JSC BasisBank

Financial Statements

For the year ended 31 December 2008

Contents

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Independent Auditors' Report

To the Supervisory Board
JSC BasisBank

Report on the Financial Statements

We have audited the accompanying financial statements of JSC BasisBank (the "Bank"), which comprise the balance sheet as at 31 December 2008, and the income statement, statement of changes in shareholders' equity and statement of cash flows for the year then ended, 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 misstatements, 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 relevant ethical requirements and plan and perform the audit to obtain reasonable assurance whether the financial statements are free of 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 auditor's 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 principles 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 opinion.

Opinion

In our opinion, the financial statements present fairly, in all material respects, the financial position of the Bank as at 31 December 2008, and its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards.

Tbilisi Branch of KPMG CIS Limited
14 May 2008

	Notes	2008 GEL'000	2007 GEL'000
Interest income	4	12,277	10,389
Interest expense	4	(5,414)	(3,887)
Net interest income		**6,863**	**6,502**
Fee and commission income	5	3,864	3,110
Fee and commission expense	6	(1,205)	(710)
Net fee and commission income		**2,659**	**2,400**
Net foreign exchange income	7	1,819	1,632
Other income/(expenses)	8	121	614
		1,940	**2,246**
Impairment (losses)/recoveries	9	(4,658)	127
General administrative expenses	10	(9,169)	(6,628)
(Loss)/income before taxes		**(2,365)**	**4,647**
Income tax benefit/(expense)	11	411	(883)
Net (loss)/income		**(1,954)**	**3,764**

The financial statements as set out on pages 4 to 45 were approved by Management Board on 14 May 2008.

Mr. Zurab Tsikhistavi
General Director

Lia Alsanikashvili
Chief Financial Officer

The income statement is to be read in conjunction with the Notes to, and forming part of, the financial statements.

	Notes	2008 GEL'000	2007 GEL'000
ASSETS			
Cash		9,052	7,126
Due from the National Bank of Georgia	12	4,511	17,260
Placements with banks and other financial institutions	13	13,242	5,918
Loans to customers	14	63,531	62,476
Available-for-sale assets	15	54	-
Held-to-maturity investments			
- Held by the bank	16	122	-
- Pledged under sale and repurchase agreements	16	2,954	-
Property and equipment	17	12,833	8,986
Intangible assets		162	76
Other assets	18	4,847	1,134
Total Assets		**111,308**	**102,976**
LIABILITIES AND SHAREHOLDERS' EQUITY			
Deposits and balances from banks and other financial institutions	19	22,553	14,251
Amounts payable under repurchase agreements	20	2,801	-
Current accounts and deposits from customers	21	62,045	69,635
Other liabilities	22	1,487	902
Deferred tax liability	23	369	680
Total Liabilities		**89,255**	**85,468**
Shareholders' Equity			
Share capital	24	5,912	5,025
Share premium	24	5,612	-
Revaluation reserve for buildings		2,188	2,489
Retained earnings		8,341	9,994
Total Shareholders' Equity		**22,053**	**17,508**
Total Liabilities and Shareholders' Equity		**111,308**	**102,976**
Commitments and Contingencies	27-29		

The balance sheet is to be read in conjunction with the Notes to, and forming part of, the financial statements.

	Notes	2008 GEL'000	2007 GEL'000
CASH FLOWS FROM OPERATING ACTIVITIES			
Interest and fee and commission receipts		15,691	13,559
Interest and fee and commission payments		(6,457)	(4,694)
Net receipts from foreign exchange		1,708	1,667
Other income		221	719
General administrative expenses		(8,184)	(5,818)
(Increase)/decrease in operating assets			
Due from the National Bank of Georgia		3,060	1,085
Placements with banks		(323)	1,595
Loans to customers		(5,349)	(14,949)
Available-for-sale assets and held-to-maturity investments		(3,073)	53
Other assets		(602)	(100)
Increase/(decrease) in operating liabilities			
Deposits and balances from banks and other financial institutions		7,065	10,334
Amounts payable under repurchase agreements		2,801	-
Current accounts and deposits from customers		(8,049)	8,875
Other liabilities		917	(141)
Net cash from operating activities before income tax paid		**(574)**	**12,185**
Income tax paid		(598)	(612)
Cash flows from operations		**(1,172)**	**11,573**
CASH FLOWS FROM INVESTING ACTIVITIES			
Purchases of property and equipment		(5,512)	(2,054)
Purchases of intangible assets		(111)	(3)
Proceeds from disposal of property and equipment		573	116
Prepayments for property and equipment		(888)	(697)
Cash flows from investing activities		**(5,938)**	**(2,638)**
CASH FLOWS FROM FINANCING ACTIVITIES			
Proceeds from issuance of share capital		887	-
Proceeds from share premium		5,612	-
Dividends paid		-	(1,500)
Cash flows from financing activities		**6,499**	**(1,500)**
Net (decrease)/increase in cash and cash equivalents		**(611)**	**7,435**
Effect of changes in exchange rates on cash and cash equivalents		(229)	2,184
Cash and cash equivalents at the beginning of the year		23,057	13,438
Cash and cash equivalents at the end of the year	31	**22,217**	**23,057**

The statement of cash flows is to be read in conjunction with the Notes to, and forming part of, the financial statements.

	Share capital GEL'000	Share premium GEL'000	Revaluation reserve for buildings GEL'000	Retained earnings GEL'000	Total equity GEL'000
Balance at 1 January 2007	**5,025**	**-**	**2,347**	**7,730**	**15,102**
Net income for the period	-	-	-	3,764	**3,764**
Deferred tax reversal due to change in income tax rate previously recognised in revaluation reserve for buildings	-	-	142	-	**142**
Total recognised income and expense					**3,906**
Dividends declared	-	-	-	(1,500)	**(1,500)**
Balance at 31 December 2007	**5,025**	**-**	**2,489**	**9,994**	**17,508**
Net loss for the period	-	-	-	(1,954)	**(1,954)**
Realisation of property and equipment revaluation reserve on sale	-	-	(301)	301	**-**
Total recognised income and expense					**(1,954)**
Shares issued	887	**-**	-	-	**887**
Share premium	-	5,612	-	-	**5,612**
Balance at 31 December 2008	**5,912**	**5,612**	**2,188**	**8,341**	**22,053**

The statement of changes in shareholders' equity is to be read in conjunction with the Notes to, and forming part of, the financial statements.

1 Background

Principal activities

JSC BasisBank is a joint-stock bank, which was established in Georgia in 1993. The principal activities of the Bank are deposit taking and customer accounts maintenance, lending and issuing guarantees, cash and settlement operations and operations with securities and foreign exchange. The activities of the Bank are regulated by the Financial Supervisory Agency ("FSA"). The Bank has 18 branches operating in Georgia.

The registered address of the Bank is Ketevan Tsamebuli 1, 0103, Tbilisi, Georgia. The majority of the Bank's assets and liabilities are located in Georgia. The average number of people employed by the Bank during the year was 256 (2007: 200).

Shareholders

As at 31 December 2008 and 2007, the following individuals owned the share capital of the Bank:

Shareholders	**2008 Ownership interest, %**	**2007 Ownership interest, %**
European Bank for Reconstruction and Development (EBRD)	15.00%	-
Zurab Tsikhistavi	13.92%	16.36%
Eldar Mildiani	9.89%	11.62%
Zurab Nishnianidze	8.51%	10.00%
Murman Ambroladze	6.58%	7.74%
Archil Maziashvili	6.33%	7.44%
Ketevan Soselia	5.62%	6.60%
Taras Nijaradze	4.58%	5.38%
Gia Petriashvili	4.57%	5.37%
Ketevan Skhirtladze	4.44%	5.22%
Goderzi Meladze	4.42%	5.19%
Tengiz Maziashvili	4.38%	5.15%
Other individuals	11.76%	13.93%
	100.00%	**100.00%**

Related party transactions are detailed in Note 30.

Georgian business environment

Georgia has been experiencing political and economic change that has affected, and may continue to affect, the activities of enterprises operating in this environment. The recent conflict between Georgia and the Russian Federation has created additional uncertainty. Consequently, operations in Georgia involve risks that typically do not exist in other markets. In addition, the recent contraction in the capital and credit markets has further increased the level of economic uncertainty in the environment. The financial statements reflect management's assessment of the impact of the Georgian business environment on the operations and the financial position of the Bank. The future business environment may differ from management's assessment.

2 Basis of preparation

Statement of compliance

The accompanying financial statements have been prepared in accordance with International Financial Reporting Standards ("IFRS").

Basis of measurement

The financial statements are prepared on the historical cost basis except that available-for-sale assets are stated at fair value and buildings are stated at revalued amounts.

Functional and presentation currency

The national currency of Georgia is the Georgian Lari ("GEL"). Management has determined the Bank's functional currency to be the GEL as it reflects the economic substance of the underlying events and circumstances of the Bank. The GEL is also the Bank's presentation currency for the purposes of these financial statements.

Financial information presented in GEL has been rounded to the nearest thousand.

Use of estimates and judgments

Management has made a number of estimates and assumptions relating to the reporting of assets and liabilities and the disclosure of contingent assets and liabilities to prepare these financial statements in conformity with IFRS. Actual results could differ from those estimates.

In particular, information about significant areas of estimation uncertainty and critical judgments in applying accounting policies is described in the following note:

- Loan impairment estimates - Note 14
- Building revaluation estimates - Note 17

3 Significant accounting policies

The following significant accounting policies have been applied in the preparation of the financial statements. The accounting policies have been consistently applied changes in accounting policies are described at the end of this Note.

Foreign currency transactions

Transactions in foreign currencies are translated to the appropriate functional currency at the foreign exchange rate ruling at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies at the balance sheet date are translated to the functional currency at the foreign exchange rate ruling at that date. Non-monetary assets and liabilities denominated in foreign currencies, which are stated at historical cost, are translated to the functional currency at the foreign exchange rate ruling at the date of the transaction. Foreign exchange differences arising on translation are recognised in the income statement.

Cash and cash equivalents

The Bank considers cash and nostro accounts with the NBG and other banks to be cash and cash equivalents. The minimum reserve deposit required by the NBG is not included in cash and cash equivalents due to restriction on its withdrawability.

Financial instruments

Classification

Financial instruments at fair value through profit or loss are financial assets or liabilities that are:

- acquired or incurred principally for the purpose of selling or repurchasing in the near term;

- part of a portfolio of identified financial instruments that are managed together and for which there is evidence of a recent actual pattern of short-term profit-taking;

- derivative financial instruments(except for derivative financial instruments that are designated and effective hedging instruments); or,

- upon initial recognition, designated by the Bank as at fair value through profit or loss.

The Bank designates financial assets and liabilities at fair value through profit or loss where either:

- the assets or liabilities are managed and evaluated on a fair value basis;

- the designation eliminates or significantly reduces an accounting mismatch which would otherwise arise; or

- the asset or liability contains an embedded derivative that significantly modifies the cash flows that would otherwise be required under the contract.

All trading derivatives in a net receivable position (positive fair value), as well as options purchased, are reported assets. All trading derivatives in a net payable position (negative fair value), as well as options written, are reported liabilities.

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market, other than those that:

- the Bank intends to sell immediately or in the near term;

- the Bank upon initial recognition designates as at fair value through profit or loss;

- the Bank upon initial recognition designates as available-for-sale; or

- the Bank may not recover substantially all of its initial investment, other than because of credit deterioration.

Held-to-maturity investments are non-derivative financial assets with fixed or determinable payments and fixed maturity that the Bank has the positive intention and ability to hold to maturity, other than those that:

- the Bank upon initial recognition designates as at fair value through profit or loss;

- the Bank designates as available-for-sale; or

- meet the definition of loans and receivables.

Available-for-sale assets are those financial assets that are designated as available-for-sale or are not classified as loans and receivables, held-to-maturity investments or financial instruments at fair value through profit or loss.

Management determines the appropriate classification of financial instruments at the time of initial recognition.

Recognition

Financial assets and liabilities are recognized in the balance sheet when the Bank becomes a party to the contractual provisions of the instrument. All regular way purchases of financial assets are accounted for at the settlement date.

Measurement

A financial asset or liability is initially measured at its fair value plus, in the case of a financial asset or liability not at fair value through profit or loss, transaction costs that are directly attributable to the acquisition or issue of the financial asset or liability.

Subsequent to initial recognition, financial assets, including derivatives that are assets, are measured at their fair values, without any deduction for transaction costs that may be incurred on sale or other disposal, except for:

- loans and receivables which are measured at amortized cost using the effective interest method;

- held-to-maturity investments which are measured at amortized cost using the effective interest method; and

- investments in equity instruments that do not have a quoted market price in an active market and whose fair value can not be reliably measured which are measured at cost.

All financial liabilities, other than those designated at fair value through profit or loss and financial liabilities that arise when a transfer of a financial asset carried at fair value does not qualify for derecognition, are measured at amortized cost. Amortized cost is calculated using the effective interest rate method. Premiums and discounts, including initial transaction costs, are included in the carrying amount of the related instrument and amortized based on the effective interest rate of the instrument. Where a valuation based on observable market data indicates a fair value gain or loss on initial recognition of an asset or liability, the gain or loss is recognised immediately in the consolidated income statement. Where an initial gain or loss is not based entirely on observable market data, it is deferred and recognised over the life of the asset or liability on an appropriate basis, or when prices become observable, or on disposal of the asset or liability.

Fair value measurement principles

The fair value of financial instruments is based on their quoted market price at the balance sheet date without any deduction for transaction costs. If a quoted market price is not available, the fair value of the instrument is estimated using pricing models or discounted cash flow techniques.

Where discounted cash flow techniques are used, estimated future cash flows are based on management's best estimates and the discount rate is a market related rate at the balance sheet date for an instrument with similar terms and conditions. Where pricing models are used, inputs are based on market related measures at the balance sheet date.

The fair value of derivatives that are not exchange-traded is estimated at the amount that the Bank would receive or pay to terminate the contract at the balance sheet date taking into account current market conditions and the current creditworthiness of the counterparties.

Gains and losses on subsequent measurement

A gain or loss arising from a change in the fair value of a financial asset or liability is recognized as follows:

- a gain or loss on a financial instrument classified as at fair value through profit or loss is recognized in the consolidated income statement;

- a gain or loss on an available-for-sale financial asset is recognized directly in equity through the consolidated statement of changes in shareholders' equity (except for impairment losses and foreign exchange gains and losses) until the asset is derecognized, at which time the cumulative gain or loss previously recognised in equity is recognized in the consolidated income statement. Interest in relation to an available-for-sale financial asset is recognized as earned in the consolidated income statement calculated using the effective interest method.

For financial assets and liabilities carried at amortized cost, a gain or loss is recognized in the consolidated income statement when the financial asset or liability is derecognized or impaired, and through the amortization process.

Derecognition

A financial asset is derecognised when the contractual rights to the cash flows from the financial asset expire or when the Bank transfers substantially all the risks and rewards of ownership of the financial asset. Any rights or obligations created or retained in the transfer are recognized separately as assets or liabilities. A financial liability is derecognised when it is extinguished.

The Bank also derecognises certain assets when it writes off balances pertaining to the assets deemed to be uncollectible.

Repurchase and reverse repurchase agreements

Securities sold under sale and repurchase ("repo") agreements are accounted for as secured financing transactions, with the securities retained in the balance sheet and the counterparty liability included in amounts payable under repo transactions. The difference between the sale and repurchase prices represents interest expense and is recognized in the consolidated income statement over the term of the repo agreement using the effective interest rate method.

Securities purchased under agreements to resell ("reverse repo") are recorded as amounts receivable under reverse repo transactions. The difference between the purchase and resale prices represents interest income and is recognized in the consolidated income statement over the term of the repo agreement using the effective interest rate method.

If assets purchased under agreement to resell are sold to third parties, the obligation to return securities is recorded as a trading liability and measured at fair value.

Offsetting

Financial assets and liabilities are offset and the net amount 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 realise the asset and settle the liability simultaneously.

Property and equipment

Owned assets

Items of property and equipment are stated at cost less accumulated depreciation and impairment losses, except for buildings which are stated at revalued amounts as described below.

Where an item of property and equipment comprises major components having different useful lives, they are accounted for as separate items of property and equipment.

Leased assets

Operating leases and the leased assets are not recognized in the Bank's balance sheet.

Revaluation

Buildings of the Bank are subject to revaluation on a regular basis. The frequency of revaluation depends upon the movements in the fair values of the buildings being revalued. A revaluation increase on an item of land and building is recognised directly in equity except to the extent that it reverses a previous revaluation decrease recognised in the income statement, in which case it is recognised in the income statement. A revaluation decrease on an item of land or buildings is recognised in the income statement except to the extent that it reverses a previous revaluation increase recognised directly in equity, in which case it is recognised directly in equity.

The revaluation reserve is transferred to retained earnings when the asset is retired or disposed of.

Depreciation

Depreciation is charged to the income statement on a straight-line basis over the estimated useful lives of the individual assets. Depreciation commences on the date of acquisition or, in respect of internally constructed assets, from the time an asset is completed and ready for use. Leasehold improvements are depreciated over the shorter of the asset's useful life and lease term. The estimated useful lives are as follows:

Buildings	50 years
Computers and communication equipment	5 years
Furniture and fittings	5 years
Motor vehicles	5 years
Leasehold improvements	2-3 years
Other	10 years

Intangible assets

Intangible assets, which are acquired by the Bank, are stated at cost less accumulated amortisation and impairment losses.

Acquired computer software licenses are capitalised on the basis of the costs incurred to acquire and bring to use the specific software.

Amortisation is charged to the income statement on a straight-line basis over the estimated useful lives of intangible assets. The estimated useful life of intangible assets is 10 years.

Impairment

Financial assets carried at amortized cost

Financial assets carried at amortized cost consist principally of loans, other receivables and unquoted available-for-sale debt securities (“loans and receivables”). The Bank reviews its loans and receivables, to assess impairment on a regular basis. A loan or receivable is impaired and impairment losses are incurred if, and only if, there is objective evidence of impairment as a result of one or more events that occurred after the initial recognition of the loan or receivable and that event (or events) has had an impact on the estimated future cash flows of the loan that can be reliably estimated.

Objective evidence that financial assets are impaired can include default or delinquency by a borrower, breach of loan covenants or conditions, restructuring of a loan or advance by the Bank on terms that the Bank would not otherwise consider, indications that a borrower or issuer will enter bankruptcy, the disappearance of an active market for a security, deterioration in the value of collateral, or other observable data relating to a group of assets such as adverse changes in the payment status of borrowers in the group, or economic conditions that correlate with defaults in the group.

The Bank first assesses whether objective evidence of impairment exists individually for loans and receivables that are individually significant, and individually or collectively for loans and receivables that are not individually significant. If the Bank determines that no objective evidence of impairment exists for an individually assessed loan or receivable, whether significant or not, it includes the loan in a group of loans and receivables with similar credit risk characteristics and collectively assesses them for impairment. Loans and receivables 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 objective evidence that an impairment loss on a loan or receivable has been incurred, the amount of the loss is measured as the difference between the carrying amount of the loan or receivable and the present value of estimated future cash flows including amounts recoverable from guarantees and collateral discounted at the loan or receivable’s original effective interest rate. Contractual cash flows and historical loss experience adjusted on the basis of relevant observable data that reflect current economic conditions provide the basis for estimating expected cash flows.

In some cases the observable data required to estimate the amount of an impairment loss on a loan or receivable may be limited or no longer fully relevant to current circumstances. This may be the case when a borrower is in financial difficulties and there is little available historical data relating to similar borrowers. In such cases, the Bank uses its experience and judgment to estimate the amount of any impairment loss.

All impairment losses in respect of loans and receivables are recognized in the income statement and are only reversed if a subsequent increase in recoverable amount can be related objectively to an event occurring after the impairment loss was recognised.

All impairment losses in respect of loans and receivables are recognized in the consolidated income statement and are only reversed if a subsequent increase in recoverable amount can be related objectively to an event occurring after the impairment loss was recognised.

When a loan is uncollectible, it is written off against the related allowance for loan impairment. The Bank writes off a loan balance (and any related allowances for loan losses) when the Bank's management determines that the loans are uncollectible and when all necessary steps to collect the loan are completed.

Financial assets carried at cost

Financial assets carried at cost include unquoted equity instruments included in available-for-sale assets that are not carried at fair value because their fair value can not be reliably measured. If there is objective evidence that such investments are impaired, the impairment loss is calculated as the difference between the carrying amount of the investment and the present value of the estimated future cash flows discounted at the current market rate of return for a similar financial asset.

All impairment losses in respect of these investments are recognized in the income statement and can not be reversed.

Non financial assets

Other non financial assets, other than deferred taxes, are assessed at each reporting date for any indications of impairment. The recoverable amount of non financial assets is the greater of their fair value less costs to sell 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 when the carrying amount of an asset or its cash-generating unit exceeds its recoverable amount.

All impairment losses in respect of non financial assets are recognized in the income statement and reversed only if there has been a change in the estimates used to determine the recoverable amount. Any impairment loss reversed is only reversed 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.

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 assessments of the time value of money and, where appropriate, the risks specific to the liability.

Credit related commitments

In the normal course of business, the Bank enters into credit related commitments, comprising undrawn loan commitments, letters of credit and guarantees, and provides other forms of credit insurance.

Financial guarantees are contracts that require the Bank to make specified payments to reimburse the holder for a loss it incurs because a specified debtor fails to make payment when due in accordance with the terms of a debt instrument.

A financial guarantee liability is recognised initially at fair value net of associated transaction costs, and is measured subsequently at the higher of the amount initially recognised less cumulative amortisation or the amount of provision for losses under the guarantee. Provisions for losses under financial guarantees and other credit related commitments are recognised when losses are considered probable and can be measured reliably.

Financial guarantee liabilities and provisions for other credit related commitment are included within other liabilities.

Share capital

Share Premium

Share premium is calculated as the difference between the par value and the amount paid for shares issued.

Dividends

The ability of the Bank to declare and pay dividends is subject to the rules and regulations of the Georgian legislation.

Dividends in relation to ordinary shares are reflected as an appropriation of retained earnings in the period when they are declared.

Taxation

Income tax comprises current and deferred tax. Income tax is recognised in the income statement except to the extent that it relates to items recognised directly in equity, in which case it is recognised in equity.

Current tax expense is the expected tax payable on the taxable income for the year, using tax rates enacted or substantially enacted at the 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. The temporary differences from the initial recognition of assets or liabilities that affect neither accounting nor taxable profit are not provided for. 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 tax rates enacted or substantially enacted at the balance sheet date.

A deferred tax asset is recognised only to the extent that it is probable that future taxable profits will be available against which the temporary differences, unused tax losses and credits 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.

Income and expense recognition

Interest income and expense are recognised in the income statement using the effective interest method.

Loan origination fees, loan servicing fees and other fees that are considered to be integral to the overall profitability of a loan, together with the related direct costs, are deferred and amortized to the interest income over the estimated life of the financial instrument using the effective interest rate method.

Other fees, commissions and other income and expense items are recognised when the corresponding service has been provided.

New Standards and Interpretations not yet adopted

A number of new Standards, amendments to Standards and Interpretations are not yet effective as at 31 December 2008, and have not been applied in preparing these financial statements. Of these pronouncements, potentially the following will have an impact on the Bank's operations. The Bank plans to adopt these pronouncements when they become effective. The Bank has not yet analysed the likely impact of these new standards on its financial statements.

- IAS 1 *Presentation of Financial Statements* (Revised), which is effective for annual periods beginning on or after 1 January 2009, specifies how an entity should present changes in equity not resulting from transactions with owners and other changes in equity in its financial statements, and introduces certain other requirements in respect of presentation of information in the financial statements.

- Amendments to IAS 39 *Financial Instruments: Recognition and Measurement – Eligible Hedged Items,* which is effective for annual periods beginning on or after 1 July 2009, which introduce additional application guidance which clarifies that changes in the cash flows or fair value of a hedged item above or below a specified price or variable can be designated.

- Amendment to IAS 18 *Revenue*, which is effective for annual periods beginning on or after 1 January 2009, provides guidance on transaction costs related to originating a financial asset, which is aligned with the definition of transaction costs as included in IAS 39.

4 Net interest income

	2008 GEL'000	2007 GEL'000
Interest income		
Loans to customers	11,966	10,004
Placements with banks and other financial institutions	239	347
Other interest income	72	38
	12,277	**10,389**
Interest expense		
Current accounts and deposits from customers	3,339	3,659
Deposits and balances from banks and other financial institutions	2,075	228
	5,414	**3,887**

5 Fee and commission income

	2008 GEL'000	2007 GEL'000
Plastic card fees	1,369	915
Guarantee and letter of credit issuance fees	698	626
Settlement fees	365	557
Account maintenance and cash operations fees	496	512
Other	936	500
	3,864	**3,110**

6 Fee and commission expense

	2008 GEL'000	2007 GEL'000
Plastic card system fees	873	405
Settlement fees	192	147
Other	140	158
	1,205	**710**

7 Net foreign exchange income

	2008 GEL'000	2007 GEL'000
Gain on spot transactions	1,708	1,667
Loss from revaluation of financial assets and liabilities	111	(35)
	1,819	**1,632**

8 Other income/(expenses)

	2008 GEL'000	2007 GEL'000
Fines and penalties received	430	356
Fines and penalties paid	(82)	(12)
(Loss)/gain on sale of repossessed assets	(101)	275
Other	(126)	(5)
	121	**614**

9 Impairment (losses)/recoveries

	2008 GEL'000	2007 GEL'000
Loans to customers	(4,125)	65
Other assets	(533)	62
	(4,658)	**127**

10 General administrative expenses

	2008 GEL'000	2007 GEL'000
Employee compensation	3,585	2,166
Payroll related taxes	1,195	817
Depreciation and amortization	1,016	786
Advertising and marketing	761	499
Occupancy	630	491
Security	539	415
Professional services	331	199
Office supplies	186	110
Repairs and maintenance	158	207
Communications and information services	148	303
Taxes other than on income	112	63
Travel and training	70	81
Other	438	491
	9,169	**6,628**

11 Income tax benefit/(expense)

	2008 GEL'000	2007 GEL'000
Current tax benefit/(expense)		
Current year	-	(764)
Over/(under) provided in prior years	100	(34)
	100	**(798)**
Deferred tax benefit/(expense)		
Origination and reversal of temporary differences	311	(170)
Change in tax rate	-	85
	311	**(85)**
Total income tax benefit/(expense) in the income statement	**411**	**(883)**

The Bank's applicable income tax rate for current tax is 15% effective from 1 January 2008 (2007: 15%).

Reconciliation of effective tax rate:

	2008 GEL'000	%	2007 GEL'000	%
Income before tax	(2,365)		4,647	
Income tax at the applicable tax rate	(355)	15%	929	20%
Change in tax rate	-	-	(85)	(2%)
(Over)/under provided in prior years	(100)	4%	34	1%
Non-deductible costs	44	(2%)	5	0%
	(401)	**17%**	**883**	**19%**

12 Due from the National Bank of Georgia

	2008 GEL'000	2007 GEL'000
Nostro accounts	3,216	12,719
Mandatory minimum reserve deposit	1,295	4,541
	4,511	**17,260**

The withdrawability of the mandatory minimum reserve deposit is restricted.

The minimum reserve deposit is a mandatory interest bearing deposit in foreign currency calculated in accordance with regulations issued by NBG and whose withdrawability is restricted. The Nostro accounts represent balances with the NBG related to settlement activity and were available for withdrawal at year end. Withdrawal of the reserve deposit in GEL is not resticted, however the Bank is subject to penalties if the average required balance is not maintained over a 14 day period.

13 Placements with banks and other financial institutions

	2008 GEL'000	2007 GEL'000
Not impaired or past due		
Nostro accounts		
OECD banks	9,749	1,318
Other foreign banks	170	146
Largest 10 Georgian banks	30	1,748
Total nostro accounts	**9,949**	**3,212**
Deposits and other advances to banks		
OECD banks	293	611
Other foreign banks	-	-
Largest 10 Georgian banks	3,000	2,095
Total deposits and other advances to banks	**3,293**	**2,706**
	13,242	**5,918**

Collateral

As of 31 December 2008 and 2007 placements with banks are not collateralized.

Concentration of placements with banks and other financial institutions

As at 31 December 2008 and 2007 the Bank had 2 and 3 banks, respectively, whose balances exceeded 10% of total placements with banks. The gross value of these balances as of 31 December 2008 and 2007 were GEL 11,321 thousand and GEL 4,997 thousand, respectively.

14 Loans to customers

	2008 GEL'000	2007 GEL'000
Corporate loans	31,992	34,674
Loans to individuals		
Loans collateralised by real estate	11,713	12,475
Credit cards	9,915	5,999
Auto loans	1,285	855
Other consumer loans	13,907	10,252
Total loans to individuals	**36,820**	**29,581**
Gross loans to customers	**68,812**	**64,255**
Impairment allowance	(5,281)	(1,779)
Net loans to customers	**63,531**	**62,476**

Movements in the loan impairment allowance for the year ended 31 December 2008 are as follows:

	2008 GEL'000	2007 GEL'000
Balance at the beginning of the year	1,779	2,133
Net charge/(recovery) for the year (Note 9)	4,125	(65)
Net write-offs	(623)	(289)
Balance at the end of the year	**5,281**	**1,779**

As at 31 December 2008, interest accrued on impaired loans amounted to GEL 205 thousand.

Credit quality of corporate loan portfolio

The following table provides information on the credit quality of the corporate loan portfolio as at 31 December 2008:

	Gross loans GEL'000	Impairment GEL'000	Net loans GEL'000	Impairment to gross loans %
Loans for which no impairment has been identified:				
- Not overdue	23,727	(949)	22,778	4.0%
- Watch list loans	1,139	(46)	1,093	4.0%
Impaired loans:				
- overdue less than 90 days	3,503	(504)	2,999	14.4%
- overdue more than 90 days and less than 1 year	3,623	(1,503)	2,120	41.5%
Total corporate loans	**31,992**	**(3,002)**	**28,990**	**9.4%**

The following table provides information on the credit quality of the corporate loan portfolio as at 31 December 2007:

	Gross loans GEL'000	Impairment GEL'000	Net loans GEL'000	Impairment to gross loans %
Loans for which no impairment has been identified:				
- Not overdue	34,426	(632)	33,794	1.8%
Impaired loans:				
- overdue less than 90 days	58	(1)	57	1.7%
- overdue more than 1 year	190	(4)	186	2.1%
Total corporate loans	**34,674**	**(637)**	**34,037**	**1.8%**

The Bank has estimated impairment provision for corporate loans based on an analysis of the future cash flows for impaired loans. The amount of the provision is measured as the difference between the carrying amount of the loan and the present value of estimated future cash flows including amounts recoverable from guarantees and collateral discounted at the loan original effective interest rate.

For corporate loans for which no objective evidence of impairment existed as at 31 December 2008, the Bank included these loans in groups of loans with similar credit risk characteristics and collectively assessed them for impairment. The Bank has created 2% (2007: 2%) provision for impairment on these loans, based on the expected loss rate of the Bank and other comparable banks in Georgia.

Changes in these estimates could effect the loan impairment provision. For example, to the extent that the net present value of the estimated cash flows differs by one percent, the loan impairment provision on corporate loans as of 31 December 2008 would be GEL 300 thousand lower/higher.

During the year ended 31 December 2008 the Bank renegotiated several commercial loans that would otherwise be past due or impaired. Such restructuring activity is aimed at managing customer relationships and maximising collection opportunities.

Analysis of movements in the impairment allowance

Movements in the loan impairment allowance of corporate loans for the years ended 31 December 2008 and 2007 are as follows:

	2008	**2007**
	GEL'000	**GEL'000**
Loan impairment allowance as at 1 January	637	739
Net loans recovered/(written off) during the year	14	(145)
Loan impairment losses during the year	2,351	43
Loan impairment allowance as at 31 December	**3,002**	**637**

Analysis of collateral

The following table provides the analysis of the corporate loan portfolio, net of impairment, by types of collateral as at 31 December 2008 and 2007:

	2008	**% of loan portfolio**	**2007**	**% of loan portfolio**
Real estate	24,113	83%	24,402	72%
Third party guarantees	3,049	11%	5,056	15%
Equipment and motor vehicles	289	1%	2,534	7%
Inventories	280	1%	877	3%
Cash	55	0%	44	0%
Unsecured	590	2%	1,124	3%
Other	614	2%	-	-
Total	**28,990**	**100%**	**34,037**	**100%**

The amounts shown in the table above represent the carrying value of the loans, and do not necessarily represent the fair value of the collateral.

During the year ended 31 December 2008 the Bank obtained assets of GEL 1,776 thousand (Note 18) by taking control of collateral accepted as security for corporate loans (31 December 2007: GEL 30 thousand).

Impaired or overdue loans with a gross value of GEL 5,798 thousand are secured by collateral with a fair value of GEL 7,723 thousand. For the remaining impaired loans of GEL 23 thousand there is no collateral or it is impracticable to determine fair value of collateral.

Credit quality of loans to individuals

The following table provides information on the credit quality of loans to individuals' portfolios as at 31 December 2008:

	Gross loans GEL'000	Impairment GEL'000	Net loans GEL'000	Impairment to gross loans %
Loans collateralised by real estate				
- Not overdue	8,694	(348)	8,346	4.0%
- overdue less than 90 days	1,510	(60)	1,450	4.0%
- overdue more than 90 days and less than 1 year	1,509	(572)	937	37.9%
Total loans collateralised by real estate	**11,713**	**(980)**	**10,733**	**8.4%**
Credit cards				
- Not overdue	9,229	(369)	8,860	4.0%
- overdue less than 90 days	627	(126)	501	20.1%
- overdue more than 90 days and less than 1 year	59	(20)	39	33.9%
Total credit cards	**9,915**	**(515)**	**9,400**	**5.2%**
Auto loans				
- Not overdue	1,210	(48)	1,162	4.0%
- overdue less than 90 days	71	(3)	68	4.2%
- overdue more than 90 days and less than 1 year	4	(1)	3	25%
Total auto loans	**1,285**	**(52)**	**1,233**	**4.0%**
Other consumer loans				
- Not overdue	11,889	(476)	11,413	4.0%
- overdue less than 90 days	1,544	(79)	1,465	5.1%
- overdue more than 90 days and less than 1 year	450	(169)	281	37.6%
- overdue more than 1 year	24	(8)	16	33.3 %
Total other consumer loans	**13,907**	**(732)**	**13,175**	**5.3%**
Total loans to individuals	**36,820**	**(2,279)**	**34,541**	**6.2%**

The following table provides information on the credit quality of loans to individual's portfolios as at 31 December 2007:

	Gross loans GEL'000	Impairment GEL'000	Net loans GEL'000	Impairment to gross loans %
Loans collateralised by real estate				
- Not overdue	10,693	187	10,506	1.7%
- overdue less than 90 days	166	3	163	1.8%
- overdue more than 90 days and less than 1 year	428	7	421	1.6%
- overdue more than 1 year	1,188	20	1,168	1.7%
Total loans collateralised by real estate	**12,475**	**217**	**12,258**	**1.7%**
Credit cards not overdue	5,999	192	5,807	3.2%
Auto loans				
- Not overdue	804	25	779	3.1%
- overdue less than 90 days	36	7	29	19.4%
- overdue more than 90 days and less than 1 year	13	4	9	30%
- overdue more than 1 year	2	2	-	100%
Total auto loans	**855**	**38**	**817**	**4.4%**
Other consumer loans				
- Not overdue	9,622	423	9,199	4.4%
- overdue less than 90 days	292	58	234	20%
- overdue more than 90 days and less than 1 year	310	186	124	60%
- overdue more than 1 year	28	28	-	100%
Total other consumer loans	**10,252**	**695**	**9,557**	**6.8%**
Total loans to individuals	**29,581**	**1,142**	**28,439**	**3.9%**

The significant assumptions used in determining the impairment losses for loans to individuals are based on the economic environment and consideration of historical and market experience and include the following loan loss rates:

- Loans collateralized by real estate – 8.4%
- Credit cards – 5.2%
- Auto loans – 4.0%
- Other consumer loans – 5.3%

Changes in these estimates could effect the loan impairment provision. For example, to the extent that the net present value of the estimated cash flows differs by plus/minus one percent, the loan impairment on loans to individuals as of 31 December 2008 would be GEL 353 thousand lower/higher.

Analysis of collateral

The Bank estimates that the fair value of the collateral for overdue or impaired loans collateralised by real estate is at least equal to 95% of the loan balance. Management believes that it is impracticable to estimate fair value of collateral held in respect of other loans to individuals.

Mortgage loans are secured by underlying housing real estate. Auto loans are secured by underlying car. Credit cards and consumer loans are not secured.

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Impaired or overdue loans with a gross value of GEL 3,095 thousand are secured by collateral with a fair value of GEL 6,042 thousand. For the remaining impaired loans of GEL 2,703 thousand there is no collateral or it is impracticable to determine fair value of collateral.

Analysis of movements in the impairment allowance

Movements in the loan impairment allowance by classes of retail loans for the year ended 31 December 2008 are as follows:

GEL'000	**Loans collateralised by real estate**	**Auto loans**	**Credit cards**	**Other loans**	**Total**
Loan impairment allowance as at 1 January	217	38	192	695	1,142
Net loans recovered/(written off) during the year	183	(4)	31	(847)	(637)
Loan impairment losses/(recoveries) during the year	580	18	292	884	1,774
Loan impairment allowance as at 31 December	**980**	**52**	**515**	**732**	**2,279**

Movements in the loan impairment allowance by classes of retail loans for the year ended 31 December 2007 are as follows:

GEL'000	**Loans collateralised by real estate**	**Auto loans**	**Credit cards**	**Other loans**	**Total**
Loan impairment allowance as at 1 January	171	4	132	1,087	1,394
Loans written off during the year as uncollectible	4	-	(147)	(1)	(144)
Loan impairment losses during the year	42	34	207	(391)	(108)
Loan impairment allowance as at 31 December	**217**	**38**	**192**	**695**	**1,142**

Industry analysis of the loan portfolio

Loans to customers were issued primarily to customers located within Georgia, who operate in the following economic sectors (shown net of impairment):

	2008 GEL'000	**2007 GEL'000**
Trade and services	12,620	17,054
Construction	8,760	9,504
Mining/metallurgy and production	4,285	3,495
Agriculture	1,500	-
Transportation and communication	633	2,260
Energy	297	-
Other	895	1,724
Loans to individuals	34,541	28,439
	63,531	**62,476**

Significant credit exposures

As at 31 December 2008 the Bank did not have any borrowers or groups of related borrowers, whose loan balances exceeded 10% of loans to customers.

Loan maturities

The maturity of the Bank's loan portfolio is presented in Note 34, which shows the remaining period from the reporting date to the contractual maturity of the loans comprising the loan portfolio. Due to the short-term nature of the loans issued by the Bank, it is likely that many of the Bank's loans to customers will be prolonged on maturity. Accordingly, the effective maturity of the loan portfolio may be significantly longer than the classification indicated based on contractual terms.

15 Available-for-sale assets

	2008 GEL'000	2007 GEL'000
Equity instruments - Unquoted		
Corporate shares	54	-
	54	**-**

Investment without a determinable fair value

Available-for-sale equity instruments stated at cost comprise unquoted equity securities in the financial services industry. There is no market for these investments and there have not been any recent transactions that provide evidence of the current fair values. In addition, discounted cash flow techniques yield a wide range of fair values due to the uncertainty regarding future cash flows.

16 Held to maturity investments

	2008 GEL'000	2007 GEL'000
Held by the bank		
Debt and other fixed-income instruments		
NBG deposit certificates	20	-
Corporate bonds	102	-
	122	**-**
Pledged under sale and repurchase agreements		
Debt and other fixed-income instruments		
NBG deposit certificates	2,954	-
	2,954	**-**

17 Property and equipment

GEL'000	Buildings	Computers and communication equipment	Furniture and fittings	Motor vehicles	Leasehold improvement	Other	Total
Cost/Revalued amount							
At 1 January 2007	6,325	1,939	372	89	-	62	**8,787**
Additions	66	1,301	158	28	414	23	**1,990**
Disposals	-	(249)	(34)	(18)	-	-	**(301)**
At 31 December 2007	**6,391**	**2,991**	**496**	**99**	**414**	**85**	**10,476**
At 1 January 2008	6,391	2,991	496	99	414	85	**10,476**
Additions	4,950	354	165	23	-	20	**5,512**
Disposals	(854)	(59)	(82)	-	-	-	**(995)**
Transfers	-	-	294	-	(294)	-	-
At 31 December 2008	**10,487**	**3,286**	**873**	**122**	**120**	**105**	**14,993**
Depreciation							
At 1 January 2007	217	500	159	28	-	12	**916**
Depreciation charge	132	499	61	18	41	8	**759**
Disposals		(134)	(34)	(17)	-	-	**(185)**
At 31 December 2007	**349**	**865**	**186**	**29**	**41**	**20**	**1,490**
At 1 January 2008	349	865	186	29	41	20	**1,490**
Depreciation charge	131	622	166	24	40	10	**993**
Disposals	(179)	(63)	(81)	-	-	-	**(323)**
Transfers	-	-	36	-	(36)	-	-
At 31 December 2008	**301**	**1,424**	**307**	**53**	**45**	**30**	**2,160**
Carrying value							
At 1 January 2007	6,108	1,439	213	61	-	50	**7,871**
At 31 December 2007	6,042	2,126	310	70	373	65	**8,986**
At 31 December 2008	**10,186**	**1,862**	**566**	**69**	**75**	**75**	**12,833**

Revalued assets

In July 2006, the buildings were revalued by Management based on the results of an independent appraisal performed by Giorgi Lezhava. The fair values of the revalued items were determined based on the discounted cash flow method (income approach) and method of sales comparison (comparative approach). For the estimation of the final value, the approach used was dependent on the reliability and completeness of the information and available market information of the specific buildings.

The carrying value of buildings as of 31 December 2008, if the buildings would not have been revalued, would be GEL 7,587 thousand (2007: GEL 7,718 thousand).

18 Other assets

	2008 GEL'000	2007 GEL'000
Repossessed assets	1,776	30
Prepayments for property and equipment	1,748	860
Receivables from payments processing systems	832	237
Accounts receivable	500	-
Prepayment of income tax	418	-
Other receivables	106	7
Allowance for impairment losses on repossessed assets	(533)	-
	4,847	**1,134**

Analysis of movements in impairment allowance for other assets

	2008 GEL'000	2007 GEL'000
Balance as at 1 January	-	62
Net charge/(recovery) for the year (Note 9)	533	(62)
Balance as at 31 December	**533**	**-**

19 Deposits and balances from banks and other financial institutions

	2008 GEL'000	2007 GEL'000
Loans from European Bank for Reconstruction and Development	10,458	4,855
Term deposits of local banks	5,028	5,608
Loan from Ministry of Finance	3,154	758
Loan from the National Bank of Georgia	2,100	3,000
Vostro accounts	1,813	30
	22,553	**14,251**

Concentration of deposits and balances from banks and other financial institutions

As at 31 December 2008 and 2007 the Bank had 3 and 4 banks and financial institutions, respectively, whose balances exceeded 10% of total deposits and balances from banks and other financial institutions. The gross value of these balances as of 31 December 2008 and 2007 were GEL 18,302 thousand and GEL 13,464 thousand, respectively.

As at 31 December 2008 the Bank had breached several covenants for loans from the Ministry of Finance (MOF). Per the loan agreements with the MOF if loan covenants are breached, MOF may declare all or any portion of the loans immediately due. As a result, these loans have been re-classified as due on demand in notes 25 and 34.

20 Amounts payable under repurchase agreements

	2008 GEL'000	2007 GEL'000
Amounts due to National Bank of Georgia	**2,801**	**-**

Collateral

As of 31 December 2008, amounts payable under repurchase agreements were collateralised by the following securities:

	2008 GEL'000	2007 GEL'000
NBG deposit certificates	**2,954**	**-**

21 Current accounts and deposits from customers

	2008 GEL'000	2007 GEL'000
Current accounts	37,745	47,727
Demand deposits	9,167	3,398
Term deposits	15,133	18,510
	62,045	**69,635**

Blocked accounts

As of 31 December 2008, the Bank maintained customer deposit balances of GEL 1,345 thousand (2007: GEL 1,288 thousand) which were blocked by the Bank as collateral for loans and off-balance sheet credit instruments granted by the Bank.

Concentrations of current accounts and customer deposits

As of 31 December 2008 and 2007, the Bank had no customer whose balances exceeded 10% of total customer accounts and deposits.

22 Other liabilities

	2008 GEL'000	2007 GEL'000
Payables for payments processing systems	1,268	502
Current income tax liability	-	281
Accrued expenses	170	77
Taxes payable, other than income tax	49	42
	1,487	**902**

23 Deferred tax asset and liability

Temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes give rise to net deferred tax liabilities as of 31 December 2008 and 2007.

Deferred tax assets and liabilities are attributable to the following:

GEL'000	**Assets**		**Liabilities**		**Net**	
	2008	**2007**	**2008**	**2007**	**2008**	**2007**
Loans to customers	303	24	-	-	303	24
Property and equipment	-	-	(1,436)	(696)	(1,436)	(696)
Other liabilities	66	-	-	(8)	66	(8)
Tax loss carry-forwards	698	-	-	-	698	-
Recognized net deferred tax assets/ (liabilities)	**1,067**	**24**	**(1,436)**	**(704)**	**(369)**	**(680)**

The tax rate applicable for deferred taxes was 15% (2007: 15%).

The above net deductible temporary differences do not expire under current tax legislation.

Movement in temporary differences during the year ended 31 December 2008

GEL'000	**Balance 1 January 2008**	**Recognised in income**	**Balance 31 December 2008**
Loans to customers	24	279	303
Property and equipment	(696)	(740)	(1,436)
Other liabilities	(8)	74	66
Tax loss carry-forwards	-	698	698
	(680)	**311**	**(369)**

Movement in temporary differences during the year ended 31 December 2007

GEL'000	Balance 1 January 2007	Recognised in income	Recognised in equity	Balance 31 December 2007
Loans to customers	8	16	-	24
Property and equipment	(721)	(117)	142	(696)
Other liabilities	(24)	16	-	(8)
	(737)	**(85)**	**142**	**(680)**

24 Share capital

Issued capital

The authorized share capital comprises 6,700,001 ordinary shares (2007: 5,200,000), with a par value of GEL 1 per share, from which 5,912,000 were issued, paid and outstanding as at 31 December 2008 (2007: 5,025,000).

Share premium

During 2008, the bank issued 887,000 new shares with a par value of GEL 1 per share for GEL 6,499 thousand which created share premium of GEL 5,612 thousand.

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 annual and general meetings of the Bank.

Dividends

Dividends payable are restricted to the maximum retained earnings of the Bank less general reserves as recorded in the Bank's statutory accounts, which are determined according to the legislation of Georgia.

At the balance sheet date the following interim dividends had been declared and paid by the Bank:

	2008 GEL'000	2007 GEL'000
0.00 GEL per ordinary share (2007: 0.30)	-	1,500

Subsequent to 31 December 2008 no dividends have been declared by the Bank.

25 Risk management

Management of risk is fundamental to the business of banking and is an essential element of the Bank's operations. The major risks faced by the Bank are those related to market risk, which includes price, interest rate and currency risks, credit risk and liquidity risk.

Risk management policies and procedures

The Bank's risk management policies aim to identify, analyse and manage the risks faced by the Bank, to set appropriate risk limits and controls, and to continuously monitor risk levels and adherence to limits. Risk management policies and procedures are reviewed regularly to reflect changes in market conditions, products and services offered and emerging best practice.

The Supervisory Board of the Bank has overall responsibility for the oversight of the risk management framework, overseeing the management of key risks and reviewing its risk management policies and procedures as well as approving significantly large exposures.
The Management Board of the Bank is responsible for monitoring and implementation of risk mitigation measures and making sure that the Bank operate within the established risk parameters.

Credit, market and liquidity risks both at portfolio and transactional levels are managed and controlled through a system of Credit Committees and an Asset and Liability Management Committee. In order to facilitate efficient decision-making, the Bank has established a hierarchy of credit committees depending on the type and amount of the exposure.

Both external and internal risk factors are identified and managed throughout the Bank's organisational structure. Particular attention is given to developing risk maps that are used to identify the full range of risk factors and serve as a basis for determining the level of assurance over the current risk mitigation procedures. Apart from the standard credit and market risk analysis, the Management Board monitors financial and non-financial risks by holding regular meetings with operational units in order to obtain expert judgments in their areas of expertise.

Market risk

Market risk is the risk that movements in market prices, including foreign exchange rates, interest rates, credit spreads and equity prices will affect the Bank's income or the value of its portfolios. Market risks comprise currency risk, interest rate risk and other price risk. Market risk arises from open positions in interest rate, currency and equity financial instruments, which are exposed to general and specific market movements and changes in the level of volatility of market prices.

The objective of market risk management is to manage and control market risk exposures within acceptable parameters, whilst optimizing the return on risk.

Overall authority for market risk is vested in the Management Board, chaired by the General Director of the Bank. Market risk limits are approved by Management Board based on recommendations of the Treasury Department.

The Bank manages its market risk by setting open position limits in relation to financial instrument, interest rate maturity and currency positions which are monitored on a regular basis and reviewed and approved by the Management Board.

The management of interest rates risk, component of market risk, by monitoring interest rate gap is supplemented by monitoring the sensitivity of the Bank's net interest margin to various standard and non-standard interest rate scenarios.

Interest rate risk

Interest rate risk is the risk that movements in interest rates will affect the Bank's income or the value of its portfolios of financial instruments.

The Bank is exposed to the effects of fluctuations in the prevailing levels of market interest rates on its financial position and cash flows. Interest margins may increase as a result of such changes but may also reduce or create losses in the event that unexpected movements arise.

Interest rate risk arises when the actual or forecasted assets of a given maturity period are either greater or less than the actual or forecasted liabilities in that maturity period.

An analysis of sensitivity of the Bank's profit and equity to changes in the market interest rate based on a simplified scenario of a 100 basis point (bp) symmetrical fall or rise in all yield curves and positions of interest-bearing assets and liabilities existing as at 31 December 2008 and 31 December 2007 is as follows:

	2008		2007	
	Profit	**Equity**	**Profit**	**Equity**
100 bp parallel increase	(54)	(54)	(22)	(22)
100 bp parallel decrease	54	54	22	22

Currency risk

The Bank has assets and liabilities denominated in several foreign currencies. Foreign currency risk arises when the actual or forecasted assets in a foreign currency are either greater or less than the liabilities in that currency. For further information on the Bank's exposure to currency risk at year end refer to Note 35.

An analysis of sensitivity of the Bank's profit for the year and equity to changes in the foreign currency exchange rates based on positions existing as at 31 December 2008 and 2007 and a simplified scenario of a 5% change in USD and Euro to Georgian Lari exchange rates is as follows:

	2008		2007	
	Profit	**Equity**	**Profit**	**Equity**
5% appreciation of USD against GEL	30	30	16	16
5% depreciation of USD against GEL	(30)	(30)	(16)	(16)
5% appreciation of EUR against GEL	(111)	(113)	(43)	(43)
5% depreciation of EUR against GEL	111	111	43	43

Credit risk

Credit risk is the risk of financial loss occurring as a result of default by a borrower or counterparty on their obligation to the Bank. The Bank has developed policies and procedures for the management of credit exposures (both for on balance sheet and off balance sheet exposures), including guidelines to limit portfolio concentration and the establishment of a Credit Committee, which actively monitors the Bank's credit risk. The Bank's credit policy is reviewed and approved by the Management Board.

The Bank's credit policy establishes:

- Procedures for review and approval of loan/credit applications;

- Methodology for the credit assessment of borrowers (corporate, small and medium size companies and retail);
- Methodology for the credit assessment of counterparties, issuers and insurance companies;
- Methodology for the evaluation of collateral;
- Credit documentation requirements;
- Procedures for the ongoing monitoring of loans and other credit exposures.

Corporate loan/credit applications are originated by the relevant client managers and are then passed on to the Corporate Loans Department. Reports produced by the department's credit analysts are based on a structured analysis focusing on the customer's business and financial performance. The Credit Committee reviews the loan/credit application on the basis of submission by the Corporate Loans Department. Individual transactions are also reviewed by the Bank's Legal, Accounting and Tax departments depending on the specific risks and pending final approval of the Credit Committee.

The Bank continuously monitors the performance of individual credit exposures and regularly reassesses the creditworthiness of its customers. The review is based on the customer's most recent financial statements and other information submitted by the borrower, or otherwise obtained by the Bank. The current market value of collateral is regularly assessed by either independent appraisal companies or the Bank's specialists, and in the event of negative movements in market prices the borrower is usually requested to put up additional security.

Retail loan/credit applications are reviewed by the Bank's Retail Loans Department through the use of scoring models and application data verification procedures.

Apart from individual customer analysis, the whole credit portfolio is assessed by the Credit Committee with regard to credit concentration and market risks.

The Bank's maximum exposure to on and off balance sheet credit risk is generally reflected in the carrying amounts of financial assets on the balance sheet and guarantees and credit commitments included in Note 33. The impact of possible netting of assets and liabilities to reduce potential credit exposure is not significant.

The Bank monitors concentrations of credit risk by industry/sector. For the analysis of concentration of credit risk in respect of loans and advances to customers refer to Note 14 "Loans to customers".

Liquidity risk

Liquidity risk is the risk that the Bank will encounter difficulty in raising funds to meet its commitments. Liquidity risk exists when the maturities of assets and liabilities do not match. The matching and/or controlled mismatching of the maturities and interest rates of assets and liabilities is fundamental to the management of financial institutions, including the Bank. It is unusual for financial institutions ever to be completely matched since business transacted is often of an uncertain term and of different types. An unmatched position potentially enhances profitability, but can also increase the risk of losses.

The Bank maintains liquidity management with the objective of ensuring that funds will be available at all times to honor all cash flow obligations as they become due. The Bank's liquidity policy is reviewed and approved by the Management Board.

The Bank seeks to actively support a diversified and stable funding base comprising long-term and short-term loans from other banks, core corporate and retail customer deposits, accompanied by diversified portfolios of highly liquid assets, in order to be able to respond quickly and smoothly to unforeseen liquidity requirements.

The liquidity management policy of the Bank requires:

- projecting cash flows by major currencies and considering the level of liquid assets necessary in relation thereto;
- maintaining a diverse range of funding sources;
- managing the concentration and profile of debts;
- maintaining debt financing plans;
- maintaining a portfolio of highly marketable assets that can easily be liquidated as protection against any interruption to cash flow;
- maintaining liquidity and funding contingency plans;
- monitoring balance sheet liquidity ratios against regulatory requirements.

The Treasury Department receives information from business units regarding the liquidity profile of their financial assets and liabilities and details of other projected cash flows arising from projected future business. The Treasury Department then provides for an adequate portfolio of short-term liquid assets to be maintained, largely made up of short-term liquid securities, loans to banks and other inter-bank facilities, to ensure that sufficient liquidity is maintained within the Bank as a whole.

The daily liquidity position is monitored and regular liquidity stress testing under a variety of scenarios covering both normal and more severe market conditions is performed by the Treasury Department. Under the normal market conditions, liquidity reports covering the liquidity position of the Bank are presented to senior management on a weekly basis. Decisions on the Bank's liquidity management are made by the Management Board and implemented by the Treasury Department.

The Bank also calculates mandatory liquidity ratios on a daily basis in accordance with the requirement of the NBG. The Bank was in compliance with these ratios during the years ended 31 December 2008 and 31 December 2007.

The following tables show the undiscounted cash flows on the Bank's financial liabilities and unrecognized loan commitments on the basis of their earliest possible contractual maturity. The total gross outflow disclosed in the table is the contractual, undiscounted cash flow on the financial liability or commitment. The Bank's expected cash flows on these financial liabilities and unrecognized loan commitments may vary significantly from this analysis.

The position of the Bank as at 31 December 2008 was as follows:

	Demand and less than 1 month	From 1 to 3 months	From 3 to 6 months	From 6 to 12 months	More than 1 year	Total gross amount	Carrying amount
Deposits and balances from banks and other financial institutions	10,032	2,888	-	1,785	9,785	24,490	22,553
Amounts payable under repurchase agreements	2,807	-	-	-		2,807	2,801
Current accounts and deposits from customers	47,434	4,908	2,360	5,961	2,346	63,009	62,045
Other liabilities	1,268	219	-	-	-	1,487	1,487
Total	**61,541**	**8,015**	**2,360**	**7,746**	**12,131**	**91,793**	**88,886**
Credit related commitments	**9.818**	**-**	**-**	**-**	**-**	**9,818**	**9,818**

The position of the Bank as at 31 December 2007 was as follows:

	Demand and less than 1 month	From 1 to 3 months	From 3 to 6 months	From 6 to 12 months	More than 1 year	Total gross amount	Carrying amount
Deposits and balances from banks and other financial institutions	6,656	2,230	-	267	7,237	16,390	14,251
Current accounts and deposits from customers	53,246	4,700	5,921	4,946	1,812	70,625	69,635
Other liabilities	621	281	-	-	-	902	902
Total	**60,523**	**7,211**	**5,921**	**5,213**	**9,049**	**87,917**	**84,788**
Undrawn credit line and overdraft commitments	**15,747**	**-**	**-**	**-**	**-**	**15,747**	**15,747**

For further information on the Bank's exposure to liquidity risk at year end refer to Note 34.

26 Capital management

The NBG sets and monitors capital requirements for the Bank.

The Bank defines as capital those items defined by statutory regulation as capital for Banks. Under the current capital requirements set by the NBG banks have to maintain a ratio of capital to risk weighted assets ("regulatory capital ratio") above the prescribed minimum level. As at 31 December 2008, this minimum level is 12%. The Bank was in compliance with the statutory capital ratio during the years ended 31 December 2008 and 31 December 2007.

27 Commitments

At any time the Bank has outstanding commitments to extend loans. These commitments take the form of approved loans and credit card limits and overdraft facilities.

The Bank provides financial guarantees and letters of credit to guarantee the performance of customers to third parties. These agreements have fixed limits and generally extend for a period of up to five years.

The contractual amounts of commitments are set out in the following table by category. The amounts reflected in the table for commitments assume that amounts are fully advanced. The amounts reflected in the table for guarantees and letters of credit represent the maximum accounting loss that would be recognised at the balance sheet date if counterparties failed completely to perform as contracted.

	2008 GEL'000	**2007 GEL'000**
Contracted amount		
Undrawn credit line commitments	2,022	973
Undrawn overdraft facilities	7,796	14,774
Letters of credit	232	32
Guarantees	9,406	6,176

The total outstanding contractual commitments to extend credit indicated above does not necessarily represent future cash requirements, as these commitments may expire or terminate without being funded.

28 Operating leases

Leases as lessee

Non-cancelable operating lease rentals are payable as follows:

	2008 GEL'000	**2007 GEL'000**
Less than one year	386	104
Between one and five years	387	840
	773	**944**

The Bank leases a number of premises under operating leases. The leases typically run for an initial period of two to five years, with an option to renew the lease after that date. None of the leases includes contingent rentals.

During the current year GEL 630 thousand was recognized in the income statement in respect of operating leases (2007: GEL 491 thousand).

29 Contingencies

Insurance

The insurance industry in Georgia is in a developing state and many forms of insurance protection common in other parts of the world are not yet generally available. The Bank does not have full coverage for its premises and equipment, business interruption, or third party liability in respect of property or environmental damage arising from accidents on Bank's property or relating to the Bank's operations. Until the Bank obtains adequate insurance coverage, there is a risk that the loss or destruction of certain assets could have a material adverse effect on the Bank's operations and financial position.

Litigation

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 conditions of the results of future operations of the Bank.

Taxation contingencies

The taxation system in Georgia is relatively new and is characterised by frequent changes in legislation, official pronouncements and court decisions, which are often unclear, contradictory and subject to varying interpretation by different tax authorities. Taxes are subject to review and investigation by a number of authorities, which have the authority to impose severe fines, penalties and interest charges. A tax year remains open for review by the tax authorities during the six subsequent calendar years; however, under certain circumstances a tax year may remain open longer. Recent events within Georgia suggest that the tax authorities are taking a more assertive position in their interpretation and enforcement of tax legislation.

These circumstances may create tax risks in Georgia that are substantially more significant than in other countries. Management believes that it has provided adequately for tax liabilities based on its interpretations of applicable Georgian tax legislation, official pronouncements and court decisions. However, the interpretations of the relevant authorities could differ and the effect on the financial position of the Bank, if the authorities were successful in enforcing their interpretations, could be significant.

30 Related party transactions

Transactions with the members of key management

Total remuneration included in employee compensation (Note 10):

	2008 GEL'000	**2007 GEL'000**
Members of the Supervisory Board	714	13
Members of the Management Board	448	393
	1,162	**406**

The outstanding balances and average interest rates as of 31 December 2008 and 2007 with the members of the key management personnel are as follows:

	2008 GEL'000	Average interest rate	2007 GEL'000	Average interest rate
Balance Sheet				
Assets				
Loans to customers	1,255	14%	1,075	16%
Other assets	500	0%	-	-
Liabilities				
Current accounts and deposits from customers	370	6%	64	3%

Other amounts included in the income statement in relation to transactions with the members of the key management personnel are as follows:

	2008 GEL'000	2007 GEL'000
Income statement		
Interest income	131	116
Interest expense	13	-

Transactions with other related parties

The outstanding balances and the related average interest rates as of 31 December 2008 and related income statement amounts of transactions for the year ended 31 December 2008 with other related parties are as follows.

	Entities with significant influence over the Bank		Close family members of key management personnel		Companies that are controlled or significantly influenced by key management personnel		Total
	GEL'000	Average interest rate	GEL'000	Average interest rate	GEL'000	Average interest rate	GEL'000
Balance Sheet							
Assets							
Loans to customers	-	-	255	17%	2,663	17%	**2,918**
Liabilities							
Deposits and balances from banks and other financial institutions	10,322	8%	-	-	-	-	**10,322**
Current accounts and deposits from customers	-	-	273	9%	829	5%	**1,102**
Income statement							
Interest income	-	-	43	-	212	-	**255**
Interest expense	660	-	13	-	7	-	**680**

The outstanding balances and the related average interest rates as of 31 December 2007 and related income statement amounts of transactions for the year ended 31 December 2007 with other related parties are as follows.

	Entities with significant influence over the Bank		Close family members of key management personnel		Companies that are controlled or significantly influenced by key management personnel		Total
	GEL'000	Average interest rate	GEL'000	Average interest rate	GEL'000	Average interest rate	GEL'000
Balance Sheet							
Assets							
Loans to customers	-	-	-	-	325	17%	325
Liabilities							
Current accounts and deposits from customers	-	-	157	-	354	11%	511
Off balance sheet items							
Guarantees	-	-	-	-	199	-	199
Undrawn credit line and overdraft commitments	-	-	-	-	103	-	103
Income statement							
Interest income	-	-	-	-	93	-	93
Interest expense	-	-	3	-	-	-	3

31 Cash and cash equivalents

Cash and cash equivalents at the end of the financial year as shown in the statement of cash flow are composed of the following items:

	2008 GEL'000	2007 GEL'000
Cash	9,052	7,126
Due from the National Bank of Georgia – nostro accounts	3,216	12,719
Placements with banks and other financial institutions – nostro accounts	9,949	3,212
	22,217	**23,057**

32 Fair value of financial instruments

The estimated fair value of all the Bank's financial assets and liabilities, as required to be disclosed by IFRS 7 Financial Instruments: Disclosures, approximates their carrying values.

The estimates of fair value are intended to approximate the amount for which a financial instrument could be exchanged between knowledgeable, willing parties in an arm's length transaction. However given the uncertainties and the use of subjective judgment, the fair value should not be interpreted as being realisable in an immediate sale of the assets or settlement of liabilities.

As disclosed in note 16 the fair value of unquoted equity securities with a carrying value of GEL 54 thousand (2007: nil) could not be determined.

33 Average effective interest rates

The table below displays the Bank's interest bearing assets and liabilities as at 31 December 2008 and 2007 and their corresponding average effective interest rates as at that date. These interest rates are an approximation of the yields to maturity of these assets and liabilities, except for loans from European Bank for Reconstruction and Development (EBRD) and Government of Georgia of GEL 13,099 thousand, the interest rates on which are reviewed on a semi-annual basis based on LIBOR as follows: GEL 10,002 thousand - 2 February 2009, GEL 3,097 thousand - 1 February 2009. Maturity of the loan from EBRD is 2012, maturity date of the loan from Government of Georgia is 2016.

	Value GEL'000	2008 Average effective interest rate	Value GEL'000	2007 Average effective interest rate
Interest Bearing Assets				
Due from the National Bank of Georgia				
Mandatory minimum reserve deposit				
- USD	1,295	2%	4,541	2%
Placements with banks and other financial institutions				
Nostro accounts				
- GEL	14	8%	-	-
- USD	8,334	2%	1,634	3%
- EUR	1,092	3%	1,126	3%
Deposits and other advances to banks				
- GEL	3,000	10%	-	-
- USD	-	-	2,095	10%
-EUR	177	3%	-	-
Loans to customers				
- GEL	36,077	18%	41,798	17%
- USD	23,903	20%	19,708	18%
- EUR	3,514	18%	968	17%
- Other	37	22%	2	24%
Held to Maturity investments				
Debt and other fixed-income instruments				
-GEL	3,076	12%	-	-

	Value GEL'000	2008 Average effective interest rate	Value GEL'000	2007 Average effective interest rate
Interest Bearing Liabilities				
Deposits and balances from banks and other financial institutions				
Vostro accounts				
- GEL	1,740	13%	-	-
- EUR	71	5%	-	-
Deposits				
- GEL	5,000	17%	5,608	9%
Loans				
- GEL	2,100	13%	3,000	14%
- USD	13,099	7%	5,613	10%
Amounts payable under repurchase	2,801	9%	-	-
- GEL				
Current accounts and deposits from				
Current accounts and demand deposits				
- GEL	10,640	6%	12,320	8%
- USD	4,792	5%	6,250	4%
- EUR	884	3%	879	4%
- Other	80	3%	43	3%
Term deposits				
- GEL	5,436	13%	7,435	10%
- USD	5,990	10%	9,042	8%
- EUR	3,338	8%	2,002	8%
- Other	13	10%	31	10%

34 Maturity analysis

The following table shows assets and liabilities by remaining contractual maturity dates as at 31 December 2008.

Assets	Less than 1 month GEL'000	1 to 3 months GEL'000	3 months to 1 year GEL'000	1 to 5 years GEL'000	More than 5 years GEL'000	No maturity GEL'000	Overdue GEL'000	Total GEL'000
Cash	9,052	-	-	-	-	-	-	9,052
Due from the National Bank of Georgia	4,511	-	-	-	-	-	-	4,511
Placements with banks and other financial institutions	13,242	-	-	-	-	-	-	13,242
Loans to customers	13,581	10,455	16,243	17,840	2,253	-	3,159	63,531
Available-for-sale assets	-	-	-	-	-	54	-	54
Held to maturity investments	2,974	-	102	-	-	-	-	3,076
Property and equipment	-	-	-	-	-	12,833	-	12,833
Intangible assets	-	-	-	-	-	162	-	162
Other assets	832		2,104	1,911	-	-	-	4,847
Total assets	**44,192**	**10,455**	**18,449**	**19,751**	**2,253**	**13,049**	**3,159**	**111,308**
Liabilities								
Deposits and balances from banks and other financial institutions	9,938	2,481	1,429	8,573	132	-	-	22,553
Amounts payable under repurchase agreements	2,801	-	-	-	-	-	-	2,801
Current accounts and deposits from customers	47,420	4,873	7,727	1,679	346	-	-	62,045
Other liabilities	1,268	219	-	-	-	-	-	1,487
Deferred tax liability	-	-	-	-	-	369	-	369
Total liabilities	**61,427**	**7,573**	**9,156**	**10,252**	**478**	**369**	**-**	**89,255**
Net position as at 31 December 2008	**(17,235)**	**2,882**	**9,293**	**9,499**	**1,775**	**12,680**	**3,159**	**22,053**
Net position as at 31 December 2007	(28,226)	(424)	18,497	11,692	5,953	8,412	1,604	17,508

Except for loans from banks and other financial institutions (Note 33), these remaining contractual maturity dates also represent the contractual interest rate repricing dates of financial instruments.

The amounts in the table above represent carrying amounts of the assets and liabilities as at the reporting date and do not include future interest payments.

35 Currency analysis

The following table shows the currency structure of assets and liabilities at 31 December 2008:

`	GEL GEL'000	USD GEL'000	EUR GEL'000	Others GEL'000	Total GEL'000
Assets					
Cash	4,429	2,428	17	2,178	9,052
Due from the National Bank of Georgia	2,863	1,630	18	-	4,511
Placements with banks and other financial institutions	3,013	8,692	1,361	176	13,242
Loans to customers	36,077	23,903	3,514	37	63,531
Available-for-sale assets	54	-	-	-	54
Held to maturity investments	3,076	-	-	-	3,076
Property and equipment	12,833	-	-	-	12,833
Intangible assets	162	-	-	-	162
Other assets	4,412	435			4,847
Total assets	**66,919**	**37,088**	**4,910**	**2,391**	**111,308**
Liabilities					
Deposits and balances from banks and other financial institutions	9,001	13,481	71	-	22,553
Amounts payable under repurchase agreements	2,801	-	-	-	2,801
Current accounts and deposits from customers	32,102	22,313	7,389	241	62,045
Other liabilities	835	585	64	3	1,487
Deferred tax liability	369	-	-	-	369
Total liabilities	**45,108**	**36,379**	**7,524**	**244**	**89,255**
Net balance sheet position as of 31 December 2008	**21,811**	**709**	**(2,614)**	**2,147**	**22,053**
Net balance sheet position as of 31 December 2007	18,147	398	(1,064)	27	17,508