
	5,554,317	3,077,118	5,995,399	1,790,269	-	16,417,103
<b>Financial liabilities</b>						
Deposits from customers	2,713,309	1,661,750	4,156,326	421,240	1,059,547	10,012,172
Loans from local financial institutions	-	400,000	280,000	1,000,000	-	1,680,000
Loans from foreign financial institutions	-	-	-	1,010,320	186,880	1,197,200
Loan from government agencies	-	452,500	215,320	188,425	-	856,245
Other liabilities	642,955	-	61,859	99,048	-	803,862
	3,356,264	2,514,250	4,713,505	2,719,033	1,246,427	14,549,479
Net financial assets/(liabilities)	2,198,053	562,868	1,281,894	(928,764)	(1,246,427)	1,867,624
Cumulative total	2,198,053	2,760,921	4,042,815	3,114,051	1,867,624	

**XacBank LLC**

**Notes to the financial statements for the year ended 31 December 2004 (continued)**

**26. Risk management disclosure (continued)**

*(iii) Interest rate risk*

The Bank's operations are subject to the risk of interest rate fluctuations to the extent that interest-earning assets and interest-bearing liabilities mature or re-price at different times or in different amounts. In the case of floating rate assets and liabilities the Bank is also exposed to basis risk, which is the difference in re-pricing characteristics of the various floating rate indices, such as six months LIBOR and different types of interest. Risk management activities are aimed at optimising net interest income, given market interest rate levels consistent with the Bank's business strategies.

Assets-liabilities risk management activities are conducted in the context of the Bank's sensitivity to interest rate changes. Interest rate risk is managed by increasing or decreasing positions within limits set by the Bank's management. These limits restrict the potential effect of movement in interest rates on interest margin and on the value of interest sensitive assets and liabilities.

The table below summarises re-pricing mismatches on the Bank's financial assets and liabilities at the balance sheet date. The carrying amounts of interest rate sensitive assets and liabilities are presented in the periods in which they next re-price to market rate or mature, and are summed to show the interest rate sensitivity gap.

**XacBank LLC**

**Notes to the financial statements for the year ended 31 December 2004 (continued)**

**26. Risk management disclosure (continued)**

*As at 31 December 2004*

	Effective interest rate %	Total MNT'000	Non-interest sensitive MNT'000	Less than three months MNT'000	Three to six months MNT'000	Six months to one year MNT'000	One to five years MNT'000	Over five years MNT'000
<b>Financial assets</b>								
Cash on hand	-	1,052,516	1,052,516	-	-	-	-	-
Balances with other banks	6.63%	4,204,447	93,847	2,901,600	-	1,209,000	-	-
Balances with the Bank of Mongolia	-	1,392,439	1,392,439	-	-	-	-	-
Investment securities	12.66%	965,169	-	366,714	-	598,455	-	-
Loans and advances	35.79%	20,044,996	-	8,423,303	6,284,705	4,332,179	1,004,809	-
Other assets	-	1,501,697	1,501,697	-	-	-	-	-
		29,161,264	4,040,499	11,691,617	6,284,705	6,139,634	1,004,809	-
<b>Financial liabilities</b>								
Deposits from customers	12.00%	15,696,429	-	7,993,024	4,851,718	2,851,687	-	-
Loans from local financial institutions	14.82%	3,581,350	-	981,350	800,000	1,800,000	-	-
Loans from foreign financial institutions	8.06%	5,108,025	-	3,506,100	-	-	1,601,925	-
Loans from government agencies	6.30%	1,648,899	-	153,825	627,493	406,170	193,681	267,730
Other liabilities	-	632,078	632,078	-	-	-	-	-
		26,666,781	632,078	12,634,299	6,279,211	5,057,857	1,795,606	(267,730)
Net financial assets/(liabilities)		2,494,483	3,408,421	(942,682)	5,494	1,081,777	(790,797)	(267,730)

**XacBank LLC**

**Notes to the financial statements for the year ended 31 December 2004 (continued)**

**26. Risk management disclosure (continued)**

*As at 31 December 2003*

	Effective interest rate	Total MNT'000	Non-interest sensitive MNT'000	Less than three months MNT'000	Three to six months MNT'000	Six months to one year MNT'000	One to five years MNT'000	Over five years MNT'000
<b>Financial assets</b>								
Cash on hand	-	637,419	637,419	-	-	-	-	-
Balances with other banks	5.36%	1,143,765	63,365	-	350,400	-	730,000	-
Balances with the Bank of Mongolia	-	1,121,497	1,121,497	-	-	-	-	-
Investment securities	8.46%	1,946,792	-	1,946,792	-	-	-	-
Loans and advances	39.02%	10,840,446	-	1,314,462	2,726,718	5,911,499	887,767	-
Other assets	-	727,184	727,184	-	-	-	-	-
		16,417,103	2,549,465	3,261,254	3,077,118	5,911,499	1,617,767	-
<b>Financial liabilities</b>								
Deposits from customers	10.8%	10,012,172	-	2,713,309	1,661,750	5,637,113	-	-
Loans from local financial institutions	14.02%	1,680,000	-	-	400,000	280,000	1,000,000	-
Loans from foreign financial institutions	5.41%	1,197,200	-	1,051,200	-	-	146,000	-
Loans from government agencies	5.85%	856,245	-	-	452,500	215,320	188,425	-
Other liabilities	-	803,862	803,862	-	-	-	-	-
		14,549,479	803,862	3,764,509	2,514,250	6,132,433	1,334,425	-
Net financial assets/(liabilities)		1,867,624	1,745,603	(503,255)	562,868	(220,934)	283,342	-

**XacBank LLC****Notes to the financial statements for the year ended 31 December 2004 (continued)****26. Risk management disclosure (continued)***(iv) Foreign currency risk*

The Bank is exposed to foreign currency risk through transactions in foreign currencies, primarily in USD. The Bank's management sets limits on the level of exposure by currencies. These limits have been set below the minimum requirements of the Bank of Mongolia.

The Bank's transactional exposures comprise the monetary assets and monetary liabilities that are not denominated in the measurement currency. These exposures are as follows:

	31 December 2004			31 December 2003		
	MNT denominated MNT'000	Foreign currencies MNT'000	Total MNT'000	MNT denominated MNT'000	Foreign currencies MNT'000	Total MNT'000
<b>Financial assets</b>						
Cash on hand	824,686	227,830	1,052,516	517,222	120,197	637,419
Balances with other banks	38,125	4,166,322	4,204,447	36,052	1,107,713	1,143,765
Balances with the Bank of Mongolia	1,250,932	141,507	1,392,439	700,923	420,574	1,121,497
Investment securities	366,714	598,455	965,169	1,946,792	-	1,946,792
Loans and advances	18,480,739	1,564,257	20,044,996	10,321,670	518,776	10,840,446
Other assets	1,077,184	424,513	1,501,697	445,305	281,879	727,184
	<b>22,038,380</b>	<b>7,122,884</b>	<b>29,161,264</b>	<b>13,967,964</b>	<b>2,449,139</b>	<b>16,417,103</b>
<b>Financial liabilities</b>						
Deposits from customers	13,515,959	2,180,470	15,696,429	9,382,519	629,653	10,012,172
Loans from local financial institutions	3,581,350	-	3,581,350	1,680,000	-	1,680,000
Loans from foreign financial institutions	-	5,108,025	5,108,025	-	1,197,200	1,197,200
Loans from government agencies	1,381,169	267,730	1,648,899	856,245	-	856,245
Other liabilities	399,007	233,071	632,078	353,791	450,071	803,862
	<b>18,877,485</b>	<b>7,789,296</b>	<b>26,666,781</b>	<b>12,272,555</b>	<b>2,276,924</b>	<b>14,549,479</b>
Net financial assets/(liabilities)	3,160,895	(666,412)	2,494,483	1,695,409	172,215	1,867,624

**XacBank LLC**

**Notes to the financial statements for the year ended 31 December 2004 (continued)**

**27. Fair value information**

As there is no active market for a large part of the Bank's financial instruments, judgement is necessary in estimating fair value, based on current economic conditions and specific risk attributable to the instrument. Based on these estimates, fair value of financial assets and liabilities are considered to not differ significantly from their carrying amount. The following methods and assumptions are used in estimating the fair value of financial instruments:

**(i) Loans and advances**

The fair value of the loan portfolio is based on the credit and interest rate characteristics of each individual loan. The estimation of the provision for loan losses includes consideration of risk premium applicable to various types of loans based on factors such as the current situation of the borrower and collateral obtained. Accordingly, the provision for loan losses is considered a reasonable estimate of the discount required to reflect the impact of the credit risk. The carrying amount of loans is a reasonable estimate of their fair value.

**(ii) Deposits from customers**

For demand deposits and deposits with no defined maturity, fair value is taken to be the amount payable on demand at the balance sheet date. The estimated fair value of fixed-maturity deposits is based on discounted cash flows using rates currently offered for deposits of similar remaining maturities. As most of the deposits have original maturity of less than one year and the rates offered by the Bank are similar to the market rate, the carrying amount of deposits is considered to be a reasonable estimate of fair value.

**(iii) Other financial assets and financial liabilities**

The majority of other financial assets and financial liabilities of the Bank matures or re-prices in less than one year. Accordingly, their fair values do not significantly differ from their respective carrying amounts.

**28. Commitments**

	<b>2004</b>	<b>2003</b>
	<b>MNT'000</b>	<b>MNT'000</b>
Property, plant and equipment		
Contracted but not provided for in the financial statements	2,418,000	-
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