

**JSC BasisBank**

**Consolidated Financial Statements  
for the year ended 31 December 2010**

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## Independent Auditors' Report

To the Supervisory Board  
JSC BasisBank

We have audited the accompanying consolidated financial statements of JSC BasisBank (the "Bank") and its subsidiaries ("the Group"), which comprise the consolidated statement of financial position as at 31 December 2010, and the consolidated statements of comprehensive income, changes in equity and cash flows for the year then ended, and notes, comprising a summary of significant accounting policies and other explanatory information.

### *Management's Responsibility for the Financial Statements*

Management is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with International Financial Reporting Standards, and for such internal control as management determines is necessary to enable the preparation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

### *Auditors' Responsibility*

Our responsibility is to express an opinion on these consolidated 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 about whether the consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the consolidated 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 consolidated 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 consolidated 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 consolidated financial statements present fairly, in all material respects, the consolidated financial position of the Group as at 31 December 2010, and its consolidated financial performance and its consolidated cash flows for the year then ended in accordance with International Financial Reporting Standards.

*Tbilisi branch of KPMG CIS Limited*

Tbilisi Branch of KPMG CIS Limited  
6 May 2011

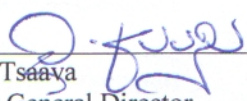


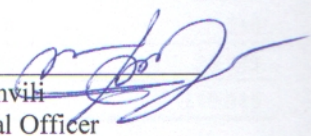


**JSC BasisBank**  
*Consolidated Statement of Comprehensive Income for the year ended 31 December 2010*

	Notes	2010 GEL'000	2009 GEL'000
Interest income	4	13,416	11,782
Interest expense	4	(6,606)	(5,372)
<b>Net interest income</b>		<b>6,810</b>	<b>6,410</b>
Fee and commission income	5	3,270	2,911
Fee and commission expense	6	(1,534)	(1,227)
<b>Net fee and commission income</b>		<b>1,736</b>	<b>1,684</b>
Net foreign exchange income	7	1,754	1,386
Other operating income	8	1,606	1,474
<b>Operating income</b>		<b>11,906</b>	<b>10,954</b>
Impairment losses	9	(1,100)	(4,379)
Personnel expenses	10	(4,998)	(4,487)
Other general administrative expenses	11	(3,738)	(4,176)
<b>Profit (loss) before income tax</b>		<b>2,070</b>	<b>(2,088)</b>
Income tax (expense)/benefit	12	(286)	134
<b>Profit (loss) for the year</b>		<b>1,784</b>	<b>(1,954)</b>
<b>Other comprehensive income, net of income tax</b>			
Revaluation of property and equipment, net of income tax		173	-
<b>Other comprehensive income for the year, net of income tax</b>		<b>173</b>	<b>-</b>
<b>Total comprehensive income for the year</b>		<b>1,957</b>	<b>(1,954)</b>
<b>Total comprehensive income attributable to:</b>			
- Equity holders of the Bank		1,957	(1,954)
- Non-controlling interests		-	-
<b>Total comprehensive income for the year</b>		<b>1,957</b>	<b>(1,954)</b>

The consolidated financial statements as set out on pages 4 to 54 were approved by the Board of Directors on 6 May 2011 and signed on its behalf by the management of the Bank:

  
 David Tsava  
 Acting General Director

  
 Lia Alsanikashvili  
 Chief Financial Officer

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

**JSC BasisBank**  
*Consolidated Statement of Financial Position as at 31 December 2010*

	Notes	2010 GEL'000	2009 GEL'000
<b>ASSETS</b>			
Cash		11,460	12,089
Due from the National Bank of Georgia	13	17,983	5,333
Placements with banks	14	5,190	15,514
Loans to customers	15	63,976	54,835
Available-for-sale assets	16	63	54
Held-to-maturity investments	17		
-Held by the Group		7,165	5,596
-Pledged under sale and repurchase agreements		2,085	-
Assets held for sale	18	2,338	4,469
Property and equipment	19	15,764	12,708
Intangible assets		275	183
Other assets	20	14,096	8,734
<b>Total assets</b>		<b>140,395</b>	<b>119,515</b>
<b>LIABILITIES</b>			
Deposits and balances from banks	21	394	924
Amounts payable under repurchase agreements	22	2,000	-
Current accounts and deposits from customers	23	95,877	81,416
Other borrowed funds	24	18,006	15,319
Deferred tax liability	12	551	235
Other liabilities	25	1,261	1,272
<b>Total liabilities</b>		<b>118,089</b>	<b>99,166</b>
<b>EQUITY</b>			
Share capital	26	5,912	5,912
Share premium		5,612	5,612
Revaluation surplus for property and equipment		2,361	2,188
Retained earnings		8,171	6,387
<b>Total equity attributable to equity holders of the Bank</b>		<b>22,056</b>	<b>20,099</b>
Non-controlling interests		250	250
<b>Total equity</b>		<b>22,306</b>	<b>20,349</b>
<b>Total liabilities and equity</b>		<b>140,395</b>	<b>119,515</b>

The consolidated statement of financial position is to be read in conjunction with the notes to, and forming part of, the consolidated financial statements.

**JSC Basis Bank**  
*Consolidated Statement of Cash Flows for the year ended 31 December 2010*

	Notes	2010 GEL'000	2009 GEL'000
<b>CASH FLOWS FROM OPERATING ACTIVITIES</b>			
Interest and fee and commission receipts		16,165	14,815
Interest and fee and commission payments		(7,594)	(6,413)
Net receipts from foreign exchange		1,754	1,371
Other income receipts		1,192	1,474
Personnel expenses and other general administrative expenses payments		(7,582)	(7,587)
Proceeds from disposal of repossessed assets		884	-
<b>(Increase) decrease in operating assets</b>			
Due from the National Bank of Georgia		(1,752)	(631)
Placements with banks		7,407	(4,438)
Loans to customers		(13,345)	(3,677)
Other assets		(1,546)	(1,549)
<b>Increase (decrease) in operating liabilities</b>			
Deposits and balances from banks		(469)	(5,953)
Amounts payable under repurchase agreements		2,000	(2,801)
Current accounts and deposits from customers		14,666	19,164
Other liabilities		(73)	487
<b>Cash flows from operations</b>		<b>11,707</b>	<b>4,262</b>
<b>CASH FLOWS FROM INVESTING ACTIVITIES</b>			
Purchases of held-to-maturity investments		(9,299)	(5,596)
Maturity of held-to-maturity investments		6,133	3,100
Purchases of property and equipment		(4,401)	(996)
Purchases of intangible assets		(127)	(50)
Proceeds from disposal of property and equipment		4	30
Prepayments for property and equipment		(174)	540
<b>Cash flows from investing activities</b>		<b>(7,864)</b>	<b>(2,972)</b>
<b>CASH FLOWS FROM FINANCING ACTIVITIES</b>			
Net receipts (repayments) of other borrowed funds		3,257	(149)
<b>Cash flows from/(used in) financing activities</b>		<b>3,257</b>	<b>(149)</b>
<b>Net increase in cash and cash equivalents</b>			
		<b>7,100</b>	<b>1,141</b>
Effect of changes in exchange rates on cash and cash equivalents		250	(27)
Cash and cash equivalents as at the beginning of the year		23,331	22,217
<b>Cash and cash equivalents as at the end of the year</b>	33	<b>30,681</b>	<b>23,331</b>

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

**JSC BasisBank**  
*Consolidated Statement of Changes in Equity for the year ended 31 December 2010*

	Attributable to equity holders of the Bank					Non-controlling interest GEL'000	Total equity GEL'000
	Share capital GEL'000	Share premium GEL'000	Revaluation surplus for property and equipment GEL'000	Retained earnings GEL'000	Total GEL'000		
<b>Balance as at 1 January 2009</b>	5,912	5,612	2,188	8,341	22,053	-	22,053
<b>Total comprehensive income</b>							
Loss for the year	-	-	-	(1,954)	(1,954)	-	(1,954)
<b>Total comprehensive income for the year</b>	-	-	-	(1,954)	(1,954)	-	(1,954)
Disposal of a non-controlling interest	-	-	-	-	-	250	250
<b>Balance at 31 December 2009</b>	<b>5,912</b>	<b>5,612</b>	<b>2,188</b>	<b>6,387</b>	<b>20,099</b>	<b>250</b>	<b>20,349</b>
 Balance as at 1 January 2010	 5,912	 5,612	 2,188	 6,387	 20,099	 250	 20,349
<b>Total comprehensive income</b>							
Profit for the year	-	-	-	1,784	1,784	-	1,784
<b>Other comprehensive income</b>							
Revaluation of property and equipment, net of income tax	-	-	173	-	173	-	173
Total other comprehensive income	-	-	173	-	173	-	173
<b>Total comprehensive income for the year</b>	-	-	173	1,784	1,957	-	1,957
<b>Balance at 31 December 2010</b>	<b>5,912</b>	<b>5,612</b>	<b>2,361</b>	<b>8,171</b>	<b>22,056</b>	<b>250</b>	<b>22,306</b>

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

# 1 Background

## (a) Organisation and operations

These consolidated financial statements include the financial statements of JSC BasisBank (the “Bank”) and its subsidiaries (together referred to as the “Group”). The principal subsidiaries of the Bank include asset management and construction companies.

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 National Bank of Georgia (“NBG”). The Bank has 18 branches operating in Georgia.

The registered address of the Bank is 1 Ketevan Tsamebuli Street, Tbilisi 0103, 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 270 (2009: 278).

On 28 September 2009 the Bank established a subsidiary – Basis Asset Management Limited, an asset management company with 100% ownership. On 29 September 2009 Basis Asset Management Limited acquired 75% of Paladi Imperial Partnership, a construction company.

The principal subsidiaries of the Bank are as follows:

Name	Country of incorporation	Principal activities	Ownership %	
			2010	2009
Basis Asset Management	Georgia	Asset management	100%	100%
Paladi Imperial	Georgia	Construction	75%	75%

## Shareholders

As at 31 December 2010 and 2009, the following individuals owned the share capital of the Bank:

Shareholders	2010	2009
	Ownership interest, %	Ownership interest, %
European Bank for Reconstruction and Development (EBRD)	15.00%	15.00%
Zurab Tsikhistavi	13.92%	13.92%
Eldar Mildiani	9.89%	9.89%
Zurab Nishnianidze	8.51%	8.51%
Murman Ambroladze	6.58%	6.58%
Archil Maziashvili	6.33%	6.33%
Ketevan Soselia	5.62%	5.62%
Taras Nijaradze	4.58%	4.58%
Gia Petriashvili	4.57%	4.57%
Giorgi Vachnadze	4.44%	4.44%
Goderzi Meladze	4.42%	4.42%
Tengiz Maziashvili	4.38%	4.38%
Other individuals	11.76%	11.76%
	<b>100.00%</b>	<b>100.00%</b>

Related party transactions are detailed in note 32.



**(b) Business environment**

**Georgian business environment**

Georgia is experiencing political and economic change that has affected, and may continue to affect, the activities of enterprises operating in this environment. The Group's operations and assets could be at risk as a result of negative changes in the political, economic or business environment within Georgia. Consequently, operations in Georgia involve risks that typically do not exist in other markets. In addition, the contraction in the capital and credit markets and its impact on the economy of Georgia have further increased the level of economic uncertainty in the environment. These consolidated financial statements reflect management's assessment of the impact of the Georgian business environment on the operations and the financial position of the Group. The future business environment may differ from management's assessment.

## **2 Basis of preparation**

**(a) Statement of compliance**

The accompanying consolidated financial statements are prepared in accordance with International Financial Reporting Standards (IFRS).

**(b) Basis of measurement**

The consolidated financial statements are prepared on the historical cost basis except that land and buildings are stated at revalued amounts.

**(c) Functional and presentation currency**

The functional currency of the Bank and its subsidiaries is the Georgian Lari ("GEL") as, being the national currency of Georgia, it reflects the economic substance of the majority of underlying events and circumstances relevant to them.

The GEL is also the presentation currency for the purposes of these consolidated financial statements.

Financial information presented in GEL is rounded to the nearest thousand.

**(d) Use of estimates and judgments**

Management makes 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 consolidated 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 notes:

- loan impairment estimates - note 15
- land and buildings revaluation estimates - note 19
- other assets impairment estimates - note 20

**(e) Changes in accounting policies and presentation**

With effect from 1 January 2010, the Group changed its accounting policies in the area of accounting for business combinations.

**(i) Accounting for business combinations**

From 1 January 2010 the Group has applied IFRS 3 *Business Combinations* (2008) in accounting for business combinations. The change in accounting policy has been applied prospectively and has had no material impact on the consolidated financial statements.

### **3 Significant accounting policies**

The accounting policies set out below are applied consistently to all periods presented in these consolidated financial statements, and are applied consistently by Group entities, except as explained in note 2(e), which addresses changes in accounting policies.

**(a) Basis of consolidation**

**(i) Subsidiaries**

Subsidiaries are entities controlled by the Bank. Control exists when the Bank has the power, directly or indirectly, to govern the financial and operating policies of an entity so as to obtain benefits from its activities. The financial statements of subsidiaries are included in the consolidated financial statements from the date that control effectively commences until the date that control effectively ceases.

**(ii) Transactions eliminated on consolidation**

Intra-group balances and transactions, and any unrealised gains arising from intra-group transactions, are eliminated in preparing the consolidated financial statements.

**(b) Non-controlling interests**

Non-controlling interests are the equity in a subsidiary not attributable, directly or indirectly, to the Bank.

Non-controlling interests are presented in the consolidated statement of financial position within equity, separately from the equity attributable to equity holders of the Bank. Non-controlling interests in profit or loss and total comprehensive income are separately disclosed in the consolidated statement of comprehensive income.

**(c) Foreign currency**

**(i) Foreign currency transactions**

Transactions in foreign currencies are translated to the respective functional currencies of the Group entities at exchange rates at the dates of the transactions. Monetary assets and liabilities denominated in foreign currencies at the reporting date are retranslated to the functional currency at the exchange rate at that date. The foreign currency gain or loss on monetary items is the difference

between amortised cost in the functional currency at the beginning of the period, adjusted for effective interest and payments during the period, and the amortised cost in foreign currency translated at the exchange rate at the end of the reporting period. Foreign currency differences arising on retranslation are recognised in profit or loss. Non-monetary items that are measured in terms of historical cost in a foreign currency are translated using the exchange rate at the date of the transaction.

**(d) Cash and cash equivalents**

Cash and cash equivalents include cash, notes and coins on hand, unrestricted balances (nostro accounts) held with the NBG and other banks. The mandatory reserve deposit with the NBG is not considered to be a cash equivalent due to restrictions on its withdrawability. Cash and cash equivalents are carried at amortised cost in the statement of financial position.

**(e) Financial instruments**

**(i) Classification**

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

*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 Group:

- intends to sell immediately or in the near term
- upon initial recognition designates as at fair value through profit or loss
- upon initial recognition designates as available-for-sale or,
- 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 Group has the positive intention and ability to hold to maturity, other than those that:

- the Group upon initial recognition designates as at fair value through profit or loss
- the Group designates as available-for-sale or,
- meet the definition of loans and receivables.

*Available-for-sale financial assets* are those non-derivative 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.

**(ii) Recognition**

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

**(iii) 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 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 that are measured at amortized cost using the effective interest method
- 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.

The amortised cost of a financial asset or liability is the amount at which the financial asset or liability is measured at initial recognition, minus principal repayments, plus or minus the cumulative amortisation using the effective interest method of any difference between the initial amount recognised and the maturity amount, minus any reduction for impairment. 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.

**(iv) Fair value measurement principles**

Fair value is the amount for which an asset could be exchanged, or a liability settled, between knowledgeable, willing parties in an arms's length transaction on the measurement date.

When available, the Group measures the fair value of an instrument using quoted prices in an active market for that instrument. A market is regarded as active if quoted prices are readily and regularly available and represent actual and regularly occurring market transactions on an arm's length basis.

If a market for a financial instrument is not active, the Group establishes fair value using a valuation technique. Valuation techniques include using recent arm's length transactions between knowledgeable, willing parties (if available), reference to the current fair value of other instruments that are substantially the same, discounted cash flow analyses and option pricing models. The chosen valuation technique makes maximum use of market inputs, relies as little as possible on estimates specific to the Group, incorporates all factors that market participants would consider in setting a price, and is consistent with accepted economic methodologies for pricing financial instruments. Inputs to valuation techniques reasonably represent market expectations and measures of the risk-return factors inherent in the financial instrument.

The best evidence of the fair value of a financial instrument at initial recognition is the transaction price, i.e., the fair value of the consideration given or received, unless the fair value of that instrument is evidenced by comparison with other observable current market transactions in the same instrument (i.e., without modification or repackaging) or based on a valuation technique whose variables include only data from observable markets. When transaction price provides the best evidence of fair value at initial recognition, the financial instrument is initially measured at the transaction price and any difference between this price and the value initially obtained from a

valuation model is subsequently recognised in profit or loss on an appropriate basis over the life of the instrument but not later than when the valuation is supported wholly by observable market data or the transaction is closed out.

**(v) *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 an available-for-sale financial asset is recognized as other comprehensive income in equity (except for impairment losses and foreign exchange gains and losses on debt financial instruments available-for-sale) until the asset is derecognized, at which time the cumulative gain or loss previously recognised in equity is recognized in profit or loss. Interest in relation to an available-for-sale financial asset is recognized in profit or loss using the effective interest method.

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

**(vi) *Derecognition***

The Group derecognises a financial asset when the contractual rights to the cash flows from the financial asset expire, or when it transfers the financial asset in a transaction in which substantially all the risks and rewards of ownership of the financial asset are transferred or in which the Group neither transfers nor retains substantially all the risks and rewards of ownership and it does not retain control of the financial asset. Any interest in transferred financial assets that qualify for derecognition that is created or retained by the Group is recognised as a separate asset or liability in the statement of financial position. The Group derecognises a financial liability when its contractual obligations are discharged or cancelled or expire.

The Group writes off assets deemed to be uncollectible.

**(vii) *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 consolidated statement of financial position and the counterparty liability included in amounts payable under repo transactions within deposits and balances from banks or current accounts and deposits from customers, as appropriate. The difference between the sale and repurchase prices represents interest expense and is recognized in profit or loss over the term of the repo agreement using the effective interest method.

Securities purchased under agreements to resell (reverse repo) are recorded as amounts receivable under reverse repo transactions within loans and advances to banks or loans to customers, as appropriate. The difference between the purchase and resale prices represents interest income and is recognized in profit or loss over the term of the repo agreement using the effective interest method.

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



***(viii) Offsetting***

Financial assets and liabilities are offset and the net amount reported in the consolidated statement of financial position 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.

**(f) Property and equipment**

***(i) Owned assets***

Items of property and equipment are stated at cost less accumulated depreciation and impairment losses, except for land and 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.

***(ii) Revaluation***

Land and buildings are subject to revaluation on a regular basis. The frequency of revaluation depends on the movements in the fair values of the land and buildings being revalued. A revaluation increase on land and buildings is recognised as other comprehensive income directly in equity except to the extent that it reverses a previous revaluation decrease recognised in profit or loss, in which case it is recognised in profit or loss. A revaluation decrease on a building is recognised in profit or loss except to the extent that it reverses a previous revaluation increase recognised as other comprehensive income directly in equity, in which case it is recognised directly in equity.

***(iii) Depreciation***

Depreciation is charged to profit or loss 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. Land is not depreciated. The estimated useful lives are as follows:

- Buildings	50 years
- computers and communication equipment	5 years
- fixtures and fittings	5 years
- motor vehicles	5 years
- leasehold improvements	2-3 years
- other	10 years

**(g) Intangible assets**

Acquired intangible assets 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 profit or loss on a straight-line basis over the estimated useful lives of intangible assets. The estimated useful life of intangible assets is 10 years.

**(h) Investment property**

Investment property is property held either to earn rental income or for capital appreciation or for both, but not for sale in ordinary course of business, or for the use in production or supply of goods or services or for administrative purposes. Investment property is measured at cost less accumulated depreciation and impairment losses.

Cost includes expenditure that is directly attributable to the acquisition of investment property. Cost includes the cost of materials and direct labour, any other costs directly attributable to bringing the asset to a working condition for its intended use.

When parts of an item of investment property have different useful lives, they are accounted for as separate items (major components) of investment property.

**(i) Assets held for sale**

Non-current assets, or disposal groups comprising assets and liabilities, that are expected to be recovered primarily through sale rather than through continuing use, are classified as held for sale. Immediately before classification as held for sale, the assets, or components of a disposal group, are remeasured in accordance with the Group's accounting policies. Thereafter generally, the assets, or disposal group, are measured at the lower of their carrying amount and fair value less cost to sell.

**(j) Repossessed assets**

The Group recognises repossessed assets in the statement of financial position when it has the full and final settlement right of the collateral, and when it is entitled to retain any excess proceeds from the realisation of the collateral.

Repossessed assets are measured at the lower of the carrying amount and the fair value less costs to sell. At initial recognition repossessed assets are measured based on the value of the defaulted loan, including expenditure incurred in the process of collateral foreclosure. Fair value less costs to sell is the estimated selling price of the collateral in the ordinary course of business, less the related selling costs. Subsequent to initial recognition, repossessed assets are reviewed for held for sale classification criteria and are reclassified accordingly when the criteria are met.

Repossessed assets are included in other assets.

Gains and losses on disposal of an item of repossessed assets are recognised net in "other operating income" in profit or loss.

**(k) Impairment**

***(i) Financial assets carried at amortized cost***

Financial assets carried at amortized cost consist principally of loans and other receivables (loans and receivables). The Group 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 on terms that the Group 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 Group 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 Group 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 Group uses its experience and judgement to estimate the amount of any impairment loss.

All impairment losses in respect of loans and receivables are recognized in profit or loss 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 uncollectable, it is written off against the related allowance for loan impairment. The Group writes off a loan balance (and any related allowances for loan losses) when management determines that the loans are uncollectible and when all necessary steps to collect the loan are completed.

**(ii) Financial assets carried at cost**

Financial assets carried at cost include unquoted equity instruments included in available-for-sale financial 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 profit or loss and can not be reversed.

**(iii) 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 profit or loss 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.

**(I) Credit related commitments**

In the normal course of business, the Group 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 Group 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 in other liabilities.

**(m) Share capital**

Ordinary shares are classified as equity.

**(i) Share premium**

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

**(ii) Dividends**

The ability of the Group 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.

**(n) Taxation**

Income tax comprises current and deferred tax. Income tax is recognised in profit or loss except to the extent that it relates to items of other comprehensive income or transactions with shareholders recognised directly in equity, in which case it is recognised within other comprehensive income or directly within 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 reporting date, and any adjustment to tax payable in respect of previous years.

Deferred tax is recognised in respect of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes. Deferred tax is not recognised for the following temporary differences: the initial recognition of assets or liabilities that affect neither accounting nor taxable profit and temporary differences related to investments in subsidiaries where the parent is able to control the timing of the reversal of the temporary difference and it is probable that the temporary difference will not reverse in the foreseeable future. Deferred tax is measured at the tax rates that are expected to be applied to the temporary differences when they reverse, based on the laws that have been enacted or substantively enacted by the reporting 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.

**(o) Income and expense recognition**

Interest income and expense are recognised in profit or loss 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 transaction costs, are deferred and amortized to interest income over the estimated life of the financial instrument using the effective interest method.



Other fees, commissions and other income and expense items are recognised in profit or loss when the corresponding service is provided.

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

**(p) 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 2010, and are not applied in preparing these consolidated financial statements. Of these pronouncements, potentially the following will have an impact on the financial position and performance. The Group plans to adopt these pronouncements when they become effective.

- Revised IAS 24 *Related Party Disclosures* (2009) introduces an exemption from the basic disclosure requirements in relation to related party disclosures and outstanding balances, including commitments, for government-related entities. Additionally, the standard has been revised to simplify some of the presentation guidance that was previously non-reciprocal. The revised standard is to be applied retrospectively for annual periods beginning on or after 1 January 2011.
- IFRS 9 *Financial Instruments* will be effective for annual periods beginning on or after 1 January 2013. The new standard is to be issued in several phases and is intended to replace International Financial Reporting Standard IAS 39 *Financial Instruments: Recognition and Measurement* once the project is completed by the end of 2010. The first phase of IFRS 9 was issued in November 2009 and relates to the recognition and measurement of financial assets.
- *Improvements to IFRSs 2010* resulting from the International Accounting Standards Board's third annual improvements project are to be dealt with on a standard-by-standard basis. The effective date of each amendment is included in the IFRSs affected.

## 4 Net interest income

	<b>2010</b> <b>GEL'000</b>	<b>2009</b> <b>GEL'000</b>
<b>Interest income</b>		
Loans to customers	12,788	11,584
Loans and advances to banks	137	66
Other interest income	491	132
	<b>13,416</b>	<b>11,782</b>
<b>Interest expense</b>		
Current accounts and deposits from customers	5,588	3,812
Other borrowed funds	968	1,166
Deposits and balances from banks	50	394
	<b>6,606</b>	<b>5,372</b>

## 5 Fee and commission income

	<b>2010</b> <b>GEL'000</b>	<b>2009</b> <b>GEL'000</b>
Credit facilities	1,094	734
Plastic card fees	933	1,236
Settlement fees	558	354
Account maintenance and cash operations fees	458	381
Other	227	206
	<b>3,270</b>	<b>2,911</b>

## 6 Fee and commission expense

	<b>2010</b> <b>GEL'000</b>	<b>2009</b> <b>GEL'000</b>
Plastic card system fees	980	885
Settlement fees	202	166
Other	352	176
	<b>1,534</b>	<b>1,227</b>

## 7 Net foreign exchange income

	<b>2010</b> <b>GEL'000</b>	<b>2009</b> <b>GEL'000</b>
Gain on spot transactions	1,754	1,371
Net gain from revaluation of financial assets and liabilities	-	15
	<b>1,754</b>	<b>1,386</b>

## 8 Other operating income

	2010 GEL'000	2009 GEL'000
Fines and penalties received	1,142	1,447
Fines and penalties paid	(55)	(29)
Gain on disposal of repossessed assets	423	-
Other	96	56
	<b>1,606</b>	<b>1,474</b>

## 9 Impairment losses

	2010 GEL'000	2009 GEL'000
Loans to customers (note 15)	(1,228)	1,212
Assets held for sale (note 18)	577	-
Other assets (note 20)	1,751	3,167
	<b>1,100</b>	<b>4,379</b>

## 10 Personnel expenses

	2010 GEL'000	2009 GEL'000
Employee compensation	3,998	3,589
Payroll related taxes	1,000	898
	<b>4,998</b>	<b>4,487</b>

## 11 Other general administrative expenses

	2010 GEL'000	2009 GEL'000
Depreciation and amortization	1,136	1,121
Occupancy	540	516
Professional services	490	396
Security	462	604
Advertising and marketing	304	657
Communications and information services	154	146
Taxes other than on income	167	137
Office supplies	119	118
Repairs and maintenance	49	36
Insurance	28	88
Travel and training	12	17
Other	277	340
	<b>3,738</b>	<b>4,176</b>

## 12 Income tax (expense)/benefit

	2010 GEL'000	2009 GEL'000
<b>Current tax expense</b>		
Current year	-	-
	-	-
<b>Deferred tax (expense)/benefit</b>		
Origination and reversal of temporary differences	(286)	134
<b>Total income tax (expense)/benefit</b>	<b>(286)</b>	<b>134</b>

In 2010, applicable tax rate for current and deferred tax is 15% (2009: 15%).

### Reconciliation of effective tax rate:

	2010 GEL'000	%	2009 GEL'000	%
Profit/(loss) before income tax	2,070		(2,088)	
Income tax at the applicable tax rate	311	15%	(313)	15%
(Non-taxable income)/non-deductible costs	(25)	(1%)	179	(9%)
	<b>286</b>	<b>14%</b>	<b>(134)</b>	<b>6%</b>

### (a) 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 2010 and 2009.

Movements in temporary differences during the years ended 31 December 2010 and 2009 are presented as follows:

GEL'000	Balance 1 January 2010	Recognised in income	Recognised in other comprehensive income	Balance 31 December 2010
Loans to customers	(143)	143	-	-
Property and equipment	(1,495)	115	(30)	(1,410)
Other assets	450	284	-	734
Other liabilities	47	12	-	59
Tax loss carry-forwards	906	(840)	-	66
	<b>(235)</b>	<b>(286)</b>	<b>(30)</b>	<b>(551)</b>

GEL'000	Balance 1 January 2009	Recognised in income	Balance 31 December 2009
Loans to customers	303	(446)	(143)
Property and equipment	(1,436)	(59)	(1,495)
Other assets	-	450	450
Other liabilities	66	(19)	47
Tax loss carry-forwards	698	208	906
	<b>(369)</b>	<b>134</b>	<b>(235)</b>

Tax loss carry forwards amount to GEL 66 thousand as at 31 December 2010 (2009: GEL 906 thousand). Of these losses, GEL 66 thousand expire in 2014.

**(b) Income tax recognised in other comprehensive income**

The tax effects relating to components of other comprehensive income for the year ended 31 December comprise the following:

	2010			2009		
	Amount before tax	Tax expense	Amount net-of-tax	Amount before tax	Tax expense	Amount net-of-tax
<b>GEL'000</b>						
Revaluation of property and equipment	203	(30)	173	-	-	-
<b>Other comprehensive income</b>	<b>203</b>	<b>(30)</b>	<b>173</b>	<b>-</b>	<b>-</b>	<b>-</b>

## **13 Due from the National Bank of Georgia**

	2010	2009
	GEL'000	GEL'000
Nostro accounts	14,373	3,446
Mandatory minimum reserve deposit	3,610	1,887
	<b>17,983</b>	<b>5,333</b>

The minimum reserve deposit is a mandatory interest bearing deposit in foreign currency calculated in accordance with the regulations issued by the 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 restricted, however the Bank is subject to penalties if the average required balance is not maintained over a 14 day period.



## 14 Placements with banks

	<b>2010</b> <b>GEL'000</b>	<b>2009</b> <b>GEL'000</b>
<b>Nostro accounts</b>		
- rated AA- to AA+	758	1,471
- rated A- to A+	442	1,083
- rated Aa3	2,352	3,563
- rated B	232	184
- not rated	1,064	1,495
<b>Total nostro accounts</b>	<b>4,848</b>	<b>7,796</b>
 <b>Deposits and other advances to banks</b>		
- rated AA- to AA+	342	341
- rated BB- to BB+	-	3,372
- rated B	-	4,005
<b>Total deposits and other advances to banks</b>	<b>342</b>	<b>7,718</b>
	<b>5,190</b>	<b>15,514</b>

None of cash and cash equivalents are impaired or past due. The above ratings are per Fitch rating agency ratings.

Included in deposits and other advances to banks is GEL 342 thousand (2009: GEL 341 thousand) which represents a blocked deposit for plastic card settlements.

As at 31 December 2010 the Group has one bank (2009: 3 banks), whose balances exceed 10% of equity. The gross value of these balances as at 31 December 2010 is GEL 2,352 thousand (2009: GEL 10,934 thousand).

## 15 Loans to customers

	<b>2010</b> <b>GEL'000</b>	<b>2009</b> <b>GEL'000</b>
<b>Loans to corporate customers</b>	<b>31,913</b>	<b>28,964</b>
 <b>Loans to retail customers</b>		
Loans collateralized by real estate	19,373	12,963
Credit cards	6,607	8,009
Auto loans	1,104	1,158
Other consumer loans	7,201	6,973
<b>Total loans to retail customers</b>	<b>34,285</b>	<b>29,103</b>
 <b>Gross loans to customers</b>	<b>66,198</b>	<b>58,067</b>
Impairment allowance	(2,222)	(3,232)
<b>Net loans to customers</b>	<b>63,976</b>	<b>54,835</b>

Movements in the loan impairment allowance by classes of loans to customers for the year ended 31 December 2010 are as follows:

	Loans to corporate customers GEL'000	Loans to retail customers GEL'000	Total GEL'000
Balance at the beginning of the year	2,154	1,078	3,232
Net reversal	(536)	(692)	(1,228)
(Write-offs)/recoveries	(613)	831	218
<b>Balance at the end of the year</b>	<b>1,005</b>	<b>1,217</b>	<b>2,222</b>

Movements in the loan impairment allowance by classes of loans to customers for the year ended 31 December 2009 are as follows:

	Loans to corporate customers GEL'000	Loans to retail customers GEL'000	Total GEL'000
Balance at the beginning of the year	3,002	2,279	5,281
Net charge (reversal)	(532)	1,744	1,212
Write-offs	(316)	(2,945)	(3,261)
<b>Balance at the end of the year</b>	<b>2,154</b>	<b>1,078</b>	<b>3,232</b>

**(a) Credit quality of loans to customers**

The following table provides information on the credit quality of loans to customers as at 31 December 2010:

	Gross loans GEL'000	Impairment allowance GEL'000	Net loans GEL'000	Impairment allowance to gross loans, %
<b>Loans corporate customers</b>				
Loans without individual signs of impairment				
- not overdue	27,279	612	26,667	2.2%
- watch list loans	795	16	779	2.0%
Impaired loans:				
- not overdue	2,118	124	1,994	5.9%
- overdue less than 90 days	1,235	122	1,113	9.9%
- overdue more than 90 days and less than 1 year	486	131	355	27.0%
Total impaired loans	3,839	377	3,462	9.8%
<b>Total loans to corporate customers</b>	<b>31,913</b>	<b>1,005</b>	<b>30,908</b>	<b>3.1%</b>

	Gross loans GEL'000	Impairment allowance GEL'000	Net loans GEL'000	Impairment allowance to gross loans, %
<b>Loans to retail customers</b>				
<b>Loans collateralized by real estate</b>				
- not overdue	17,593	649	16,944	3.7%
- overdue less than 30 days	868	39	829	4.5%
- overdue 30-89 days	727	67	660	9.2%
- overdue 90-179 days	185	48	137	25.9%
<b>Total loans collateralized by real estate</b>	<b>19,373</b>	<b>803</b>	<b>18,570</b>	<b>4.1%</b>
<b>Credit cards</b>				
- not overdue	6,461	139	6,322	2.2%
- overdue less than 30 days	69	6	63	8.7%
- overdue 30-89 days	62	23	39	37.1%
- overdue 90-179 days	15	7	8	46.7%
<b>Total credit cards</b>	<b>6,607</b>	<b>175</b>	<b>6,432</b>	<b>2.6%</b>
<b>Auto loans</b>				
- not overdue	1,057	22	1,035	2.1%
- overdue less than 30 days	19	1	18	5.3%
- overdue 30-89 days	25	5	20	20.0%
- overdue 90-179 days	3	1	2	33.3%
<b>Total auto loans</b>	<b>1,104</b>	<b>29</b>	<b>1,075</b>	<b>2.6%</b>
<b>Other consumer loans</b>				
- not overdue	6,947	190	6,757	2.7%
- overdue less than 30 days	201	6	195	3.0%
- overdue 30-89 days	40	8	32	20.0%
- overdue 90-179 days	13	6	7	46.2%
<b>Total other consumer loans</b>	<b>7,201</b>	<b>210</b>	<b>6,991</b>	<b>2.9%</b>
<b>Total loans to retail customers</b>	<b>34,285</b>	<b>1,217</b>	<b>33,068</b>	<b>3.5%</b>
<b>Total loans to customers</b>	<b>66,198</b>	<b>2,222</b>	<b>63,976</b>	<b>3.4%</b>

The following table provides information on the credit quality of the loans to customers portfolio as at 31 December 2009:

	Gross loans GEL'000	Impairment allowance GEL'000	Net loans GEL'000	Impairment allowance to gross loans, %
<b>Loans to corporate customers</b>				
Loans without individual signs of impairment				
- not overdue	22,818	452	22,366	2.0%
- watch list loans	336	7	329	2.1%
Impaired loans:				
- not overdue	3,552	645	2,907	18.2%
- overdue less than 90 days	2,171	963	1,208	44.4%
- overdue more than 90 days and less than 1 year	87	87	-	100%
Total impaired loans	5,810	1,695	4,115	29.2%
<b>Total loans to corporate customers</b>	<b>28,964</b>	<b>2,154</b>	<b>26,810</b>	<b>7.4%</b>
<b>Loans to retail customers</b>				
<b>Loans collateralized by real estate</b>				
- not overdue	11,891	357	11,534	3.0%
- overdue less than 30 days	654	25	629	3.8%
- overdue 30-89 days	221	37	184	16.7%
- overdue 90-179 days	191	63	128	33.0%
- overdue more than 360 days	6	1	5	16.7%
<b>Total loans collateralized by real estate</b>	<b>12,963</b>	<b>483</b>	<b>12,480</b>	<b>3.7%</b>
<b>Credit cards</b>				
- not overdue	7,805	234	7,571	3.0%
- overdue less than 30 days	43	7	36	16.3%
- overdue 30-89 days	135	49	86	36.3%
- overdue 90-179 days	16	9	7	56.3%
- overdue 180-360 days	10	10	-	100.0%
<b>Total credit cards</b>	<b>8,009</b>	<b>309</b>	<b>7,700</b>	<b>3.9%</b>
<b>Auto loans</b>				
- not overdue	1,104	33	1,071	3.0%
- overdue less than 30 days	39	3	36	7.7%
- overdue 90-179 days	15	6	9	40.0%
<b>Total auto loans</b>	<b>1,158</b>	<b>42</b>	<b>1,116</b>	<b>3.6%</b>
<b>Other consumer loans</b>				
- not overdue	6,656	200	6,456	3.0%
- overdue less than 30 days	207	13	194	6.3%
- overdue 30-89 days	70	11	59	15.7%
- overdue 90-179 days	37	17	20	45.9%
- overdue 180-360 days	2	2	-	100.0%
- overdue more than 360 days	1	1	-	100.0%
<b>Total consumer loans</b>	<b>6,973</b>	<b>244</b>	<b>6,729</b>	<b>3.5%</b>
<b>Total loans to retail customers</b>	<b>29,103</b>	<b>1,078</b>	<b>28,025</b>	<b>3.7%</b>
<b>Total loans to customers</b>	<b>58,067</b>	<b>3,232</b>	<b>54,835</b>	<b>5.6%</b>

As at 31 December 2010 included in the loan portfolio are loans to corporate and retail customers that would otherwise be past due or impaired of GEL 4,751 thousand and GEL 3,620 thousand, respectively (2009: GEL 4,411 thousand of loans to corporate customers). Such restructuring activity is aimed at managing customer relationships and maximising collection opportunities. Renegotiated loans are included in the category of assets without individual signs of impairment in the tables above, unless the borrower fails to comply with the renegotiated terms.

**(b) Key assumptions and judgments for estimating the loan impairment**

**(i) Loans to corporate customers**

Loan impairment results from one or more events that occurred after the initial recognition of the loan and that have an impact on the estimated future cash flows associated with the loan, and which can be reliably estimated. Loans without individual signs of impairment do not have objective evidence of impairment that can be directly attributed to them.

The objective indicators of loan impairment include the following:

- overdue payments under the loan agreement
- significant difficulties in the financial conditions of the borrower
- deterioration in business environment, negative changes in the borrower's markets

The Group estimates loan impairment for loans to corporate customers based on an analysis of the future cash flows for impaired loans and based on its past loss experience for portfolios of loans for which no indications of impairment has been identified.

In determining the impairment allowance for loans to corporate customers, management makes the following key assumptions:

- for non-impaired loans the Group creates a collective provision of 2% (2009: 2%) based on the expected loss rate of the Group and other comparable banks in Georgia
- for impaired loans a discount of 25% to the originally appraised value if the property pledged is sold and a delay of 36 months on average in obtaining proceeds from the foreclosure of collateral.

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 minus one percent, the impairment allowance on loans to corporate customers as at 31 December 2010 would be GEL 309 thousand higher (2009: GEL 268 thousand higher).

**(ii) Loans to retail customers**

The Group estimates loan impairment for loans to retail customers based on its past historical loss experience on each type of loan. The significant assumptions used by management in determining the impairment losses for loans to retail customers include:

- loss migration rates are constant and can be estimated based on the historic loss migration pattern for the past 24 months for loans collateralised by real estate, auto loans and other consumer loans.
- loans to individuals overdue for more than 180 days are allocated 100% probability of loss.

The significant assumptions used in determining the impairment losses for loans to individuals include the following loan loss rates:

- Loans collateralized by real estate – 4.1%
- Credit cards – 2.6%
- Auto loans – 2.6%
- Other consumer loans – 2.9%

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 minus three percent, the impairment allowance on loans to retail customers as at 31 December 2010 would be GEL 992 thousand higher (2009: GEL 840 thousand).

**(c) Analysis of collateral**

**(i) Loans to corporate customers**

The following table provides the analysis of loans to corporate customers portfolio, net of impairment, by types of collateral as at 31 December 2010:

	<b>2010</b> <b>GEL'000</b>	<b>% of loan</b> <b>portfolio</b>	<b>2009</b> <b>GEL'000</b>	<b>% of loan</b> <b>portfolio</b>
Real estate	23,460	76%	18,363	68%
Third party guarantee	2,037	7%	2,414	9%
Equipment and motor vehicles	800	2%	2,089	8%
Cash	4,197	14%	2,267	9%
Inventories	-	-	809	3%
Other collateral	-	-	23	-
No collateral	414	1%	845	3%
	<b>30,908</b>	<b>100%</b>	<b>26,810</b>	<b>100%</b>

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.

Impaired or overdue loans to corporate customers with a gross value of GEL 4,517 thousand (2009: GEL 5,695 thousand) are secured by collateral with a fair value of GEL 16,062 thousand (2009: GEL 13,433 thousand). For the remaining impaired loans of GEL 203 thousand (2009: GEL 115 thousand), there is no collateral or it is impracticable to determine the fair value of collateral.

During the year ended 31 December 2010 the Group obtained assets with the carrying amount of GEL 3,989 thousand by taking control of collateral securing loans to corporate customers (2009: GEL 11,247 thousand)

**(ii) Loans to retail customers**

Mortgage loans are secured by the underlying housing real estate. Auto loans are secured by the underlying cars, other consumer loans are secured by different types of collateral. Credit card overdrafts are not secured.

Impaired or overdue loans to retail customers with a gross value of GEL 1,828 thousand (2009: GEL 1,395 thousand) are secured by collateral with a fair value of GEL 7,222 thousand (2009: GEL 3,483 thousand). For the remaining impaired loans of GEL 398 thousand (2009: GEL 252 thousand), there is no collateral or it is impracticable to determine the fair value of collateral. The Bank estimates that the fair value of the collaterals for loans to individuals is at least equal to the carrying amount of the loans.

**(d) Industry and geographical analysis of the loan portfolio**

Loans to customers were issued primarily to customers located within the Georgia who operate in the following economic sectors:

	<b>2010</b> <b>GEL'000</b>	<b>2009</b> <b>GEL'000</b>
Trade and services	18,218	10,640
Education	4,306	2,595
Mining/metallurgy and production	3,662	5,403
Construction	2,803	4,995
Transportation and communication	807	1,720
Agriculture	466	710
Energy	147	308
Other	499	439
Loans to retail customers	33,068	28,025
<b>Total loans to customers</b>	<b>63,976</b>	<b>54,835</b>

**(e) Significant credit exposures**

As at 31 December 2010 and 2009 the Group did not have borrowers or groups of connected borrowers whose loan balances exceed 10% of equity.

**(f) Loan maturities**

The maturity of the loan portfolio is presented in note 27(d), which shows the remaining period from the reporting date to the contractual maturity of the loans. Due to the short-term nature of the loans issued by the Group, it is likely that many of the loans will be prolonged at maturity. Accordingly, the effective maturity of the loan portfolio may be significantly longer than the term based on contractual terms.

## 16 Available-for-sale financial assets

	2010 GEL'000	2009 GEL'000
<b>Equity instruments – Unquoted</b>		
Corporate shares	63	54
	<b>63</b>	<b>54</b>

No available-for-sale financial assets are past due or impaired.

### Investment without a determinable fair value

Available-for-sale equity instruments stated at cost comprise unquoted equity securities in the financial services industry in Georgia. 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.

## 17 Held-to-maturity investments

	2010 GEL'000	2009 GEL'000
<b><i>Held by the Group</i></b>		
<b>Debt and other fixed-income instruments</b>		
Georgian Government bonds	2,165	5,596
NBG deposit certificates	5,000	-
	<b>7,165</b>	<b>5,596</b>
<b><i>Pledged under sale and repurchase agreements</i></b>		
<b>Debt and other fixed-income instruments</b>		
NBG deposit certificates	2,085	-
	<b>2,085</b>	<b>-</b>

No held to maturity investments are past due or impaired.



## 18 Assets held for sale

In 2010 the Group's management committed to sell property, plant and equipment of GEL 2,338 thousand. Efforts to sell the assets have commenced, and a sale is highly probable in 2011.

Assets held for sale of GEL 4,469 as at 31 December 2009 were reclassified to repossessed assets in 2010 as the assets no longer meet the held for sale classification criteria.

During the year an impairment loss of GEL 577 thousand on the remeasurement of the disposal group to the lower of its carrying amount and its fair value less costs to sell has been recognised in impairment loss (see note 9).

As at 31 December 2010 management believes that the carrying amount of assets and liabilities of the disposal group approximately equals to its fair value less costs to sell.

	<b>2010</b>	<b>2009</b>
	<b>GEL'000</b>	<b>GEL'000</b>
<b>Assets classified as held for sale</b>		
Land and buildings	2338	2,762
Construction in progress	-	1,707
	<b>2,338</b>	<b>4,469</b>

The table below presents the movement in the assets held for sale for the year ended 31 December 2010:

<b>'000 GEL</b>	<b>2010</b>
<b>Assets held for sale as at the beginning of the year</b>	<b>4,469</b>
Transferred to repossessed assets	(4,469)
Transferred from repossessed assets	2,915
Impairment loss (note 9)	(577)
<b>Assets held for sale as at the end of the year</b>	<b>2,338</b>

## 19 Property and equipment

<b>GEL'000</b>	<b>Land and Buildings</b>	<b>Computers and communication equipment</b>	<b>Fixtures and fittings</b>	<b>Motor vehicles</b>	<b>Leasehold improvements</b>	<b>Other</b>	<b>Total</b>
<b>Cost/revalued amount</b>							
At 1 January 2010	10,612	3,866	884	131	129	134	15,756
Additions	4,236	119	39	-	4	3	4,401
Disposals	-	(49)	(22)	-	(8)	(10)	(89)
Transfer to investment property	(440)	-	-	-	-	-	(440)
Revaluation	(525)	-	-	-	-	-	(525)
<b>At 31 December 2010</b>	<b>13,883</b>	<b>3,936</b>	<b>901</b>	<b>131</b>	<b>125</b>	<b>127</b>	<b>19,103</b>
<b>Depreciation</b>							
At 1 January 2010	517	1,981	382	79	46	43	3,048
Depreciation charge	215	724	117	27	2	14	1,099
Disposals	-	(50)	(22)	-	(2)	(2)	(76)
Transfer to investment property	(4)	-	-	-	-	-	(4)
Revaluation	(728)	-	-	-	-	-	(728)
<b>At 31 December 2010</b>	<b>-</b>	<b>2,655</b>	<b>477</b>	<b>106</b>	<b>46</b>	<b>55</b>	<b>3,339</b>
<b>Carrying value</b>							
<b>At 31 December 2010</b>	<b>13,883</b>	<b>1,281</b>	<b>424</b>	<b>25</b>	<b>79</b>	<b>72</b>	<b>15,764</b>
<b>Cost/revalued amount</b>							
At 1 January 2009	10,487	3,286	873	122	120	105	14,993
Acquisitions through assets purchase	2,762	-	-	-	-	-	2,762
Additions	125	771	53	9	9	29	996
Disposals	-	(191)	(42)	-	-	-	(233)
Transfer to assets held for sale	(2,762)	-	-	-	-	-	(2,762)
<b>At 31 December 2009</b>	<b>10,612</b>	<b>3,866</b>	<b>884</b>	<b>131</b>	<b>129</b>	<b>134</b>	<b>15,756</b>
<b>Depreciation</b>							
At 1 January 2009	301	1,424	307	53	45	30	2,160
Depreciation charge	216	719	116	26	1	13	1,091
Disposals	-	(162)	(41)	-	-	-	(203)
<b>At 31 December 2009</b>	<b>517</b>	<b>1,981</b>	<b>382</b>	<b>79</b>	<b>46</b>	<b>43</b>	<b>3,048</b>
<b>Carrying value</b>							
<b>At 31 December 2009</b>	<b>10,095</b>	<b>1,885</b>	<b>502</b>	<b>52</b>	<b>83</b>	<b>91</b>	<b>12,708</b>

### (a) Revalued assets

At 31 December 2010 land and buildings were revalued by management based on the results of an independent appraisal performed by Georgian Valuation Company Ltd. The basis used for the appraisal was market approach. The market approach was based upon an analysis of results of comparable sales and recent market transactions of similar land and buildings.

The carrying value of land and buildings as at 31 December 2010, if the land and buildings would not have been revalued, would be GEL 11,367 thousand (2009: GEL 7,621 thousand).

Included in land and buildings are the 2nd and 3rd floors of the head office building on 1 Ketevan Tsamebuli Street acquired by the Group in an auction organized by the Ministry of Georgia of Economic Development on 23 March 2010. The purchase consideration was settled by the Group assuming the liability to finance the construction of the Ministry of Justice building. The liability was determined to be GEL 3,114 thousand and the outstanding part of the liability was GEL 68 thousand as at 31 December 2010. The ownership of the floors acquired is restricted until the liability for construction has been extinguished.

## 20 Other assets

	2010 GEL'000	2009 GEL'000
Accounts receivable	564	300
Receivables from payments processing systems	101	187
Other financial receivables	460	335
Impairment allowance	(147)	-
<b>Total other financial assets</b>	<b>978</b>	<b>822</b>
Reposessed assets	13,205	8,804
Prepayments for property and equipment	1,382	1,208
Prepayments	1,112	545
Taxes other than income tax, recoverable	1,422	1,055
Investment property	436	-
Impairment allowance on reposessed assets	(4,439)	(3,700)
<b>Total other non-financial assets</b>	<b>13,118</b>	<b>7,912</b>
<b>Total other assets</b>	<b>14,096</b>	<b>8,734</b>

### (a) Analysis of movements in the impairment allowance

Movements in the impairment allowance for the year ended 31 December 2010 and 2009 are as follows:

	2010 GEL'000	2009 GEL'000
Balance at the beginning of the year	3,700	533
Net charge (note 9)	1,751	3,167
Transfer to assets held for sale	865	-
<b>Balance at the end of the year</b>	<b>4,586</b>	<b>3,700</b>

The nature and carrying value of repossessed assets as at 31 December 2010 and 2009 were as follows:

	Carrying value 31 December 2010 GEL'000	Carrying value 31 December 2009 GEL'000
Land and buildings	7,059	3,286
Construction in progress	1,707	1,818
	<b>8,766</b>	<b>5,104</b>

During the year, repossessed assets of GEL 2,915 thousand (2009: GEL 1,707 thousand), representing land and buildings (2009: construction in progress), were transferred to assets classified as held for sale.

Repossessed assets with carrying value of GEL 461 thousand (2009: none) were disposed during the year.

Management believes that the carrying amount of repossessed assets approximately equals to their fair value less costs to sell as at 31 December 2010.

Repossessed assets with a carrying value of GEL 312 thousand (2009: 4,082 thousand) are restricted for different time periods by the end of which the borrowers can re-purchase back the assets from the Group.

## 21 Deposits and balances from banks

	2010 GEL'000	2009 GEL'000
Vostro accounts	394	924

## 22 Amounts payable under repurchase agreements

	2010 GEL'000	2009 GEL'000
Amounts due to NBG	2,000	-

### (a) Collateral

As of 31 December 2010, amounts payable under repurchase agreements were collateralised by the following securities:

	2010 GEL'000	2009 GEL'000
NBG deposit certificates	2,085	-

## 23 Current accounts and deposits from customers

	<b>2010</b> <b>GEL'000</b>	<b>2009</b> <b>GEL'000</b>
Current accounts	37,004	36,732
Demand deposits	26,553	21,814
Term deposits	32,320	22,870
	<b>95,877</b>	<b>81,416</b>

As at 31 December 2010, the Group maintains customer deposit balances of GEL 7,358 thousand (2009: GEL 7,022 thousand) that serve as collateral for loans and off-balance sheet credit instruments granted by the Group.

As at 31 December 2010, the Group has five customers (2009: 4 customers), whose balances exceed 10% of equity. These balances as at 31 December 2010 are GEL 14,025 thousand (2009: GEL 12,020 thousand).

## 24 Other borrowed funds

	<b>2010</b> <b>GEL'000</b>	<b>2009</b> <b>GEL'000</b>
Loans from World Business Capital	8,864	2,529
Loans from European Bank for Reconstruction and Development (EBRD)	7,813	10,409
Loan from Ministry of Finance	1,225	2,253
Other	104	128
	<b>18,006</b>	<b>15,319</b>

## 25 Other liabilities

	<b>2010</b> <b>GEL'000</b>	<b>2009</b> <b>GEL'000</b>
Payables for payments processing systems	448	984
Accrued expenses	57	39
Other financial liabilities	267	24
<b>Total other financial liabilities</b>	<b>772</b>	<b>1,047</b>
Taxes payable, other than income tax	489	225
<b>Total other non-financial liabilities</b>	<b>489</b>	<b>225</b>
<b>Total other liabilities</b>	<b>1,261</b>	<b>1,272</b>

## **26 Equity**

### **(a) Issued capital and share premium**

The authorized share capital comprises 6,700,000 ordinary shares (2009: 6,700,000), with a par value of GEL 1 per share, from which 5,912,000 were issued, paid and outstanding as at 31 December 2010 (2009: 5,912,000).

During 2008, the Group 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 Group.

### **(b) Dividends**

Dividends payable are restricted to the maximum retained earnings of the Group less general reserves as recorded in the Group's statutory accounts, which are determined according to the legislation of Georgia. Subsequent to 31 December 2010 no dividends have been declared by the Group.

## **27 Risk management**

Management of risk is fundamental to the business of banking and is an essential element of the Group's operations. The major risks faced by the Group are those related to market risk, credit risk and liquidity risk.

### **(a) Risk management policies and procedures**

The risk management policies aim to identify, analyse and manage the risks faced by the Group, 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 Group 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 Group is responsible for monitoring and implementation of risk mitigation measures and making sure that the Group operates 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 Group 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 Group'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 Risk Department monitors financial and non-financial risks by holding regular meetings with operational units in order to obtain expert judgments in their areas of expertise.

### **(b) Market risk**

Market risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in market prices. Market risk comprises currency risk, interest rate risk and other price risks. 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 Group. Market risk limits are approved by Management Board based on recommendations of the Treasury Department.

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

**(i) Interest rate risk**

Interest rate risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in market interest rates. The Group 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 occur.

**Interest rate gap analysis**

Interest rate risk is managed principally through monitoring interest rate gaps. A summary of the interest gap position for major financial instruments is as follows:

<b>GEL '000</b>	<b>Less than 1 month</b>	<b>1-3 months</b>	<b>3-12 months</b>	<b>1-5 years</b>	<b>More than 5 years</b>	<b>Carrying amount</b>
<b>31 December 2010</b>						
<b>ASSETS</b>						
Cash	11,460	-	-	-	-	11,460
Due from National Bank of Georgia	17,983	-	-	-	-	17,983
Placements with banks	5,190	-	-	-	-	5,190
Loans to customers	4,744	7,070	20,410	28,410	3,342	63,976
Available-for-sale assets	-	-	-	-	63	63
Held-to-maturity investments	-	7,085	2,165	-	-	9,250
	<b>39,377</b>	<b>14,155</b>	<b>22,575</b>	<b>28,410</b>	<b>3,405</b>	<b>107,922</b>
<b>LIABILITIES</b>						
Deposits and balances from banks	394	-	-	-	-	394
Amounts payable under repurchase agreements	-	-	2,000	-	-	2,000
Current accounts and deposits from customers	65,125	8,140	18,613	3,712	287	95,877
Other borrowed funds	-	1,735	2,017	9,897	4,357	18,006
	<b>65,519</b>	<b>9,875</b>	<b>22,630</b>	<b>13,609</b>	<b>4,644</b>	<b>116,277</b>
	<b>(26,142)</b>	<b>4,280</b>	<b>(55)</b>	<b>14,801</b>	<b>(1,239)</b>	<b>(8,355)</b>
<b>31 December 2009</b>						
<b>ASSETS</b>						
Cash	12,089	-	-	-	-	12,089
Due from National Bank of Georgia	5,333	-	-	-	-	5,333
Placements with banks	15,514	-	-	-	-	15,514
Loans to customers	3,913	5,741	23,690	19,802	1,689	54,835
Available-for-sale assets	-	-	-	-	54	54
Held-to-maturity investments	-	-	5,596	-	-	5,596
	<b>36,849</b>	<b>5,741</b>	<b>29,286</b>	<b>19,802</b>	<b>1,743</b>	<b>93,421</b>



GEL '000	Less than 1 month	1-3 months	3-12 months	1-5 years	More than 5 years	Carrying amount
<b>LIABILITIES</b>						
Deposits and balances from banks	924	-	-	-	-	924
Current accounts and deposits from customers	56,892	4,608	16,707	2,726	483	81,416
Other borrowed funds	2,278	1,734	1,445	8,252	1,610	15,319
	<b>60,094</b>	<b>6,342</b>	<b>18,152</b>	<b>10,978</b>	<b>2,093</b>	<b>97,659</b>
	<b>(23,245)</b>	<b>(601)</b>	<b>11,134</b>	<b>8,824</b>	<b>(350)</b>	<b>(4,238)</b>

### Average interest rates

The table below displays average effective interest rates for interest bearing assets and liabilities as at 31 December 2010 and 2009. These interest rates are an approximation of the yields to maturity of these assets and liabilities.

	2010			2009		
	Average effective interest rate, %			Average effective interest rate, %		
	GEL	USD	Other currencies	GEL	USD	Other currencies
<b>Interest bearing assets</b>						
Due from the National Bank of Georgia	0%	0.5%	0.5%	0%	0.5%	0.5%
Nostro accounts with banks	-	-	1%	1%	-	-
Placements with banks	-	-	-	4%	4%	-
Loans to customers	16%	18%	18%	18%	20%	20%
Held-to-maturity investments	10%	-	-	8%	-	-
<b>Interest bearing liabilities</b>						
Deposits and balances from banks	7%	-	-	3%	-	-
- Amounts payable under repurchase agreements	8%	-	-	-	-	-
Current accounts and deposits from customers						
- Current accounts and demand deposits	4%	4%	1%	4%	5%	1%
- Term deposits	10%	10%	10%	12%	11%	11%
Other borrowed funds	-	5%	0%	6%	-	-

### **Interest rate sensitivity analysis**

The management of interest rate risk based on interest rate gap analysis is supplemented by monitoring the sensitivity of financial assets and liabilities. An analysis of sensitivity of profit or loss and equity (net of taxes) to changes in interest rate repricing risk 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 2010 and 2009 is as follows:

	<b>2010</b>		<b>2009</b>	
	<b>Profit or loss GEL'000</b>	<b>Equity GEL'000</b>	<b>Profit or loss GEL'000</b>	<b>Equity GEL'000</b>
100 bp parallel fall	414	414	(47)	(47)
100 bp parallel rise	(414)	(414)	47	47

### **(ii) Currency risk**

The Group has assets and liabilities denominated in several foreign currencies.

Currency risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in market interest rates. The Group does not hedge its exposure to currency risk.

The following table shows the foreign currency exposure structure of financial assets and liabilities as at 31 December 2010:

	<b>GEL GEL'000</b>	<b>USD GEL'000</b>	<b>EUR GEL'000</b>	<b>Others GEL'000</b>	<b>Total GEL'000</b>
<b>Assets</b>					
Cash	5,044	3,104	3,090	222	11,460
Due from the National Bank of Georgia	4,006	9,696	4,281	-	17,983
Placements with banks	10	3,479	1,508	193	5,190
Loans to customers	18,328	40,316	5,324	8	63,976
Available-for-sale assets	63	-	-	-	63
Held to maturity investments	9,250	-	-	-	9,250
Other financial assets	876	51	51	-	978
<b>Total assets</b>	<b>37,577</b>	<b>56,646</b>	<b>14,254</b>	<b>423</b>	<b>108,900</b>
<b>Liabilities</b>					
Deposits and balances from banks	387	6	1	-	394
Amounts payable under repurchase agreements	2,000	-	-	-	2,000
Current accounts and deposits from customers	39,941	41,156	14,360	420	95,877
Other borrowed funds	98	17,908	-	-	18,006
Other financial liabilities	674	68	29	1	772
<b>Total liabilities</b>	<b>43,100</b>	<b>59,138</b>	<b>14,390</b>	<b>421</b>	<b>117,049</b>
<b>Net position as at 31 December 2010</b>	<b>(5,523)</b>	<b>(2,492)</b>	<b>(136)</b>	<b>2</b>	<b>(8,149)</b>

The following table shows the currency structure of financial assets and liabilities as at 31 December 2009:

	<b>GEL</b>	<b>USD</b>	<b>EUR</b>	<b>Others</b>	<b>Total</b>
	<b>GEL'000</b>	<b>GEL'000</b>	<b>GEL'000</b>	<b>GEL'000</b>	<b>GEL'000</b>
<b>Assets</b>					
Cash	6,012	3,130	2,884	63	12,089
Due from the National Bank of Georgia	3,089	1,632	607	5	5,333
Placements with banks	4,017	8,736	2,502	259	15,514
Loans to customers	22,318	28,900	3,608	9	54,835
Available-for-sale assets	54	-	-	-	54
Held to maturity investments	5,596	-	-	-	5,596
Other financial assets	150	636	36	-	822
<b>Total assets</b>	<b>41,236</b>	<b>43,034</b>	<b>9,637</b>	<b>336</b>	<b>94,243</b>
<b>Liabilities</b>					
Deposits and balances from banks	923	1	-	-	924
Current accounts and deposits from customers	42,329	29,299	9,515	273	81,416
Other borrowed funds	128	15,191	-	-	15,319
Other financial liabilities	151	656	211	29	1,047
<b>Total liabilities</b>	<b>43,531</b>	<b>45,147</b>	<b>9,726</b>	<b>302</b>	<b>98,706</b>
<b>Net position as at 31 December 2009</b>	<b>(2,295)</b>	<b>(2,113)</b>	<b>(89)</b>	<b>34</b>	<b>(4,463)</b>

A strengthening of the GEL, as indicated below, against the following currencies at 31 December 2010 and 2009 would have increased (decreased) equity and profit or loss by the amounts shown below. This analysis is on net of tax basis and is based on foreign currency exchange rate variances that the Group considered to be reasonably possible at the end of the reporting period. The analysis assumes that all other variables, in particular interest rates, remain constant.

	<b>2010</b>		<b>2009</b>	
	<b>Profit or loss GEL'000</b>	<b>Equity GEL'000</b>	<b>Profit or loss GEL'000</b>	<b>Equity GEL'000</b>
10% appreciation of USD against GEL	(212)	(212)	(180)	(180)
10% appreciation of EUR against GEL	(12)	(12)	(8)	(8)

A weakening of the GEL against the above currencies at 31 December 2010 and 2009 would have had the equal but opposite effect on the above currencies to the amounts shown above, on the basis that all other variables remain constant.

**(c) Credit risk**

Credit risk is the risk of financial loss to the Group if a customer or counterparty to a financial instrument fails to meet its contractual obligations. The Group has policies and procedures for the management of credit exposures (both for recognised financial assets and unrecognised contractual commitments), including guidelines to limit portfolio concentration and the establishment of a Credit Committee, which actively monitors credit risk. The credit policy is reviewed and approved by the Management Board.

The credit policy establishes:

- procedures for review and approval of loan credit applications
- methodology for the credit assessment of borrowers (corporate 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 Group's Legal, Accounting and Tax departments depending on the specific risks and pending final approval of the Credit Committee.

The Group 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 Group. The current market value of collateral is regularly assessed by either independent appraisal companies or the Group'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.

During the year the Group negotiated a four year guarantee agreement from the U.S. Agency for International Development (USAID) to cover 50% of losses in respect of qualifying loans. Qualifying loans include loans to small and medium size corporate customers with the condition that 35% of the qualifying portfolio is represented by agricultural loans. According to the guarantee agreement the aggregate principal amount outstanding of all qualifying loans covered at any one time shall not exceed USD 6 million. As at 31 December 2010 no qualifying loans were advanced to customers.

The maximum exposure to credit risk is generally reflected in the carrying amounts of financial assets on the consolidated statement of financial position and unrecognised contractual commitments. The impact of possible netting of assets and liabilities to reduce potential credit exposure is not significant.

The maximum exposure to credit risk from financial assets at the reporting date is as follows:

	<b>2010</b> <b>GEL'000</b>	<b>2009</b> <b>GEL'000</b>
<b>ASSETS</b>		
Due from National Bank of Georgia	17,983	5,333
Placements with banks	5,190	15,514
Loans to customers	63,976	54,835
Available-for-sale assets	63	54
Held-to-maturity investments	9,250	5,596
Other financial assets	978	822
<b>Total maximum exposure</b>	<b>97,440</b>	<b>82,154</b>

For the analysis of concentration of credit risk in respect of loans to customers refer to note 15.

The maximum exposure to credit risk from unrecognised contractual commitments at the reporting date is presented in note 29.

#### **(d) Liquidity risk**

Liquidity risk is the risk that the Group will encounter difficulty in meeting obligations associated with its financial liabilities that are settled by delivering cash or another financial asset. 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 liquidity management. 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 Group 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 liquidity policy is reviewed and approved by the Management Board.

The Group 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 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 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 Group 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 are presented to senior management on a weekly basis. Decisions on liquidity management are made by the Management Board and implemented by the Treasury Department.

The following tables show the undiscounted cash flows on financial assets and liabilities and credit-related commitments on the basis of their earliest possible contractual maturity. The total gross inflow and outflow disclosed in the tables is the contractual, undiscounted cash flow on the financial asset, liability or commitment.

The maturity analysis for financial liabilities as at 31 December 2010 is as follows:

	<b>Demand and less than 1 month</b>	<b>From 1 to 3 months</b>	<b>From 3 to 6 months</b>	<b>From 6 to 12 months</b>	<b>More than 1 year</b>	<b>Total gross amount outflow (inflow)</b>	<b>Carrying amount</b>
<b>GEL'000</b>							
<b>Non-derivative liabilities</b>							
Deposits and balances from banks	394	-	-	-	-	394	394
Amounts payable under repurchase agreements	-	-	2,063	-	-	2,063	2,000
Current accounts and deposits from customers	65,358	8,527	12,474	6,798	4,832	97,989	95,877
Other borrowed funds	-	1,792	-	2,565	15,935	20,292	18,006
Other financial liabilities	448	324	-	-	-	772	772
<b>Total liabilities</b>	<b>66,200</b>	<b>10,643</b>	<b>14,537</b>	<b>9,363</b>	<b>20,767</b>	<b>121,510</b>	<b>117,049</b>
<b>Credit related commitments</b>	<b>11,890</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>11,890</b>	<b>11,890</b>

The maturity analysis for financial liabilities as at 31 December 2009 is as follows:

	<b>Demand and less than 1 month</b>	<b>From 1 to 3 months</b>	<b>From 3 to 6 months</b>	<b>From 6 to 12 months</b>	<b>More than 1 year</b>	<b>Total gross amount outflow (inflow)</b>	<b>Carrying amount</b>
<b>GEL'000</b>							
<b>Non-derivative liabilities</b>							
Deposits and balances from banks	924	-	-	-	-	924	924
Current accounts and deposits from customers	57,186	4,852	3,700	14,030	4,013	83,781	81,416
Other borrowed funds	2,278	1,832	24	1,805	11,114	17,053	15,319
Other financial liabilities	875	51	-	91	30	1,047	1,047
<b>Total</b>	<b>61,263</b>	<b>6,735</b>	<b>3,724</b>	<b>15,926</b>	<b>15,157</b>	<b>102,805</b>	<b>98,706</b>
<b>Credit related commitments</b>	<b>17,167</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>17,167</b>	<b>17,167</b>

The tables above show the undiscounted cash flows of non-derivative financial liabilities, including unrecognised loan commitments on the basis of their earliest possible contractual maturity.

In accordance with Georgian legislation, individuals can withdraw their term deposits at any time, forfeiting in most of the cases the accrued interest. These deposits are classified in accordance with their stated maturity dates. The amount of such deposits, by each time band, is as follows:

- less than 1 month: GEL 1,177 thousand (2009: GEL 1,018 thousand)
- from 1 to 3 months: GEL 3,633 thousand (2009: GEL 2,645 thousand)
- from 3 to 6 months: GEL 4,341 thousand (2009: GEL 1,993 thousand)
- from 6 to 12 months: GEL 4,225 thousand (2009: GEL 3,971 thousand)
- more than one year: GEL 3,084 thousand (2009: GEL 2,567 thousand)

The table below shows an analysis, by expected maturities, of the amounts recognised in the statement of financial position as at 31 December 2010:

GEL'000	Demand and less than 1 month	From 1 to 3 months	From 3 to 12 months	From 1 to 5 years	More than 5 years	No maturity	Overdue	Total
<b>Non-derivative assets</b>								
Cash	11,460	-	-	-	-	-	-	11,460
Due from the National Bank of Georgia	17,983	-	-	-	-	-	-	17,983
Placements with banks	5,190	-	-	-	-	-	-	5,190
Loans to customers	3,837	7,070	20,410	28,410	3,342	-	907	63,976
Available-for-sale assets	-	-	-	-	-	63	-	63
Held to maturity investments	-	7,085	2,165	-	-	-	-	9,250
Assets held for sale	-	-	2,338	-	-	-	-	2,338
Property and equipment	-	-	-	-	-	15,764	-	15,764
Intangible assets	-	-	-	-	-	275	-	275
Other assets	2,050	1,422	-	1,422	-	9,202	-	14,096
<b>Total assets</b>	<b>40,520</b>	<b>15,577</b>	<b>24,913</b>	<b>29,832</b>	<b>3,342</b>	<b>25,304</b>	<b>907</b>	<b>140,395</b>
<b>Non-derivative liabilities</b>								
Deposits and balances from banks	394	-	-	-	-	-	-	394
Amounts payable under repurchase agreements	-	-	2,000	-	-	-	-	2,000
Current accounts and deposits from customers	65,125	8,140	18,613	3,712	287	-	-	95,877
Other borrowed funds	-	1,735	2,017	9,897	4,357	-	-	18,006
Deferred tax liability	-	-	-	-	-	551	-	551
Other liabilities	448	813	-	-	-	-	-	1,261
<b>Total liabilities</b>	<b>65,967</b>	<b>10,688</b>	<b>22,630</b>	<b>13,609</b>	<b>4,644</b>	<b>551</b>	<b>-</b>	<b>118,089</b>
<b>Net position</b>	<b>(25,447)</b>	<b>4,889</b>	<b>2,283</b>	<b>16,223</b>	<b>(1,302)</b>	<b>24,753</b>	<b>907</b>	<b>22,306</b>



The table below shows an analysis, by expected maturities, of the amounts recognised in the statement of financial position as at 31 December 2009:

<b>GEL'000</b>	<b>Demand and less than 1 month</b>	<b>From 1 to 3 months</b>	<b>From 3 to 12 months</b>	<b>From 1 to 5 years</b>	<b>More than 5 years</b>	<b>No maturity</b>	<b>Overdue</b>	<b>Total</b>
<b>Non-derivative assets</b>								
Cash	12,089	-	-	-	-	-	-	12,089
Due from the National Bank of Georgia	5,333	-	-	-	-	-	-	5,333
Placements with banks	15,514	-	-	-	-	-	-	15,514
Loans to customers	3,248	5,741	23,690	19,802	1,689	-	665	54,835
Available-for-sale assets	-	-	-	-	-	54	-	54
Held to maturity investments	-	-	5,596	-	-	-	-	5,596
Assets held for sale	-	-	4,469	-	-	-	-	4,469
Property and equipment	-	-	-	-	-	12,708	-	12,708
Intangible assets	-	-	-	-	-	183	-	183
Other assets	2,122	-	300	1,208	-	5,104	-	8,734
<b>Total assets</b>	<b>38,306</b>	<b>5,741</b>	<b>34,055</b>	<b>21,010</b>	<b>1,689</b>	<b>18,049</b>	<b>665</b>	<b>119,515</b>
<b>Non-derivative liabilities</b>								
Deposits and balances from banks	924	-	-	-	-	-	-	924
Current accounts and deposits from customers	56,892	4,608	16,707	2,726	483	-	-	81,416
Other borrowed funds	2,278	1,734	1,445	8,252	1,610	-	-	15,319
Deferred tax liability	-	-	-	-	-	235	-	235
Other liabilities	1,100	51	91	30	-	-	-	1,272
<b>Total liabilities</b>	<b>61,194</b>	<b>6,393</b>	<b>18,243</b>	<b>11,008</b>	<b>2,093</b>	<b>235</b>	<b>-</b>	<b>99,166</b>
<b>Net position</b>	<b>(22,888)</b>	<b>(652)</b>	<b>15,812</b>	<b>10,002</b>	<b>(404)</b>	<b>17,814</b>	<b>665</b>	<b>20,349</b>

The key measure used by the Group for managing liquidity risk is the ratio of net liquid assets to deposits from customers. For this purpose net liquid assets include cash and cash equivalents and investment grade debt securities for which there is an active and liquid market less any deposits from banks, other borrowings and commitments maturing within the next month. The reported ratios of net liquid assets to deposits from customers at the reporting date are as follows:

	<b>2010</b> <b>GEL'000</b>	<b>2009</b> <b>GEL'000</b>
Ratio of net liquid assets to deposits from customers	30%	22%

A similar, but not identical, calculation is used to measure compliance with the liquidity limit established by the NBG.

## 28 Capital management

The NBG sets and monitors capital requirements for the Bank.

The Group 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 2010, this minimum level is 12%. The Group was in compliance with the statutory capital ratio during the years ended 31 December 2010 and 31 December 2009.

The following table shows the composition of the capital position calculated in accordance with the requirements of the NBG, as at 31 December:

	<b>2010</b> <b>GEL'000</b>	<b>2009</b> <b>GEL'000</b>
	<b>Unaudited</b>	<b>Unaudited</b>
<b>Primary capital</b>		
Share capital	5,912	5,912
Share premium	5,612	5,612
Retained earnings according to the NBG regulations	6,220	7,855
Deductions	(275)	(183)
<b>Total primary capital</b>	<b>17,469</b>	<b>19,196</b>
<b>Secondary capital</b>		
Profit/(loss) for the year according to NBG regulations	1,818	(2,422)
General reserve	1,167	1,163
<b>Total secondary capital</b>	<b>2,985</b>	<b>(1,259)</b>
Deductions	(2,627)	(15)
<b>Total authorized capital</b>	<b>17,827</b>	<b>17,922</b>
<b>Risk weighted assets, combining credit, market and operational risks</b>	<b>118,343</b>	<b>111,586</b>
<b>Total capital ratio</b>	<b>15.1%</b>	<b>16.1%</b>

The risk-weighted assets are measured by means of a hierarchy of risk weights classified according to the nature and reflecting an estimate of credit, market and other risks associated with each asset and counterparty, taking into account any eligible collateral or guarantees. A similar treatment is adopted for unrecognised contractual commitments, with some adjustments, to reflect the more contingent nature of the potential losses.

## 29 Commitments

The Group has outstanding commitments to extend loans. These commitments take the form of approved loans and credit card limits and overdraft facilities.

The Group 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 Group also provides guarantees by acting as settlement agent in securities borrowing and lending transactions.

The Group applies the same credit risk management policies and procedures when granting credit commitments, financial guarantees and letters of credit as it does for granting loans to customers.

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 reporting date if counterparties failed completely to perform as contracted.

	<b>2010</b> <b>GEL'000</b>	<b>2009</b> <b>GEL'000</b>
<b>Contracted amount</b>		
Guarantees	7,177	10,160
Undrawn credit line commitments	3,116	2,230
Undrawn overdraft facilities	1,597	4,416
Letters of credit	-	361
	<b>11,890</b>	<b>17,167</b>

The total outstanding contractual commitments above do not necessarily represent future cash requirements, as these commitments may expire or terminate without being funded.

As of 31 December 2010 and 2009, the Group had no customers, whose balances exceed 10% of total commitments.

## 30 Operating leases

### (a) Leases as lessee

Non-cancelable operating lease rentals as at 31 December are payable as follows:

	<b>2010</b> <b>GEL'000</b>	<b>2009</b> <b>GEL'000</b>
Less than 1 year	95	492
Between 1 and 5 years	133	97
	<b>228</b>	<b>589</b>

The Group leases a number of premises and equipment 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. Lease payments are usually increased annually to reflect market rentals. None of the leases includes contingent rentals.

## **31 Contingencies**

### **(a) 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 Group does not have full coverage for its equipment, business interruption, or third party liability in respect of property or environmental damage arising from accidents on Group's property or relating to the Group's operations. Until the Group obtains adequate insurance coverage, there is a risk that the loss or destruction of certain assets could have a material adverse effect on the Group's operations and financial position.

### **(b) Litigation**

In the ordinary course of business, the Group 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.

### **(c) 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 Group, if the authorities were successful in enforcing their interpretations, could be significant.

## 32 Related party transactions

### (a) Transactions with the members of the Board of Directors and the Management Board

Total remuneration included in personnel expenses for the year ended 31 December is as follows:

	<b>2010</b> <b>GEL'000</b>	<b>2009</b> <b>GEL'000</b>
Members of the Supervisory Board	227	339
Members of the Management Board	472	589
	<b>699</b>	<b>928</b>

The outstanding balances and average interest rates as of 31 December for transactions with the members of the Board of Directors and the Management Board are as follows:

	<b>2010</b> <b>GEL'000</b>	<b>Average</b> <b>interest rate,</b> <b>%</b>	<b>2009</b> <b>GEL'000</b>	<b>Average</b> <b>interest rate,</b> <b>%</b>
<b>Consolidated statement of financial position</b>				
<b>ASSETS</b>				
Loans to customers	566	17%	748	17%
Other assets	-	-	300	-
<b>LIABILITIES</b>				
Current accounts and deposits from customers	107	4%	531	4%

Amounts included in profit or loss in relation to other transactions with the members of the Supervisory Board and the Management Board for the year ended 31 December are as follows:

	<b>2010</b> <b>GEL'000</b>	<b>2009</b> <b>GEL'000</b>
<b>Profit or loss</b>		
Interest income	13	17
Interest expense	(16)	(53)

**(b) Transactions with other related parties**

The outstanding balances and the related average interest rates as of 31 December 2010 and related profit or loss amounts of transactions for the year ended 31 December 2010 with other related parties are as follows:

	Entities with significant influence over the Group		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
<b>Consolidated statement of financial position</b>							
<b>ASSETS</b>							
Loans to customers	291	19%	267	15%	428	16%	672
<b>LIABILITIES</b>							
Current accounts and deposits from customers	365	7%	620	4%	433	1%	948
Other borrowed funds	7,813	7%	-	-	-	-	7,813
<b>Profit (loss)</b>							
Interest income	15		1		5		6
Interest expense	(394)		(66)		(10)		(421)
Personnel expenses	(21)		-		-		-

The outstanding balances and the related average interest rates as of 31 December 2009 and related profit or loss amounts of transactions for the year ended 31 December 2009 with other related parties are as follows:

	Entities with significant influence over the Group		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
<b>Consolidated statement of financial position</b>							
<b>ASSETS</b>							
Loans to customers	-	-	244	19%	82	21%	326
<b>LIABILITIES</b>							
Current accounts and deposits from customers	-	-	446	6%	464	1%	910
Other borrowed funds	10,409	7%	-	-	-	-	10,409
<b>Profit (loss)</b>							
Interest income	-		12		14		26
Interest expense	(730)		(36)		(27)		(793)

### 33 Cash and cash equivalents

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

	<b>2010</b> <b>GEL'000</b>	<b>2009</b> <b>GEL'000</b>
Cash	11,460	12,089
Due from the National Bank of Georgia – nostro accounts	14,373	3,446
Placements with banks – nostro accounts	4,848	7,796
	<b>30,681</b>	<b>23,331</b>

### 34 Fair value of financial instruments

Management believes that the fair value of the Company's financial assets and liabilities approximates their carrying amounts.

As disclosed in note 16 the fair value of unquoted equity securities with a carrying value of GEL 63 thousand (2009: GEL 54 thousand) could not be determined.