

JSC Progress Bank
Financial Statements

Period from 30 November 2007
(date of establishment) to 31 December 2008
Together with Independent Auditors' Report

CONTENTS

INDEPENDENT AUDITORS' REPORT

Balance sheet.....	1
Statement of operations.....	2
Statement of changes in equity.....	3
Cash flow statement.....	4

NOTES TO FINANCIAL STATEMENTS

1. Principal activities.....	5
2. Basis of preparation.....	5
3. Summary of significant accounting policies.....	5
4. Significant accounting judgements and estimates.....	10
5. Cash and cash equivalents.....	11
6. Loans to customers.....	11
7. Property and equipment.....	12
8. Intangible assets.....	13
9. Taxation.....	13
10. Amounts due to customers.....	14
11. Other assets and liabilities.....	14
12. Subordinated debt.....	14
13. Equity.....	15
14. Commitments and contingencies.....	15
15. Other income.....	16
16. Personnel and other operating expenses.....	16
17. Net fee and commission income.....	16
18. Risk management.....	16
19. Maturity analysis of assets and liabilities.....	22
20. Fair value of financial instruments.....	22
21. Related party disclosures.....	23
22. Capital adequacy.....	24

INDEPENDENT AUDITORS' REPORT

To the Shareholder and Board of Directors of JSC Progress Bank –

We have audited the accompanying financial statements of JSC Progress Bank, which comprise the balance sheet as at 31 December 2008, and the statement of operations, statement of changes in equity and cash flow statement for the period from 30 November 2007 (date of establishment) to 31 December 2008, and a summary of significant accounting policies and other explanatory notes.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with International Financial Reporting Standards. This responsibility includes: designing, implementing and maintaining internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error; selecting and applying appropriate accounting policies; and making accounting estimates that are reasonable in the circumstances.

Auditors' Responsibility

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 comply with ethical requirements and plan and perform the audit to obtain reasonable assurance whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditors' judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the financial statements present fairly, in all material respects, the financial position of JSC Progress Bank as at 31 December 2008, and its financial performance and its cash flows for the period from 30 November 2007 (date of establishment) to 31 December 2008 in accordance with International Financial Reporting Standards.

31 March 2009

BALANCE SHEET**As of 31 December 2008***(Thousands of Georgian Lari)*

	<i>Notes</i>	<i>2008</i>
Assets		
Cash and cash equivalents	5	6,462
Loans to customers	6	2,844
Deferred income tax assets	9	95
Property and equipment	7	3,443
Intangible assets	8	196
Other assets	11	197
Total assets		13,237
Liabilities		
Amounts due to customers	10	274
Other liabilities	11	72
Subordinated debt	12	1,436
Total liabilities		1,782
Equity		
Share capital	13	12,000
Net loss for the period		(545)
Total equity		11,455
Total liabilities and equity		13,237

Signed and authorised for release on behalf of the Management Board of the Bank

Konstantine Sulamanidze

Chief Executive Officer

Akaki Kordzadze

Head of Financial Department

31 March 2009

The accompanying notes on pages 5 to 24 are an integral part of these financial statements.

STATEMENT OF OPERATIONS**Period from 30 November 2007 (date of establishment) to 31 December 2008***(Thousands of Georgian Lari)*

	<i>Notes</i>	<i>2008</i>
Interest income		
Amounts due from credit institutions		629
Investment securities		578
Loans to customers		29
		<u>1,236</u>
Interest expense		
Subordinated debt		(39)
		<u>1,197</u>
Net interest income		1,197
Loan impairment charge		(76)
		<u>1,121</u>
Net interest income after loan impairment charge	6	1,121
Net gains/(losses) from foreign currencies:		
- dealing		(10)
- translation differences		413
Other income	15	6
Non-interest income		<u>407</u>
Personnel expenses	16	(1,380)
Depreciation and amortisation	7, 8	(219)
Net fee and commission expense	17	(166)
Other operating expenses	16	(405)
Non-interest expenses		<u>(2,170)</u>
Loss before income tax		(640)
Income tax benefit	9	95
Net loss for the period		<u><u>(545)</u></u>

Signed and authorised for release on behalf of the Management Board of the Bank

Konstantine Sulamanidze

Chief Executive Officer

Akaki Kordzadze

Head of Financial Department

31 March 2009

The accompanying notes on pages 5 to 24 are an integral part of these financial statements.

STATEMENT OF CHANGES IN EQUITY**Period from 30 November 2007 (date of establishment) to 31 December 2008***(Thousands of Georgian Lari)*

	<i>Share capital</i>	<i>Net loss for the period</i>	<i>Total equity</i>
30 November 2007 (date of establishment)	–	–	–
Issuance of share capital (Note 13)	12,000		12,000
Net loss for the period		(545)	(545)
31 December 2008	12,000	(545)	11,455

The accompanying notes on pages 5 to 24 are an integral part of these financial statements.

CASH FLOW STATEMENT**Period from 30 November 2007 (date of establishment) to 31 December 2008***(Thousands of Georgian Lari)*

	<u>Notes</u>	<u>2008</u>
Cash flows from operating activities		
Interest received		1,219
Interest paid		(4)
Fees and commissions received		8
Foreign currency dealing losses		(10)
Other income received	16	6
Salaries and employment benefits paid	17	(1,380)
Administrative expenses paid		(328)
Other operating expenses paid		(76)
Fee and commission expenses paid		(174)
Cash flows used in operating activities before changes in operating assets and liabilities		(739)
<i>Net (increase) decrease in operating assets</i>		
Loans to customers		(2,682)
Other assets		(77)
<i>Net increase (decrease) in operating liabilities</i>		
Amounts due to customers		292
Other liabilities		72
Net cash used in operating activities before income tax		(2,395)
Income taxes paid		(120)
Net cash used in operating activities		(2,515)
Cash flows from investing activities		
Purchase of property and equipment	7	(3,658)
Purchase of intangible assets	8	(200)
Net cash used in investing activities		(3,858)
Cash flows from financing activities		
Contribution of share capital	13	12,000
Payment of subordinated debt		(155)
Proceeds from subordinated debt		1,555
Net cash from financing activities		13,400
Effect of exchange rates changes on cash and cash equivalents		174
Net increase in cash and cash equivalents		6,462
Cash and cash equivalents, beginning		-
Cash and cash equivalents, ending		6,462

The accompanying notes on pages 5 to 24 are an integral part of these financial statements.

(Thousands of Georgian Lari)

1. Principal activities

JSC Progress Bank (the “Bank”) was established on 30 November 2007 as a joint stock company with registration number N1-22159 under the laws of the Republic of Georgia. The Bank operates under a general banking licence No. N0110244 issued by the National Bank of Georgia (“NBG”; the central bank) on 31 December 2007, and NBG licences for operations with precious metals and foreign currencies.

The Bank accepts deposits from the public and extends credit, transfers payments in Georgia and abroad, exchanges currencies and provides other banking services to its customers. The Bank does not have branches or other operating outlets. The Bank’s registered legal address is 8 Baratashvili St, Tbilisi, Georgia.

As of 31 December 2008, the Bank is wholly-owned by JSC Kala Capital, which is also the ultimate parent of the Bank. The ultimate parent is controlled by an individual - Kakha Kaladze.

As of 31 December 2008, members of the Board of Directors and Management Board did not hold shares of the Bank.

2. Basis of preparation

These financial statements have been prepared in accordance with International Financial Reporting Standards (“IFRS”).

The Bank is required to maintain its records and prepare its financial statements for regulatory purposes in Georgian Lari in accordance with International Financial Reporting Standards (IFRS). These financial statements cover the period from 30 November 2007 (date of establishment) to 31 December 2008 which is longer than 12 months, as the Bank has effectively commenced full banking operations in 2008.

The financial statements have been prepared under the historical cost convention except as disclosed in the accounting policies below.

These financial statements are presented in thousands of Georgian Lari (“GEL”), unless otherwise indicated.

3. Summary of significant accounting policies

Financial assets

Initial recognition

Financial assets in the scope of IAS 39 are classified as either financial assets at fair value through profit or loss, loans and receivables, held-to-maturity investments, or available-for-sale financial assets, as appropriate. When financial assets are recognised initially, they are measured at fair value, plus, in the case of investments not at fair value through profit or loss, directly attributable transaction costs. The Bank determines the classification of its financial assets upon initial recognition, and subsequently can reclassify financial assets in certain cases as described below.

Date of recognition

All regular way purchases and sales of financial assets are recognised on the trade date i.e. the date that the Bank commits to purchase or sell the asset. Regular way purchases or sales are purchases or sales of financial assets that require delivery of assets within the period generally established by regulation or convention in the marketplace.

Day 1’ profit

Where the transaction price in a non-active market is different to the fair value from other observable current market transactions in the same instrument or based on a valuation technique whose variables include only data from observable markets, the Bank immediately recognises the difference between the transaction price and fair value (a ‘Day 1’ profit) in the income statement. In cases where use is made of data which is not observable, the difference between the transaction price and model value is only recognised in the income statement when the inputs become observable, or when the instrument is derecognised.

(Thousands of Georgian Lari)

3. Summary of significant accounting policies (continued)

Financial assets at fair value through profit or loss

Financial assets classified as held for trading are included in the category 'financial assets at fair value through profit or loss'. Financial assets are classified as held for trading if they are acquired for the purpose of selling in the near term.

Loans and receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. They are not entered into with the intention of immediate or short-term resale and are not classified as trading securities or designated as investment securities available-for-sale. Such assets are carried at amortised cost using the effective interest method. Gains and losses are recognised in the income statement when the loans and receivables are derecognised or impaired, as well as through the amortisation process.

Determination of fair value

For all other financial instruments not listed in an active market, the fair value is determined by using appropriate valuation techniques. Valuation techniques include net present value techniques, comparison to similar instruments for which market observable prices exist, options pricing models and other relevant valuation models.

Offsetting

Financial assets and liabilities are offset and the net amount is reported in the balance sheet when there is a legally enforceable right to set off the recognised amounts and there is an intention to settle on a net basis, or to realise the asset and settle the liability simultaneously. This is not generally the case with master netting agreements, and the related assets and liabilities are presented gross in the balance sheet.

Reclassification of Financial Assets

Amendments to IAS 39 "Financial instruments: Recognition and measurement" and IFRS 7 "Financial instruments: Disclosures"

Amendments to IAS 39 and IFRS 7 were issued on 13 October 2008 and allow reclassification of non-derivative financial assets out of the held for trading category in particular circumstances. The amendments also allow transfer of certain financial assets from the available for sale category to loans and receivables category. The effective date of those amendments is 1 July 2008. Any reclassification made in periods beginning on or after 1 November 2008 shall take effect only from the date when the reclassification is made. The disclosures about reclassifications made are presented in Notes 8 and 13. The Bank did not reclassify any financial assets from held for trading or available for sale categories and hence these amendments did not have any impact on the financial position or performance of the Bank.

Cash and cash equivalents

Cash and cash equivalents consist of cash on hand, amount due from the NBG, excluding obligatory reserves, and amounts due from credit institutions that mature within ninety days of the date of origination and are free from contractual encumbrances.

Borrowings

Issued financial instruments or their components are classified as liabilities, where the substance of the contractual arrangement results in the Bank having an obligation either to deliver cash or another financial asset to the holder, or to satisfy the obligation other than by the exchange of a fixed amount of cash or another financial asset for a fixed number of own equity instruments. Such instruments include amounts due to customers and subordinated debt. After initial recognition, borrowings are subsequently measured at amortised cost using the effective interest method. Gains and losses are recognised in the income statement when the borrowings are derecognised as well as through the amortisation process.

Leases

Operating - Bank as lessee

Leases of assets under which the risks and rewards of ownership are effectively retained by the lessor are classified as operating leases. Lease payments under an operating lease are recognised as expenses on a straight-line basis over the lease term and included into other operating expenses.

(Thousands of Georgian Lari)

3. Summary of significant accounting policies (continued)

Impairment of financial assets

The Bank assesses at each balance sheet date whether there is any objective evidence that a financial asset or a group of financial assets is impaired. A financial asset or a group of financial assets is deemed to be impaired if, and only if, there is objective evidence of impairment as a result of one or more events that has occurred after the initial recognition of the asset (an incurred 'loss event') and that loss event (or events) has an impact on the estimated future cash flows of the financial asset or the group of financial assets that can be reliably estimated. Evidence of impairment may include indications that the borrower or a group of borrowers is experiencing significant financial difficulty, default or delinquency in interest or principal payments, the probability that they will enter bankruptcy or other financial reorganisation and where observable data indicate that there is a measurable decrease in the estimated future cash flows, such as changes in arrears or economic conditions that correlate with defaults.

Loans to customers

For loans to customers carried at amortised cost, the Bank first assesses individually whether objective evidence of impairment exists individually for financial assets that are individually significant, or collectively for financial assets that are not individually significant. If the Bank determines that no objective evidence of impairment exists for an individually assessed financial asset, whether significant or not, it includes the asset in a group of financial assets with similar credit risks characteristics and collectively assesses them for impairment. Assets that are individually assessed for impairment and for which an impairment loss is, or continues to be, recognised are not included in a collective assessment of impairment.

If there is an objective evidence that an impairment loss has been incurred, the amount of the loss is measured as the difference between the assets' carrying amount and the present value of estimated future cash flows (excluding future expected credit losses that have not yet been incurred). The carrying amount of the asset is reduced through the use of an allowance account and the amount of the loss is recognised in the income statement. Interest income continues to be accrued on the reduced carrying amount based on the original effective interest rate of the asset. Loans together with the associated allowance are written off when there is no realistic prospect of future recovery and all collateral has been realised or has been transferred to the Bank. If, in a subsequent year, the amount of the estimated impairment loss increases or decreases because of an event occurring after the impairment was recognised, the previously recognised impairment loss is increased or reduced by adjusting the allowance account. If a future write-off is later recovered, the recovery is credited to the income of operations statement.

The present value of the estimated future cash flows is discounted at the financial asset's original effective interest rate. If a loan has a variable interest rate, the discount rate for measuring any impairment loss is the current effective interest rate. The calculation of the present value of the estimated future cash flows of a collateralised financial asset reflects the cash flows that may result from foreclosure less costs for obtaining and selling the collateral, whether or not foreclosure is probable.

For the purpose of a collective evaluation of impairment, financial assets are grouped on the basis of the Bank's internal credit grading system that considers credit risk characteristics such as asset type, industry, geographical location, collateral type, past-due status and other relevant factors.

Future cash flows on a group of financial assets that are collectively evaluated for impairment are estimated on the basis of historical loss experience for assets with credit risk characteristics similar to those in the group. Historical loss experience is adjusted on the basis of current observable data to reflect the effects of current conditions that did not affect the years on which the historical loss experience is based and to remove the effects of conditions in the historical period that do not exist currently. Estimates of changes in future cash flows reflect, and are directionally consistent with, changes in related observable data from year to year (such as changes in unemployment rates, property prices, commodity prices, payment status, or other factors that are indicative of incurred losses in the group or their magnitude). The methodology and assumptions used for estimating future cash flows are reviewed regularly to reduce any differences between loss estimates and actual loss experience.

(Thousands of Georgian Lari)

3. Summary of significant accounting policies (continued)

Financial guarantees

In the ordinary course of business, the Bank gives financial guarantees, consisting of letters of credit, guarantees and acceptances. Financial guarantees are initially recognised in the financial statements at fair value, in 'Other liabilities', being the premium received. Subsequent to initial recognition, the Bank's liability under each guarantee is measured at the higher of the amortised premium and the best estimate of expenditure required settling any financial obligation arising as a result of the guarantee.

Any increase in the liability relating to financial guarantees is taken to the income of operations statement. The premium received is recognised in the statement of operations on a straight-line basis over the life of the guarantee.

Taxation

The current income tax expense is calculated in accordance with the regulations in force in the Republic of Georgia.

Deferred tax assets and liabilities are calculated in respect of temporary differences using the liability method. Deferred income taxes are provided for all temporary differences arising between the tax bases of assets and liabilities and their carrying values for financial reporting purposes, except where the deferred income tax arises from the initial recognition of goodwill or of an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit nor taxable profit or loss.

A deferred tax asset is recorded only to the extent that it is probable that taxable profit will be available against which the deductible temporary differences can be utilised. Deferred tax assets and liabilities are measured at tax rates that are expected to apply to the period when the asset is realised or the liability is settled, based on tax rates that have been enacted or substantively enacted at the balance sheet date.

Deferred income tax is provided on temporary differences arising on investments in subsidiaries, associates and joint ventures, except where the timing of the reversal of the temporary difference can be controlled and it is probable that the temporary difference will not reverse in the foreseeable future.

Georgia also has various operating taxes that are assessed on the Bank's activities. These taxes are included as a component of other operating expenses.

Property and equipment

Property and equipment are carried at cost less accumulated depreciation and any accumulated impairment in value. Such cost includes the cost of replacing part of equipment when that cost is incurred if the recognition criteria are met. Buildings are measured at fair value less depreciation and impairment charged subsequent to the date of the revaluation.

The carrying values of property and equipment are reviewed for impairment when events or changes in circumstances indicate that the carrying value may not be recoverable.

Depreciation of an asset begins when it is available for use. Depreciation is calculated on a straight-line basis over the following estimated useful lives:

	<u>Years</u>
Building	50
Furniture and fixtures	5
Computers and office equipment	5
Motor vehicles	5

Leasehold improvements are amortized over the life of the related leased asset.

Costs related to repairs and renewals are charged when incurred and included in other operating expenses, unless they qualify for capitalization.

(Thousands of Georgian Lari)

3. Summary of significant accounting policies (continued)

Intangible assets

Intangible assets include computer software and licences.

Intangible assets acquired separately are measured on initial recognition at cost. The cost of intangible assets acquired in a business combination is fair value as at the date of acquisition. Following initial recognition, intangible assets are carried at cost less any accumulated amortisation and any accumulated impairment losses. The useful lives of intangible assets are assessed to be either finite or indefinite. Intangible assets with finite lives are amortised over the useful economic lives and assessed for impairment whenever there is an indication that the intangible asset may be impaired. Amortisation periods for intangible assets with indefinite useful lives are reviewed at least at each financial year-end.

Provisions

Provisions are recognised when the Bank has a present legal or constructive obligation as a result of past events, and it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation and a reliable estimate of the amount of obligation can be made.

Retirement and other employee benefit obligations

The Bank does not have any pension arrangements separate from the State pension system of the Georgia, which requires current contributions by the employer calculated as a percentage of current gross salary payments; such expense is charged in the period the related salaries are earned. In addition, the Bank has no post-retirement benefits or significant other compensated benefits requiring accrual.

Share capital

Share capital

Ordinary shares are classified as share capital in equity. Any excess of the fair value of consideration received over the par value of shares issued is recognised as additional paid-in capital.

Contingencies

Contingent liabilities are not recognised in the balance sheet but are disclosed unless the possibility of any outflow in settlement is remote. A contingent asset is not recognised in the balance sheet but disclosed when an inflow of economic benefits is probable.

Recognition of income and expenses

Revenue is recognised to the extent that it is probable that the economic benefits will flow to the Bank and the revenue can be reliably measured. The following specific recognition criteria must also be met before revenue is recognised:

Interest and similar income and expense

For all financial instruments measured at amortised cost and interest bearing securities classified as trading or available-for-sale, interest income or expense is recorded at the effective interest rate, which is the rate that exactly discounts estimated future cash payments or receipts through the expected life of the financial instrument or a shorter period, where appropriate, to the net carrying amount of the financial asset or financial liability. The calculation takes into account all contractual terms of the financial instrument and includes any fees or incremental costs that are directly attributable to the instrument and are an integral part of the effective interest rate, but not future credit losses. The carrying amount of the financial asset or financial liability is adjusted if the Bank revises its estimates of payments or receipts. The adjusted carrying amount is calculated based on the original effective interest rate and the change in carrying amount is recorded as interest income or expense.

Once the recorded value of a financial asset or a group of similar financial assets has been reduced due to an impairment loss, interest income continues to be recognised using the original effective interest rate applied to the new carrying amount.

(Thousands of Georgian Lari)

3. Summary of significant accounting policies (continued)

Fee and commission income

Fees earned for the provision of services over a period of time are accrued over that period. These fees include commission income and asset management, custody and other management and advisory fees. Loan commitment fees for loans that are likely to be drawn down and other credit related fees are deferred (together with any incremental costs) and recognised as an adjustment to the effective interest rate on the loan.

Functional and reporting currencies and foreign currency translation

The financial statements are presented in Georgian Lari, which is the Bank's functional and presentation currency. Transactions in foreign currencies are initially recorded in the functional currency, converted at the rate of exchange ruling at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies are retranslated at the functional currency rate of exchange ruling at the balance sheet date. Gains and losses resulting from the translation of foreign currency transactions are recognised in the statement of operations as gains less losses from foreign currencies - translation differences. Non-monetary items that are measured in terms of historical cost in a foreign currency are translated using the exchange rates as at the dates of the initial transactions. Non-monetary items measured at fair value in a foreign currency are translated using the exchange rates at the date when the fair value was determined.

Differences between the contractual exchange rate of a transaction in a foreign currency and the NBG exchange rate on the date of the transaction are included in gains less losses from dealing in foreign currencies. The official NBG exchange rates at 31 December 2008 and 30 November 2007 were 1.6670 GEL and 1.6210 GEL to 1 USD, respectively.

Future changes in accounting policies

Standards and interpretations issued but not yet effective

Improvements to IFRS

In May 2008, the IASB issued amendments to IFRS, which resulted from the IASB's annual improvements project. They comprise amendments that result in accounting changes for presentation, recognition or measurement purposes as well as terminology or editorial amendments related to a variety of individual IFRS standards. Most of the amendments are effective for annual periods beginning on or after 1 January 2009, with earlier application permitted. The Bank is currently evaluating the potential impact that the adoption of the amendments will have on its financial statements.

IAS 23 "Borrowing Costs"(Revised)

A revised IAS 23 Borrowing costs was issued in March 2007, and becomes effective for financial years beginning on or after 1 January 2009. The standard has been revised to require capitalisation of borrowing costs when such costs relate to a qualifying asset. A qualifying asset is an asset that necessarily takes a substantial period of time to get ready for its intended use or sale. In accordance with the transitional requirements in the Standard, the Bank will adopt this as a prospective change. Accordingly, borrowing costs will be capitalised on qualifying assets with a commencement date after 1 January 2009. No changes will be made for borrowing costs incurred to this date that have been expensed.

4. Significant accounting judgements and estimates

Estimation uncertainty

In the process of applying the Bank's accounting policies, management has used its judgements and made estimates in determining the amounts recognised in the financial statements. The most significant use of judgements and estimates are as follows:

Fair value of financial instruments

Where the fair values of financial assets and financial liabilities recorded on the balance sheet cannot be derived from active markets, they are determined using a variety of valuation techniques that include the use of mathematical models. The input to these models is taken from observable markets where possible, but where this is not feasible, a degree of judgement is required in establishing fair values.

(Thousands of Georgian Lari)

4. Significant accounting judgements and estimates (continued)

Allowance for loan impairment

The Bank regularly reviews its loans and receivables to assess impairment. The Bank uses its experienced judgement to estimate the amount of any impairment loss in cases where a borrower is in financial difficulties and there are few available sources of historical data relating to similar borrowers. Similarly, the Bank estimates changes in future cash flows based on the observable data indicating that there has been an adverse change in the payment status of borrowers in a group, or national or local economic conditions that correlate with defaults on assets in the group. Management uses estimates based on historical loss experience for assets with credit risk characteristics and objective evidence of impairment similar to those in the group of loans and receivables. The Bank uses its experienced judgement to adjust observable data for a group of loans or receivables to reflect current circumstances.

5. Cash and cash equivalents

	<i>2008</i>
Cash on hand	527
Current account with the National Bank of Georgia	68
Current accounts with other credit institutions	2,856
Time deposit with credit institution up to 90 days	3,011
Cash and cash equivalents	6,462

Time deposit with credit institution is placed with a Georgian bank with maturity of 13 days.

6. Loans to customers

	<i>2008</i>
Corporate loans	2,884
Consumer loans	35
Gross loans	2,919
Less – Allowance for impairment	(75)
Loans to customers, net	2,844

Allowance for impairment of loans to customers

A reconciliation of the allowance for impairment of loans to customers by class is as follows:

	<i>Corporate loans 2008</i>	<i>Consumer loans 2008</i>	<i>Total 2008</i>
At 30 November 2007	-	-	-
Charge for the period	74	1	75
At 31 December 2008	74	1	75
Individual impairment	-	-	-
Collective impairment	74	1	75
	74	1	75
Gross amount of loans, individually determined to be impaired, before deducting any individually assessed impairment allowance	-	-	-

*(Thousands of Georgian Lari)***6. Loans to customers (continued)***Concentration of loans to customers*

As of 31 December 2008, the Bank had issued 19 loans to its customers. From these 19 loans, 6 were provided to corporate customers. 5 loans to corporate customers represent the largest part of total gross portfolio (98.8%). A collective allowance of GEL 73 was recognised against these loans.

Loans have been extended to the following types of customers:

	<i>2008</i>
Private companies	2,884
Individuals	35
Total Loans (Gross)	2,919
Less: Allowance for impairment	(75)
Total Loans (Net)	2,844

Loans are made within Georgia in the following industry sectors:

	<i>2008</i>
Services	1,438
Micro-financing	845
Real estate construction	601
Individuals	35
Total Loans (Gross)	2,919
Less: Allowance for impairment	(75)
Total Loans (Net)	2,844

7. Property and equipment

The movements in property and equipment were as follows:

	<i>Buildings</i>	<i>Furniture and fixtures</i>	<i>Computers and office equipment</i>	<i>Motor vehicles</i>	<i>Assets under construction</i>	<i>Total</i>
Cost						
30 November 2007	-	-	-	-	-	-
Additions	1,988	793	394	357	126	3,658
31 December 2008	1,988	793	394	357	126	3,658
Accumulated depreciation						
30 November 2007	-	-	-	-	-	-
Depreciation charge	31	19	36	11	118	215
31 December 2008	31	19	36	11	118	215
Net book value:						
30 November 2007	-	-	-	-	-	-
31 December 2008	1,957	774	358	346	8	3,443

(Thousands of Georgian Lari)

8. Intangible assets

The movements in intangible assets were as follows:

	<i>Licenses</i>	<i>Computer software</i>	<i>Total</i>
Cost			
30 November 2007	-	-	-
Additions	110	90	200
31 December 2008	110	90	200
Accumulated amortization			
30 November 2007	-	-	-
Amortisation charge	3	1	4
31 December 2008	3	1	4
Net book value:			
30 November 2007	-	-	-
31 December 2008	107	89	196

9. Taxation

The corporate income tax expense (benefit) comprises:

	<i>2008</i>
Current tax expense	-
Deferred tax benefit – origination and reversal of temporary differences	(95)
Income tax benefit	(95)

Georgian legal entities must individually report taxable income and remit profit taxes thereon to the appropriate authorities. The tax rate for banks for profits other than on state securities was 15% in 2008 and 20% in 2007. The tax rate for interest income on state securities was 10%.

The effective income tax rate differs from the statutory income tax rates. As of 31 December 2008 a reconciliation of income tax expense based on statutory tax rates with actual is as follows:

	<i>2008</i>
Loss before income tax	(640)
Statutory tax rate	15%
Theoretical income tax expense/(benefit) at the statutory rate	(96)
- Non-deductible expenditure	1
Income tax benefit	(95)

Deferred tax assets and liabilities as of 31 December 2008 and their movements for the period comprise:

	<i>Origination and reversal of temporary differences</i>			<i>31 December 2008</i>
	<i>30 November 2007 (date of establishment)</i>	<i>In the income statement</i>	<i>Directly in equity</i>	
Tax effect of deductible temporary differences:				
Tax loss carried forward	-	(133)	-	(133)
Other liabilities	-	(9)	-	(9)
Deferred tax assets	-	142	-	142
Tax effect of taxable temporary differences:				
Property and equipment	-	44	-	44
Other assets	-	3	-	3
Deferred tax liabilities	-	47	-	47
Deferred tax assets - net	-	95	-	95

The Bank has available GEL 887 of tax loss carry forward which will expire in 2013.

(Thousands of Georgian Lari)

10. Amounts due to customers

Amounts due to customers of Gel 274 as of 31 December 2008 are comprised of customer current deposits. GEL 257 (93.5% of total deposits) was due to corporate customers (8 out of 33 customers).

Amounts due to customers include accounts with the following types of customers:

	<u>2008</u>
Private enterprises	257
Employees	10
Individuals	7
Amounts due to customers	<u>274</u>

An analysis of customer accounts by economic sector follows:

	<u>2008</u>
Real estate construction	220
Trade	36
Individuals and employees	17
Energy	1
Amounts due to customers	<u>274</u>

11. Other assets and liabilities

Other assets comprise:

	<u>2008</u>
Other prepaid taxes	120
Prepayments	73
Obligatory reserve in NBG	4
Total other assets	<u>197</u>

Credit institutions in Georgia are required to maintain a non-interest earning cash deposit (obligatory reserve) with the NBG, the amount of which depends on the level of funds attracted by the credit institution. The Bank's ability to withdraw these deposits is restricted by the statutory legislature.

Other liabilities comprise:

	<u>2008</u>
Accounts payable	38
Property tax payable	17
Advances received	7
VAT payable	5
Withholding tax payable	5
Total other liabilities	<u>72</u>

12. Subordinated debt

As of 31 December 2008 subordinated debt of GEL 1,436 represents an unsecured GEL-denominated long-term debt from JSC Kala Capital, sole shareholder of the Bank. On 17 July 2008 the Bank signed a subordinated debt agreement with JSC Kala Capital for GEL 1,400 at an interest rate of 7% per annum maturing on 14 July 2016. In the event of bankruptcy or liquidation of the Bank, repayment of this loan is subordinate to the repayment of the Bank's liabilities to all other creditors.

(Thousands of Georgian Lari)

13. Equity

As of 31 December 2008 the number of authorised, issued and paid-up ordinary shares is 12,000,000 with a nominal value per share of GEL 1. All the shares were purchased at the amount equal to the par value.

Movements in shares outstanding, issued and fully paid were as follows:

	Number of shares	Nominal value of shares	Total
30 November 2007	-	-	-
Increase in share capital	12,000	1	12,000
31 December 2007 and 2008	12,000	1	12,000

The share capital of the Bank was contributed by the shareholder in Georgian Lari and is entitled to dividends and any capital distribution in Georgian Lari.

14. Commitments and contingencies

Operating environment

As an emerging market, Georgia does not possess a well-developed business and regulatory infrastructure that would generally exist in a more mature market economy. Operations in Georgia may involve risks that are not typically associated with those in developed markets (including the risk that the Georgian Lari is not freely convertible outside of the country, and undeveloped debt and equity markets). However over the last few years the Georgian government has made a number of developments that positively affect the overall investment climate of the country, specifically implementing the reforms necessary to create banking, judicial, taxation and regulatory systems. This includes the adoption of a new body of legislation (including new Tax Code and procedural laws). In management's view, these steps contribute to mitigate the risks of doing business in Georgia.

The existing tendency aimed at the overall improvement of the business environment is expected to persist. The future stability of the Georgian economy is largely dependent upon these reforms and developments and the effectiveness of economic, financial and monetary measures undertaken by the Government. However, the Georgian economy is vulnerable to market downturns and economic slowdowns elsewhere in the world. During the year there have been major events that have an effect on the Bank's operations – the military conflict in August 2008 involving Georgia, the Russian Federation and South Ossetia, and the financial crisis which significantly affected global economies from last quarter of 2008. Though no direct damage has been sustained by the Bank during the military conflict, it had caused significant damage to the Georgian economy and the Fitch and S&P country ratings were downgraded. The ongoing global financial crisis and the military conflict have resulted in capital markets instability, deterioration of liquidity in the banking sector, and tighter credit conditions within Georgia. The Georgian Government has introduced a range of stabilization measures aimed at ensuring solvency and providing liquidity and supporting refinancing of foreign debt for Georgian banks and companies.

While management believes it is taking appropriate measures to support the sustainability of the Bank's business in the current circumstances, unexpected further deterioration in the areas described above could negatively affect the Bank's results and financial position in a manner not currently determinable.

Legal

In the ordinary course of business, the Bank is subject to legal actions and complaints. Management believes that the ultimate liability, if any, arising from such actions or complaints will not have a material adverse effect on the financial condition or the results of future operations of the Bank.

Commitments and contingencies

As of 31 December 2008 the Bank's commitments and contingencies comprised guarantees issued amounting to GEL 501.

*(Thousands of Georgian Lari)***15. Other income**

Other income of GEL 6 is comprised of income from guarantees of GEL 5 and fines of GEL 1 .

16. Personnel and other operating expenses

Personnel and other operating expenses comprise:

	<u>2008</u>
Salaries and bonuses	1,270
Social benefit expenses	100
Vacation and sick leave	10
Personnel expenses	<u>1,380</u>
Advertising	74
Taxes other than income tax	73
Lease expense	64
Vehicle expenses (excluding repair expenses)	47
Office supplies and stationery	51
Business trips	21
Utilities	11
Entertainment	11
Postal	9
Real estate insurance	7
Building security	2
Employee uniform expense	2
Cash packing	1
Other expenses	32
Other operating expenses	<u>405</u>

17. Net fee and commission expense

Net fee and commission expense comprises:

	<u>2008</u>
Settlements operations	3
Other	5
Fee and commission income	<u>8</u>
Settlements operations	(173)
Other	(1)
Fee and commission expense	<u>(174)</u>
Net fee and commission expense	<u>(166)</u>

18. Risk management**Introduction**

Risk is inherent in the Bank's activities but it is managed through a process of ongoing identification, measurement and monitoring, subject to risk limits and other controls. This process of risk management is critical to the Bank's continuing profitability and each individual within the Bank is accountable for the risk exposures relating to his or her responsibilities. The Bank is exposed to credit risk, liquidity risk and market risk, the latter being subdivided into trading and non-trading risks. It is also subject to operational risks.

The independent risk control process does not include business risks such as changes in the environment, technology and industry. They are monitored through the Bank's strategic planning process.

(Thousands of Georgian Lari)

18. Risk management (continued)

Introduction (continued)

Risk management structure

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

Board of Directors

The Board of Directors is responsible for the overall risk management approach and for approving the risk strategies and principles.

Management Board

The Management Board has the responsibility to monitor the overall risk process within the Bank.

Risk Committee

The Risk Committee has the overall responsibility for the development of the risk strategy and implementing principles, frameworks, policies and limits. It is responsible for the fundamental risk issues and manages and monitors relevant risk decisions.

Bank Treasury

Bank Treasury is responsible for managing the Bank's assets and liabilities and the overall financial structure. It is also primarily responsible for the funding and liquidity risks of the Bank.

Internal Audit

Risk management processes throughout the Bank are audited annually by the internal audit function that examines both the adequacy of the procedures and the Bank's compliance with the procedures. Internal Audit discusses the results of all assessments with management, and reports its findings and recommendations to the Audit Committee.

Risk measurement and reporting systems

The Bank's risks are measured using a method which reflects both the expected loss likely to arise in normal circumstances and unexpected losses, which are an estimate of the ultimate actual loss based on statistical models. The models make use of probabilities derived from historical experience, adjusted to reflect the economic environment. The Bank also runs worst case scenarios that would arise in the event that extreme events which are unlikely to occur do, in fact, occur.

Monitoring and controlling risks is primarily performed based on limits established by the Bank. These limits reflect the business strategy and market environment of the Bank as well as the level of risk that the Bank is willing to accept, with additional emphasis on selected industries. In addition the Bank monitors and measures the overall risk bearing capacity in relation to the aggregate risk exposure across all risks types and activities.

Information compiled from all the businesses is examined and processed in order to analyse, control and identify early risks. This information is presented and explained to the Management Board, the Risk Committee, and the head of each business division. The report includes aggregate credit exposure, credit metric forecasts and hold limit exceptions. On a monthly basis detailed reporting of industry, customer and geographic risks takes place. Senior management assesses the appropriateness of the allowance for credit losses on a quarterly basis. The Board of Directors receives a comprehensive risk report once a quarter which is designed to provide all the necessary information to assess and conclude on the risks of the Bank.

For all levels throughout the Bank, specifically tailored risk reports are prepared and distributed in order to ensure that all business divisions have access to extensive, necessary and up-to-date information.

A daily briefing is given to the Management Board and all other relevant employees of the Bank on the utilisation of market limits, proprietary investments and liquidity, plus any other risk developments.

(Thousands of Georgian Lari)

18. Risk management (continued)

Risk mitigation

As part of its overall risk management, the Bank uses certain financial instruments to manage exposures resulting from changes in interest rates, foreign currencies, equity risks, credit risks, and exposures arising from forecast transactions.

The Bank actively uses collateral to reduce its credit risks (see below for more detail).

Excessive risk concentration

Concentrations arise when a number of counterparties are engaged in similar business activities, or activities in the same geographic region, or have similar economic features that would cause their ability to meet contractual obligations to be similarly affected by changes in economic, political or other conditions. Concentrations indicate the relative sensitivity of the Bank's performance to developments affecting a particular industry or geographical location.

In order to avoid excessive concentrations of risks, the Bank's policies and procedures include specific guidelines to focus on maintaining a diversified portfolio. Identified concentrations of credit risks are controlled and managed accordingly.

Credit risk

Credit risk is the risk that the Bank will incur a loss because its customers, clients or counterparties failed to discharge their contractual obligations. The Bank manages and controls credit risk by setting limits on the amount of risk it is willing to accept for individual counterparties and for geographical and industry concentrations, and by monitoring exposures in relation to such limits.

The Bank has established a credit quality review process to provide early identification of possible changes in the creditworthiness of counterparties, including regular collateral revisions. Counterparty limits are established by the use of a credit risk classification system, which assigns each counterparty a risk rating. Risk ratings are subject to regular revision. The credit quality review process allows the Bank to assess the potential loss as a result of the risks to which it is exposed and take corrective action.

Credit-related commitments risks

The Bank makes available to its customers guarantees which may require that the Bank make payments on their behalf. Such payments are collected from customers based on the terms of the letter of credit. They expose the Bank to similar risks to loans and these are mitigated by the same control processes and policies.

The table below shows the maximum exposure to credit risk for the components of the balance sheet, including derivatives. The maximum exposure is shown gross, before the effect of mitigation through the use of master netting and collateral agreements.

	<i>Notes</i>	<i>Maximum exposure 2008</i>
Cash and cash equivalents (excluding cash on hand)	5	5,935
Loans to customers	6	2,844
Other assets	11	197
		8,976
Financial commitments and contingencies	14	501
Total credit risk exposure		9,477

Where financial instruments are recorded at fair value, the amounts shown above represent the current credit risk exposure but not the maximum risk exposure that could arise in the future as a result of changes in values.

(Thousands of Georgian Lari)

18. Risk management (continued)

Credit risk (continued)

Credit quality per class of financial assets

The credit quality of financial assets is managed by the Bank internal credit ratings. The table below shows the credit quality by class of asset for loan-related balance sheet lines, based on the Bank's credit rating system.

	<i>Notes</i>	<i>Neither past due nor impaired</i>			<i>Past due or individually impaired 2008</i>	<i>Total 2008</i>
		<i>High grade 2008</i>	<i>Standard grade 2008</i>	<i>Sub-standard grade 2008</i>		
Cash equivalents	5	3,011	-	-	-	3,011
Loans to customers	6					
Corporate		2,884	-	-	-	2,884
Consumer		35	-	-	-	35
Total		5,930	-	-	-	5,930

It is the Bank's policy to maintain accurate and consistent risk ratings across the credit portfolio. The attributable risk ratings are assessed and updated regularly.

The credit risk assessment policy for non-past due and individually non-impaired financial assets has been determined by the Bank as follows:

A financial asset with average overdue days of less than or equal to 10 days is assessed as a financial asset with High Grade;

A financial asset with average overdue days of more than 10 days and less than or equal to 20 days is assessed as a financial asset with Standard Grade;

A financial asset with average overdue days of more than 20 days and less than or equal to 90 days is assessed as a financial asset with Substandard Grade.

During the year 2008 the Bank did not have either past due or impaired loans in its loan portfolio.

Impairment assessment

The main considerations for the loan impairment assessment include whether any payments of principal or interest are overdue by more than 90 days or there are any known difficulties in the cash flows of counterparties, credit rating downgrades, or infringement of the original terms of the contract. The Bank addresses impairment assessment in two areas: individually assessed allowances and collectively assessed allowances.

Individually assessed allowances

The Bank determines the allowances appropriate for each individually significant loan on an individual basis. Items considered when determining allowance amounts include the sustainability of the counterparty's business plan, its ability to improve performance once a financial difficulty has arisen, projected receipts and the expected dividend payout should bankruptcy ensue, the availability of other financial support and the realisable value of collateral, and the timing of the expected cash flows. The impairment losses are evaluated at each reporting date, unless unforeseen circumstances require more careful attention.

Collectively assessed allowances

Allowances are assessed collectively for losses on loans to customers that are not individually significant (including residential mortgages and unsecured consumer lending) and for individually significant loans where there is not yet objective evidence of individual impairment. Allowances are evaluated on each reporting date with each portfolio receiving a separate review.

(Thousands of Georgian Lari)

18. Risk management (continued)

The collective assessment takes account of impairment that is likely to be present in the portfolio even though there is no yet objective evidence of the impairment in an individual assessment. Impairment losses are estimated by taking into consideration the following information: historical losses on the portfolio, current economic conditions, the appropriate delay between the times a loss is likely to have been incurred and the time it will be identified as requiring an individually assessed impairment allowance, and expected receipts and recoveries once impaired. Local management is responsible for deciding the length of this period which can extend for as long as one year. The impairment allowance is then reviewed by credit management to ensure alignment with the Bank's overall policy.

Financial guarantees and letters of credit are assessed and provision made in a similar manner as for loans.

All monetary assets and liabilities of the Bank are concentrated in Georgia.

Liquidity risk and funding management

Liquidity risk is the risk that the Bank will be unable to meet its payment obligations when they fall due under normal and stress circumstances. To limit this risk, management has arranged diversified funding sources in addition to its core deposit base, manages assets with liquidity in mind, and monitors future cash flows and liquidity on a daily basis. This incorporates an assessment of expected cash flows and the availability of high grade collateral which could be used to secure additional funding if required.

The Bank maintains a portfolio of highly marketable and diverse assets that can be easily liquidated in the event of an unforeseen interruption of cash flow. The Bank also has committed lines of credit that it can assess to meet liquidity needs. In addition, the Bank maintains a cash deposit (obligatory reserve) with the NBG, the amount of which depends on the level of customer funds attracted.

The liquidity position is assessed and managed by the Bank based on certain liquidity ratio established by the NBG. As at 31 December, this ratio was as follows:

Average liquidity ratio for the year	2008, % 586%
--------------------------------------	------------------------

Analysis of financial liabilities by remaining contractual maturities

The table below summarises the maturity profile of the Bank's financial liabilities at 31 December 2008 based on contractual undiscounted repayment obligations. Repayments which are subject to notice are treated as if notice were to be given immediately. However, the Bank expects that many customers will not request repayment on the earliest date the Bank could be required to pay and the table does not reflect the expected cash flows indicated by the Bank's deposit retention history.

Financial liabilities	On demand	Less than 3 months	3 to 12 months	1 to 5 years	Over 5 years	Total
As at 31 December 2008						
Amounts due to customers	274	-	-	-	-	274
Other liabilities	72	-	-	-	-	72
Subordinated debt	-	-	-	-	2,194	2,194
Total undiscounted financial liabilities	346	-	-	-	2,194	2,540

Included in amounts due to customers are term deposits of individuals. In accordance with the Georgian legislation, the Bank is obliged to repay such deposits upon demand of a depositor.

The table below shows the contractual expiry by maturity of the Bank's financial commitments and contingencies.

	Less than 3 months	3 to 12 months	1 to 5 years	Over 5 years	Total
2008	-	-	501	-	501

The Bank expects that not all of the contingent liabilities or commitments will be drawn before expiry of the commitments.

*(Thousands of Georgian Lari)***18. Risk management (continued)****Market risk**

Market risk is the risk that the fair value or future cash flows of financial instruments will fluctuate due to changes in market variables such as interest rates, foreign exchanges, and equity prices. Except for the concentrations in foreign currency, the Bank has no significant concentration of market risk.

Interest rate risk

Interest rate risk arises from the possibility that changes in interest rates will affect future cash flows or the fair values of financial instruments. However, changes in interest rates do not impact any component of the Bank's financial assets or liabilities. All interest-bearing loans and borrowings, loans to customers and cash and cash equivalents have fixed interest rates and therefore management do not believe the Bank is exposed to the interest rate risk from these financial assets and liabilities.

Currency risk

Currency risk is the risk that the value of a financial instrument will fluctuate due to changes in foreign exchange rates. The Management Board has set limits on positions by currency based on the NBG regulations. Positions are monitored on a daily basis.

The tables below indicate the currencies to which the Bank had significant exposure at 31 December 2008 on its non-trading monetary assets and liabilities and its forecast cash flows. The analysis calculates the effect of a reasonably possible movement of the currency rate against the GEL, with all other variables held constant on the income statement (due to the fair value of currency sensitive non-trading monetary assets and liabilities). The effect on equity does not differ from the effect on the income statement. A negative amount in the table reflects a potential net reduction in income statement or equity, while a positive amount reflects a net potential increase.

	GEL	USD	EUR	GBP	Total
Assets					
Cash and cash equivalents	5,049	1,165	240	8	6,462
Loans to customers	2,020	824	-	-	2,844
Deferred tax assets	95	-	-	-	95
Property and equipment	3,443	-	-	-	3,443
Intangible assets	196	-	-	-	196
Other assets	197	-	-	-	197
Total assets	11,000	1,989	240	8	13,237
Liabilities					
Amounts due to customers	30	209	35	-	274
Other liabilities	34	38	-	-	72
Subordinated debt	1,436	-	-	-	1,436
Total Liabilities	1,500	247	35	-	1,782
Equity					
Share capital	12,000	-	-	-	12,000
Accumulated loss	(545)	-	-	-	(545)
Total Equity	11,455	-	-	-	11,455
Net balance sheet position	1,955	1,742	205	8	-
Increase in currency rate in %		8.92%	15.02%	25.22%	
Effect on profit		155	31	2	
Decrease in currency rate in %		-8.92%	15.02%	-25.22%	
Effect on profit		(155)	(31)	(2)	

*(Thousands of Georgian Lari)***18. Risk management (continued)****Operational risk**

Operational risk is the risk of loss arising from systems failure, human error, fraud or external events. When controls fail to perform, operational risks can cause damage to reputation, have legal or regulatory implications, or lead to financial loss. The Bank cannot expect to eliminate all operational risks, but a control framework and monitoring and responding to potential risks could be effective tools to manage the risks. Controls should include effective segregation of duties, access, authorisation and reconciliation procedures, staff education and assessment processes, including the use of internal audit.

19. Maturity analysis of assets and liabilities

The table below shows an analysis of assets and liabilities according to when they are expected to be recovered or settled. See Note 18 "Risk management" for the Bank's contractual undiscounted repayment obligations.

	<i>2008</i>		<i>Total</i>
	<i>Within one year</i>	<i>More than one year</i>	
Cash and cash equivalents	6,462	-	6,462
Loans to customers	2,844	-	2,844
Deferred income tax assets	-	95	95
Property and equipment	-	3,443	3,443
Intangible assets	-	196	196
Other assets	197	-	197
Total	9,503	3,734	13,237
Other liabilities	72	-	72
Amounts due to customers	274	-	274
Subordinated debt	-	1,436	1,436
Total	346	1,436	1,782
Net	9,157	2,298	11,455

20. Fair Values of Financial Instruments

Set out below is a comparison by class of the carrying amounts and fair values of the Bank's financial instruments that are carried in the financial statements. The table does not include the fair values of non-financial assets and non-financial liabilities.

	<i>Carrying value 2008</i>	<i>Fair value 2008</i>	<i>Unrecognised gain/(loss) 2008</i>
Financial assets			
Cash and cash equivalents	5,935	5,935	-
Loans to customers	2,844	2,844	-
Financial liabilities			
Amounts due to customers	273	273	-
Subordinated debt	1,436	1,098	338
Total unrecognised change in unrealised fair value			338

The following describes the methodologies and assumptions used to determine fair values for those financial instruments which are not already recorded at fair value in the financial statements.

*(Thousands of Georgian Lari)***20. Fair Values of Financial Instruments (continued)****Assets for which fair value approximates carrying value**

For financial assets and financial liabilities that are liquid or have a short term maturity (less than three months) it is assumed that the carrying amounts approximate their fair value. This assumption is also applied to demand deposits, savings accounts without a specific maturity and variable rate financial instruments.

Fixed rate financial instruments

The fair value of fixed rate financial assets and liabilities carried at amortised cost are estimated by comparing market interest rates when they were first recognised with current market rates offered for similar financial instruments. The estimated fair value of fixed interest bearing deposits is based on discounted cash flows using prevailing money-market interest rates for debts with similar credit risk and maturity.

21. Related party disclosures

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

Related parties may enter into transactions which unrelated parties might not, and transactions between related parties may not be effected on the same terms, conditions and amounts as transactions between unrelated parties.

The volumes of related party transactions, outstanding balances at the year end, and related expense and income for the year are as follows:

	<i>2008</i>		
	<i>Parent</i>	<i>Entities under common control</i>	<i>Key management personnel</i>
Loans outstanding at 30 November 2007 (date of establishment), gross	-	-	-
Loans issued during the period	-	-	38
Loan repayments during the period	-	-	(2)
Loans outstanding at 31 December 2008, gross	-	-	36
Less: allowance for impairment at 31 December 2008	-	-	(1)
Loans outstanding at 31 December 2008, net	-	-	35
Interest income on loans			1
Deposits at 30 November 2007 (date of establishment)	-	-	-
Deposits received during the year	-	232	11
Deposits at 31 December 2008	-	232	11
Interest expense on deposits	-	2	-
Received subordinated debt at 30 November 2007	-	-	-
Loans received during the period	1,555	-	-
Loan repayments during the period	(155)	-	-
Loans outstanding at 31 December 2008	1,400	-	-
Interest expense on subordinated debt	48	-	-

Compensation of key management personnel was comprised of the following:

	<i>2008</i>
Supervisory Board	438
Board of Directors	290
Total key management compensation	728

(Thousands of Georgian Lari)

22. Capital adequacy

The Bank maintains an actively managed capital base to cover risks inherent in the business. The adequacy of the Bank's capital is monitored using, among other measures, the ratios established by the NBG in supervising the Bank.

During the period the Bank is in compliance with externally imposed capital requirements.

The primary objectives of the Bank's capital management are to ensure that the Bank complies with externally imposed capital requirements and that the Bank maintains strong credit ratings and healthy capital ratios in order to support its business and to maximise shareholders' value.

The Bank manages its capital structure and makes adjustments to it in the light of changes in economic conditions and the risk characteristics of its activities. In order to maintain or adjust the capital structure, the Bank may adjust the amount of dividend payment to shareholders, return capital to shareholders or issue capital securities. No changes were made in the objectives, policies and processes from the previous years.

NBG capital adequacy ratio

The NBG requires banks to maintain a capital adequacy ratio of 12% of risk-weighted assets, computed based on IFRS financial statements. As of 31 December 2008, the Bank's capital adequacy ratio on this basis was as follows:

	<i>2008</i>
Core capital	11,804
Supplementary capital	967
Less: deductions from capital	-
Total capital	12,771
Risk-weighted assets	12,965
Capital adequacy ratio	98.50%

Regulatory capital consists of core capital, which comprises share capital and retained earnings (accumulated loss) including current year profit (loss). Certain adjustments are made to IFRS-based results and reserves, as prescribed by the NBG. The other component of regulatory capital is supplementary capital, which includes subordinated debt.