JSC TBC Bank

Financial statements
Year ended December 31, 2002

Together with report of independent auditors

ERNST & YOUNG

Ernst & Young (CIS) Limited
Podsosensky Pereulok 20/12
Moscow 103062 Russia
Phone: 7 (095) 705 92 92
Fax: 7 (095) 705 92 93

Эрнст энд Янг (СНГ) Лимитед
Россия, 103062 Москва
Подсосенский переулок, 20/12
Телефон: 7 (095) 705 92 92
Факс: 7 (095) 705 92 93
ОКПО 40128555

Report of Independent Auditors

To the Shareholders of JSC TBC Bank –

We have audited the accompanying balance sheet of JSC TBC Bank (the "Bank") as of December 31, 2002, and related statements of income, changes in shareholders' equity and cash flow for the year then ended. These financial statements are the responsibility of the Bank's management. Our responsibility is to express an opinion on these financial statements based on our audit. The financial statements of the Bank as of December 31, 2001, were audited by other auditors, whose report dated February 18, 2002, expressed an unqualified opinion on those financial statements.

We conducted our audit in accordance with International Standards on Auditing. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Bank as of December 31, 2002, and the results of its operations and its cash flow for the year then ended in accordance with International Financial Reporting Standards as published by the International Accounting Standards Board.

February 17, 2003

Ernst & Young (CIS) Limited

JSC TBC Bank

Balance Sheets

(Thousands of Georgian Lari)

	Notes	December 31, 2002	December 31, 2001
Assets			
Cash and due from National Bank	5	36,358	17,865
Amounts due from credit institutions	6	33,178	15,444
Investment securities:			
– available-for-sale	7	2,942	6,385
– held-to-maturity	7	3,643	-
Loans to customers	8	101,166	72,503
Tax assets	9	33	-
Investments in associates	10	675	336
Property and equipment	12	8,408	4,533
Intangible assets	13	344	331
Other assets	14	1,321	1,423
Total assets		**188,068**	**118,820**
Liabilities			
Amounts owed to credit institutions	15	20,620	25,949
Amounts owed to customers	16	133,524	70,098
Tax liabilities	9	788	413
Provisions	11	525	259
Other liabilities	14	2,265	1,259
Total liabilities		**157,722**	**97,978**
Shareholders' equity			
Share capital		5,000	5,000
Additional paid-in capital		2,298	2,298
Retained earnings and reserves		23,048	13,544
Total shareholders' equity	17	**30,346**	**20,842**
Total liabilities and shareholders' equity		**188,068**	**118,820**
Financial commitments and contingencies	18	**18,230**	**6,634**

Signed and authorized for release on behalf of the Board of Directors

Vakhtang Butskhrikidze General Director

Vano Baliashvili Deputy General Director

February 17, 2003

The accompanying notes are an integral part of these financial statements.

JSC TBC Bank

Statements of Income
Years ended December 31, 2002 and 2001

(Thousands of Georgian Lari)

	Notes	2002	2001
Interest income			
Loans to customers		20,303	16,769
Amounts due from credit institutions		1,616	1,016
Debt securities		1,785	15
		23,704	**17,800**
Interest expense			
Amounts owed to customers		5,640	3,243
Amounts owed to credit institutions		1,584	1,642
		7,224	**4,885**
Net interest income		**16,480**	**12,915**
Impairment of interest earning assets		2,282	3,644
		14,198	**9,271**
Fees and commissions income		7,274	5,411
Fees and commissions expense		1,036	591
Fees and commissions, net		**6,238**	**4,820**
Foreign exchange gains, net		2,111	1,708
Translation gains (losses), net		(177)	2
Dealing profits, net		917	-
Dividend income		201	86
Other operating income		1,377	822
Non interest income		**4,429**	**2,618**
Losses from affiliated undertakings		**275**	**207**
Salaries and employment benefits	**19**	6,431	4,126
Administrative expenses	**19**	4,315	3,453
Depreciation and amortization		935	573
Other provisions (reversal)	**11**	(272)	1,164
Other operating expenses		371	928
Non interest expense		**11,780**	**10,244**
Income before taxation		**12,810**	**6,258**
Income tax expense	**9**	2,306	1,760
Net income		**10,504**	**4,498**

The accompanying notes are an integral part of these financial statements.

JSC TBC Bank

Statements of Changes in Shareholders' Equity
Years ended December 31, 2002 and 2001

(Thousands of Georgian Lari)

	Share capital (nominal)	Additional paid-in capital	Retained earnings	Total shareholders' equity
December 31, 2000	**5,000**	**2,298**	**9,046**	**16,344**
Net income	-	-	4,498	4,498
December 31, 2001	**5,000**	**2,298**	**13,544**	**20,842**
Dividends	-	-	(1,000)	(1,000)
Net income	-	-	10,504	10,504
December 31, 2002	**5,000**	**2,298**	**23,048**	**30,346**

The accompanying notes are an integral part of these financial statements.

JSC TBC Bank

Statements of Cash Flow
Years ended December 31, 2002 and 2001

(Thousands of Georgian Lari)

	Notes	2002	2001
Cash flows from operating activities			
Interest, fees and commissions received		30,620	23,759
Interest, fees and commissions paid		(7,655)	(5,217)
Dividends received		201	82
Dealing gains		917	-
Foreign exchange gains		2,111	1,708
Receipts from other operating activities		1,377	826
Salaries and employment benefits		(5,668)	(3,389)
Administrative expenses		(4,072)	(3,335)
Other operating expenses		(371)	(928)
Cash flows from operating profits before changes in operating assets and liabilities		**17,460**	**13,506**
(Increase) decrease in operating assets			
Obligatory reserve with National Bank		(8,260)	(3,234)
Amounts due from credit institutions		(1,506)	1,124
Loans to customers		(29,801)	(23,286)
Other assets		21	(903)
Increase (decrease) in operating liabilities			
Amounts owed to credit institutions		(6,599)	8,044
Amounts owed to customers		61,560	14,675
Other liabilities		-	(118)
Net cash flows from operating activities before profit taxes		**32,875**	**9,808**
Corporate income tax paid		(1,964)	(1,146)
Net cash flows from operating activities		**30,911**	**8,662**
Cash flows from investing activities			
Investment securities purchased		(3,846)	(4,416)
Investment securities sold		1,456	-
Equity investments purchased		(339)	-
Property and equipment purchased		(2,092)	(2,160)
Property and equipment sold		-	181
Intangible assets purchased		(197)	(274)
Net cash flows from investing activities		**(5,018)**	**(6,669)**
Cash flows from financing activities			
Dividends paid		(1,000)	-
Net cash flows from financing activities		**(1,000)**	**-**
Effects of exchange rate changes on cash and cash equivalents		235	99
Change in cash and cash equivalents		**25,128**	**2,092**
Cash and cash equivalents, beginning		**22,226**	**20,134**
Cash and cash equivalents, ending	**20**	**47,354**	**22,226**

The accompanying notes are an integral part of these financial statements.

NOTE 1 – PRINCIPAL ACTIVITIES

TBC Bank (the "Bank") was formed on December 17, 1992, as a joint stock company under the laws of Georgia. The Bank possesses general banking license №85 from the National Bank of Georgia ("NBG"), granted on January 20, 1993. The Bank accepts deposits from the public and makes loans, transfers payments in Georgia and abroad, exchanges currencies and provides banking services for its commercial and retail customers.

The Bank is the largest bank in Georgia in terms of assets calculated under the local accounting rules. Its main office is in Tbilisi and it has nine branches in Tbilisi, Rustavi, Kutaisi, Poti, Borjomi and Telavi. The Bank's registered legal address is 121, Rustaveli Street, 383720 Borjomi, Georgia.

As of December 31, 2002, three shareholders owned 50.94% of the outstanding shares. The Bank had an average of 331 employees during the year (2001 – 249) and 381 employees at the end of 2002 (2001 – 288).

NOTE 2 – OPERATING ENVIRONMENT

Georgia continues to undergo substantial political, economic and social changes. As an emerging market, Georgia does not possess a well-developed business and regulatory infrastructure that would generally exist in a more mature market economy. Furthermore, the Georgian Government has not yet fully implemented the reforms necessary to create banking, judicial, taxation and regulatory systems that usually exist in more developed markets. As a result, operations in Georgia involve risks that are not typically associated with those in developed markets. Such risks persist in the current environment with results that include but are not limited to, a currency that is not freely convertible outside of the country, onerous currency controls and low liquidity levels for debt and equity markets.

The Bank could be affected, for the foreseeable future, by these risks and their consequences. As a result, there are significant uncertainties that may affect future operations, the recoverability of the Bank's assets, and the ability of the Bank to maintain or pay its debts as they mature. The accompanying financial statements do not include any adjustments that may result from the future clarification of these uncertainties. Such adjustments, if any, will be reported in the Bank's financial statements in the period when they become known and estimable.

NOTE 3 – BASIS OF PRESENTATION

a) General
The financial statements have been prepared in accordance with International Financial Reporting Standards as published by the International Accounting Standards Board ("IFRS") and are presented in thousands of Georgian Lari ("GEL"), unless otherwise indicated.

The Bank is required to maintain its records and prepare its financial statements for regulatory purposes in Georgian Lari in accordance with IFRS and banking legislation. The financial statements are prepared under the historical cost convention modified for the measurement at fair value of available-for-sale investment securities.

The preparation of financial statements in conformity with IFRS requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosures of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

b) Adoption of International Accounting Standard ("IAS") 39
Effective January 31, 2001, the Bank adopted IAS 39 "Financial instruments: Recognition and Measurement". The accounting policies relating to originated loans to other banks and to customers, investment securities, amounts owed to credit institutions and to customers, and estimation of allowance for impairment of financial assets have been changed to conform to this standard.

Prior to adoption of IAS 39, securities, except for trading securities, were measured at cost, providing only for permanent diminution in value.

NOTE 4 – PRINCIPAL ACCOUNTING POLICIES

a) Cash and cash equivalents

Cash and cash equivalents are recognized and measured at the fair value of consideration received. Cash and cash equivalents consist of cash on hand and amounts due from the NBG – excluding obligatory reserves, and credit institutions that mature within ninety days of the date of origination and are free from contractual encumbrances.

b) Amounts due from credit institutions

In the normal course of business, the Bank maintains current accounts or deposits for various periods of time with other banks. Amounts due from credit institutions with a fixed maturity term are subsequently re-measured at amortized cost using the effective interest rate method. Those that do not have fixed maturities are carried at cost. Amounts due from credit institutions are carried net of any allowance for impairment.

c) Recognition of financial instruments

The Bank recognizes financial assets and liabilities on its balance sheet when, and only when, it becomes a party to the contractual provisions of the instrument. Financial assets and liabilities are recognized using trade date accounting.

Financial assets and liabilities are initially recognized at cost, which is the fair value of consideration given or received, respectively, including or net of any transaction costs incurred, respectively. The accounting policies for subsequent re-measurement of these items are disclosed in the respective accounting policies set out in the note.

d) Investment securities

Following the adoption of IAS 39 as of January 1, 2001, the Bank classified its investment securities into two categories:

- Securities with fixed maturities and fixed or determinable payments that Management has both the positive intent and the ability to hold to maturity are classified as held-to-maturity; and
- Securities that are not classified by the Bank as held-to-maturity or trading are included in the available-for-sale portfolio.

The Bank classifies investment securities depending upon the intent of management at the time of the purchase. Shares of associates and subsidiaries held by the Bank exclusively with a view to their future disposal are also classified as available-for-sale. Investment securities are initially recognized in accordance with the policy stated above and subsequently re-measured using the following policies:

1. Held-to-maturity investment securities – at amortized cost using the effective yield method. Allowance for impairment is estimated on a case-by-case basis.

2. Available-for-sale securities are subsequently measured at fair value, which is equal to the market value as at the balance sheet date. When debt securities with fixed maturities are non-marketable or no information is available on market of similar instruments, fair value has been estimated as the discounted future cash flows using current interest rates. Non-marketable securities that do not have fixed maturities are stated at cost, less allowance for diminution in value unless there are other appropriate and workable methods of reasonably estimating their fair value.

Gains and losses arising from changes in the fair value of available-for-sale securities are recognized in shareholders' equity in the period that the change occurs. When the securities are disposed of or impaired, the related accumulated fair value adjustment is included in the statement of income as gains less losses from investment securities.

e) Loans to customers

Loans granted by the Bank by providing funds directly to the borrower are categorized as loans originated by the Bank and are initially recognized in accordance with the policy stated above. The difference between nominal amount of consideration given and the fair value of loans issued at other than market terms is recognized in the period the loan is issued as initial recognition of loans to customers at fair value. Loans to customers with fixed maturities are subsequently measured at amortized cost using the effective interest rate method. Those that do not have fixed maturities are carried at cost. Loans and advances to customers are carried net of any allowance for impairment.

Loans are placed on non-accrual status when full payment of principal or interest is in doubt (a loan with principal and interest unpaid for at least ninety days). When a loan is placed on non-accrual status, contractual interest income is not recognized in the financial statements. A non-accrual loan may be restored to accrual status when principal and interest amounts contractually due are reasonably assured of repayment within a reasonable period.

f) Operating leases

Leases of assets under which the risks and rewards of ownership are effectively retained with the lessor are classified as operating leases. The Bank is the lessee. Lease payments under operating leases are recognized as expenses on a straight-line basis over the lease term and included into administrative and operating expenses.

g) Taxation

The current income tax charge is calculated in accordance with the regulations of Georgia and of the cities in which the Bank has offices and branches and its subsidiaries are located. Deferred income taxes are calculated using the liability method. Deferred taxes reflect the effects of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for income tax purposes. Deferred tax assets are recognized when it is probable that sufficient taxable profits will be available against which the deferred tax assets can be utilised.

Georgia also has various operating taxes, which are assessed on the Bank activities. These taxes are included as a component of administrative and operating expenses in the statement of income.

h) Investments in associates

Investments in associates are accounted for using the equity method. Equity accounting is discontinued when the carrying amount of the investment in an associated undertaking reaches zero, unless the Bank has incurred obligations or guaranteed obligations in respect of the associated undertaking.

Investments in non-consolidated subsidiaries are carried at cost less any allowance for diminution in value. The Bank has not consolidated these subsidiaries, as the financial effect is immaterial to the Bank as a whole.

i) Allowance for impairment of financial assets

The Bank establishes allowances for impairment of financial assets when it is probable that the Bank will not be able to collect the principal and interest according to the contractual terms of loans issued, held-to-maturity securities and other financial assets, which are carried at cost and amortized cost. The allowance for impairment of financial assets is defined as the difference between carrying amounts and the present value of expected future cash flows, including amounts recoverable from guarantees and collateral, discounted at the original effective interest rate of the financial instrument. For instruments that do not have fixed maturities, expected future cash flows are discounted using periods during which the Bank expects to realize the financial instrument.

The allowance is based on the Bank’s own loss experience and management’s judgment as to the level of losses that will most likely be recognized from assets in each credit risk category by reference to the debt service capability and repayment history of the borrower. The allowances for impairment of financial assets in the accompanying financial statements have been determined on the basis of existing economic and political conditions. The Bank is not in a position to predict what changes in conditions will take place in Georgia and what effect such changes might have on the adequacy of the allowances for impairment of financial assets in future periods.

Changes in allowances are reported in the statement of income of the related period. When an asset is not collectable, it is written off against the related allowance for impairment; if the amount of the impairment subsequently decreases due to an event occurring after the write-down, the reversal of the allowance is credited to the related impairment of financial assets in the statement of income.

j) Property and equipment

Property and equipment are carried at historical or revalued cost less accumulated depreciation and any accumulated impairment for diminution in value. Depreciation on assets under construction and those not placed in service commences from the date the assets are ready for their intended use. Depreciation is calculated on a straight-line basis over the following estimated useful lives:

	Years
Buildings	30
Furniture and equipment	5-8
Vehicles	4-5
Computers and communication equipment	3-5
Leasehold improvements	Contractual maturity, less than or equal to 10 years
Other	2-8

Leasehold improvements are amortized over the life of the related leased asset. The carrying amounts of property and equipment are reviewed at each balance sheet date to assess whether they are recorded in excess of their recoverable amounts, and where carrying values exceed this estimated recoverable amount, assets are written down to their recoverable amount. An allowance for impairment is recognized in the respective period, and the related charge is included in other administrative and operating expenses.

Expenses related to repairs and renewals are charged to the statement of income when incurred and included in other administrative and operating expenses, unless they qualify for capitalization.

k) Intangible assets

Intangible assets are recorded at historical cost less accumulated amortization. Amortization is provided to write off the cost on a straight-line basis over the estimated useful economic life of the asset. The economic lives range from one to 10 years. Intangible assets under development are not depreciated. Amortization of these assets will begin when the related assets are placed in service.

l) Provisions

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

m) Retirement and other benefit obligations

The Bank does not have pension arrangements on its own, separate from the State pension system of Georgia. Georgian system requires current contributions by the employer calculated as a percentage of current gross salary payments; such expense is charged to the statement of income in the period the related compensation is earned by the employee.

n) Share capital

Share capital is recognized at cost. Share capital contributions made in the form of assets other than cash are stated at their fair value at the date of contribution. Treasury stock is recorded at cost. Gains and losses on sales of treasury stock are charged or credited to additional paid-in capital.

(Thousands of Georgian Lari)

External costs directly attributable to the issue of new shares, other than on a business combination, are deducted from equity net of any related income taxes. Dividends on ordinary shares are recognized in shareholders' equity as a reduction in the period in which they are declared. Dividends that are declared after the balance sheet date are treated as a subsequent event under IAS 10 "Events After the Balance Sheet Date" and disclosed accordingly.

o) Contingencies

Contingent liabilities are not recognized in the financial statements unless it is probable that an outflow of resources will be required to settle the obligation and a reliable estimate can be made. A contingent asset is not recognized in the financial statements but disclosed when an inflow of economic benefits is probable.

p) Income and expense recognition

Interest income and expense are recognized on an accrual basis calculated using the effective interest rate method. Interest income includes coupon income earned on investment and trading securities. Commissions and other income are credited to income when the related transactions are completed. Loan origination fees for loans issued to customers, when significant, are deferred (together with related direct costs) and recognized as an adjustment to the loans' effective yield. Non-interest expenses are recognized at the time the transaction occurs.

q) Foreign currency translation

Foreign currency transactions are accounted for at the exchange rates prevailing at the date of transaction. Monetary assets and liabilities denominated in foreign currencies are translated into Georgian Lari at official NBG exchange rates at the balance sheet date. Gains and losses resulting from the translation of foreign currency transactions are recognized in the statement of income as gains less losses from foreign currencies. Differences between the contractual exchange rate of a certain transaction and the NBG exchange rate on the date of the transaction are included in gains less losses from foreign currencies. The official NBG exchange rates at December 31, 2002 and 2001, were 2.09 and 2.06 Georgian Lari to the US Dollar, respectively.

r) Reclassifications

The following reclassifications have been made to 2001 balances to conform to the 2002 presentation:

Amount	**As originally reported in 2001**	**As reclassified**	**Explanation**
7,892	Consumer loans	Pawn loans	Correct misclassification
3,626	Other loans	Pawn loans	Correct misclassification
86	Other operating income	Dividend income	Additional detailed classification

NOTE 5 – CASH AND DUE FROM NATIONAL BANK

Cash and due from National Bank comprise:

	2002	**2001**
Cash on hand	13,562	5,649
Current accounts	3,665	1,345
Obligatory reserves	19,131	10,871
Cash and due from National Bank	**36,358**	**17,865**

NBG requires credit institutions to maintain cash deposits (reserves), the amount of which depends on the level of deposits attracted by the credit institution. The Bank's ability to withdraw such deposits is not restricted by statutory legislation.

Reserves calculated on the basis of NBG requirements as of December 31, 2002, comprised 18,885 GEL. Reserves maintained by the Bank as of December 31, 2002, exceeded required level by 246 GEL.

(Thousands of Georgian Lari)

NOTE 6 – AMOUNTS DUE FROM CREDIT INSTITUTIONS

Amounts due from credit institutions comprise:

	2002	2001
Current accounts	28,867	15,526
Time deposits	4,535	-
	33,402	**15,526**
Less – Allowance for impairment	(224)	(82)
Amounts due from credit institutions, net	**33,178**	**15,444**

The Bank estimates allowance for impairment on the placements with banks in non-OECD countries as 2% of the balances of such placements as of December 31, 2002. Current accounts include 1,658 GEL, which are blocked under Letters of Credit and Guarantees (2001 – 294 GEL). As of December 31, 2002 estimated fair value of amounts due from credit institutions comprise 33,222 GEL (2001 – 15,526 GEL).

NOTE 7 – INVESTMENT SECURITIES

Investment securities – held-to-maturity comprise:

	2002	2001
Treasury bills, nominal value	3,846	-
Discount on Treasury bills	(203)	-
Held-to-maturity securities	**3,643**	**-**

Treasury bills of the Ministry of Finance have stated interest at rates ranging from 42% to 85% and mature in 90 to 182 days.

Investment securities – available-for-sale comprise of:

	2002	2001
Investments in subsidiaries and associates	20	2,520
Other equity investments	2,922	4,615
	2,942	**7,135**
Less – Allowance for diminution in value	-	(750)
Available-for-sale securities, net	**2,942**	**6,385**

As of December 31, 2002, the Bank has investments in the following subsidiaries, associates and other available-for-sale investments.

Name	**Bank holding %**	**Total shareholders' funds of investee**	**Carrying value of investment**	**Principal activity**	**Country**
TBC Broker LLC	100%	20	20	Corporate finance	Georgia
JSC Bank of Georgia	11%	44,926	2,801	Banking	Georgia
Others	-	-	121	-	Georgia
			2,942		

The Bank has not consolidated its investment in TBC Broker LLC, as the financial effect is immaterial to the Bank as a whole. The investment in TBC Broker LLC is stated at cost.

(Thousands of Georgian Lari)

The Bank's investment in JSC Bank of Georgia is carried at cost, as these shares do not have a quoted market price and other methods of reasonably estimating fair value are not workable due to the absence of comparable quoted companies and the lack of reliable information for use in any valuation analysis. In management's opinion, the carrying value of the shares is realizable and approximates its fair value.

As of December 31, 2001, the Bank had investment in JSC Centraluri Univermagi (a former Central Department Store of the city of Tbilisi) in the amount of 1,750 GEL (gross value – 2,500 GEL and reserve for impairment – 750 GEL). The Bank's holding was 93%. However, the investment had not been consolidated with the results of the Bank as the control was intended to be temporary as the subsidiary was acquired with a view to its subsequent disposal. During 2002, the Bank increased its investment in JSC Centraluri Univermagi by 116 GEL that resulted in increase of its holding to 95%. Later on in 2002, taking advantage of the dominating voting rights, the Bank dissolved the subsidiary and obtained its property and equipment that entirely consisted of the Central Department Store building. Upon acquisition of the building, the Bank reclassified its investment and recognized the building as asset under construction at its appraisal value of 2,404 GEL using the report of an independent appraiser (see Note 12). The Bank wrote off 212 GEL and recovered 538 GEL of allowance for impairment.

As of December 31, 2001, the Bank had an equity investment in JSC Microfinance Bank of Georgia ("MBG") totaling 1,693 GEL. During 2002, the Bank disposed in full its share in MBG for 2,610 GEL. The net gain of 917 GEL has been recognized as dealing profits in the statement of income.

NOTE 8 – LOANS TO CUSTOMERS

Loans to customers are made principally within Georgia and comprise:

	2002	2001
Trading enterprises	32,939	24,129
Pawn loans	16,515	11,518
Manufacturing	14,767	14,346
Consumer	12,472	4,644
Services	10,086	7,802
Energy	4,930	3,573
Communications and transportation	4,835	6,557
Heavy industry	2,772	296
Real estate and construction	2,446	1,175
Other	5,404	2,722
	107,166	**76,762**
Less – Allowance for impairment	(6,000)	(4,259)
Loans to customers, net	**101,166**	**72,503**

As of December 31, 2002, the estimated fair value of loans to customers was 105,830 GEL (2001 – 72,701 GEL).

The Bank accepted quoted and unquoted securities and other property as collateral for commercial loans, which the Bank is not permitted to sell or re-pledge in the absence of default. The Bank's loan portfolio has been extended to the following types of enterprises:

	2002	2001
Private companies	87,506	64,226
Individuals	19,660	12,536
Loans to customers	**107,166**	**76,762**

(Thousands of Georgian Lari)

NOTE 9 – TAXATION

The corporate income tax expense comprises:

	2002	2001
Current tax charge	2,339	1,559
Deferred taxation	(33)	201
Income tax expense	**2,306**	**1,760**

Georgian legal entities must individually report taxable income and remit profit taxes thereon to the appropriate authorities. The tax rate for the Bank for profits was 20% in 2002 and 2001.

Tax assets and liabilities consist of the following:

	2002	2001
Deferred tax assets	33	-
Tax assets	**33**	**-**
Current tax liabilities	788	413
Tax liabilities	**788**	**413**

The effective income tax rate differs from the statutory income tax rates. A reconciliation of the income tax expense based on statutory rates with actual is as follows:

	2002	2001
IFRS income before tax	**12,810**	**6,258**
Statutory tax rate	20%	20%
Theoretical income tax expense at the statutory rate	**2,562**	**1,252**
Tax exempt income	(343)	(8)
Impairment charge (reversal) for assets	(196)	184
Change in unrecognized deferred tax asset	144	(195)
Non tax deductible expenditures:		
- Charity	63	277
- Staff bonuses	21	115
Losses from affiliated undertakings	55	41
Effect of change in taxation rate	-	53
Withholding and other tax provisions	-	41
Income tax expense	**2,306**	**1,760**

(Thousands of Georgian Lari)

Deferred tax assets comprise:

	2002	2001
Tax effect of deductible temporary differences		
Available-for-sale securities	523	-
Provisions	144	-
Intangible assets	2	
Accrued liabilities	-	12
Gross deferred tax asset	**669**	**12**
Unrecognized deferred tax asset	(144)	-
Deferred tax asset	**525**	**12**
Tax effect of taxable temporary differences		
Property and equipment	492	-
Deferred tax liability	**492**	**12**
Net deferred tax asset	**33**	**-**

Georgia currently has a number of laws related to various taxes imposed by state governmental authorities. Applicable taxes include value added tax, corporate income tax (profits tax), one turnover based tax, and payroll (social) taxes, together with others. Laws related to these taxes have not been in force for significant periods, in contrast to more developed market economies. Therefore, implementing regulations are often unclear or nonexistent and few precedents have been established. It creates tax risks in Georgia substantially more significant than typically found in countries with more developed tax systems.

Management believes that the Bank is in substantial compliance with the tax laws affecting its operations. The local tax inspectorate has reviewed the Bank's 2002 operations and has not found any violations of the tax code or any other applicable laws. However, the risk remains that relevant authorities could take differing positions with regard to interpretive issues.

NOTE 10 – INVESTMENTS IN ASSOCIATES

Investments in associated companies are:

	2002	2001
Balance beginning of the period	401	144
Purchase cost	614	471
Share of net loss	(275)	(207)
Write-off	-	(7)
	740	**401**
Less – Allowance for diminution in value	(65)	(65)
Investments in associates, net	**675**	**336**

Investments in associates represent investments in the following entities:

Name	Bank holding %	Cost	Principal activity	Country
JSC United Financial Corporation	42%	353	Plastic cards processing	Georgia
JSC Georgian Pensions and Insurance Holding	20%	250	Pensions and insurance	Georgia
UFC International Limited	40%	137	Plastic card processing	Virgin Islands
		740		

(Thousands of Georgian Lari)

NOTE 11 – ALLOWANCES FOR LOSSES

The movements in allowances for impairment on interest earning assets during 2002, were as follows:

	Amounts due from credit institutions	Loans to customers	Total allowances
December 31, 2001	**82**	**4,259**	**4,341**
Charges	142	2,140	2,282
Recoveries	-	1,413	1,413
Write-offs	-	(1,812)	(1,812)
December 31, 2002	**224**	**6,000**	**6,224**

The movements in allowances for other losses during 2002, were as follows:

	Investments in associates	Investment securities	Other assets	Other risks	Total reserves
December 31, 2001	**65**	**750**	**216**	**259**	**1,290**
Provisions charged (reversal)	-	(538)	-	266	(272)
Write-offs	-	(212)	(25)	-	(237)
December 31, 2002	**65**	**-**	**191**	**525**	**781**

The movements in allowances for impairment on interest earning assets during 2001, were as follows:

	Amounts due from credit institutions	Loans to customers	Total allowances
December 31, 2000	**35**	**3,852**	**3,887**
Charges	47	3,597	3,644
Recoveries	-	1,425	1,425
Write-offs	-	(4,615)	(4,615)
December 31, 2001	**82**	**4,259**	**4,341**

The movements in allowances for other losses during 2001, were as follows:

	Investments in associates	Investment securities	Other assets	Other risks	Total reserves
December 31, 2000	**48**	**-**	**32**	**55**	**135**
Provisions charged	24	750	186	204	1,164
Write off of assets	(7)	-	(2)	-	(9)
December 31, 2001	**65**	**750**	**216**	**259**	**1,290**

Allowances for impairment of assets are deducted from the related asset. Provisions for claims, guarantees and commitments are recorded in liabilities. In accordance with the Georgian legislation, loans must be immediately written off if overdue more than 150 days.

(Thousands of Georgian Lari)

NOTE 12 – PROPERTY AND EQUIPMENT

The movements of property and equipment were as follows:

	Land and buildings	Furniture, fixtures and equipment	Assets under construction	Total
Cost				
December 31, 2001	**2,972**	**2,375**	**678**	**6,025**
Additions	121	1,437	3,123	4,681
Disposals	-	(54)	(35)	(89)
Transfers	749	283	(1,032)	-
December 31, 2002	**3,842**	**4,041**	**2,734**	**10,617**
Accumulated depreciation				
December 31, 2001	**543**	**949**	**-**	**1,492**
Charge	159	592	-	751
Disposals	-	(34)	-	(34)
December 31, 2002	**702**	**1,507**	**-**	**2,209**
Net book value				
December 31, 2001	2,429	1,426	678	4,533
December 31, 2002	**3,140**	**2,534**	**2,734**	**8,408**

As discussed in Note 7, during 2002, the Bank dissolved its subsidiary and acquired its property and equipment that consisted of the Central Department Store building. Upon acquisition of the building, the Bank reclassified its investment and recognized the building as an asset under construction at its appraised value of 2,404 GEL using the report of an independent appraiser.

NOTE 13 – INTANGIBLE ASSETS

The movements of intangible assets were as follows:

	Intangible assets
Cost	
December 31, 2001	**510**
Additions	197
December 31, 2002	**707**
Amortization	
December 31, 2001	**179**
Charge	184
December 31, 2002	**363**
Net book value	
December 31, 2001	331
December 31, 2002	**344**

(Thousands of Georgian Lari)

NOTE 14 – OTHER ASSETS AND LIABILTIIES

Other assets comprise:

	2002	2001
Prepaid operating taxes	509	353
Prepayments	406	276
Trade debtors	266	247
Real estate and assets	149	532
Other	182	231
	1,512	**1,639**
Less – Allowance for impairment	(191)	(216)
Other assets	**1,321**	**1,423**

Other liabilities comprise:

	2002	2001
Accrued expenses	1,618	855
Operating taxes payable	336	125
Sundry creditors	116	207
Other	195	72
Other liabilities	**2,265**	**1,259**

Accrued expenses include 1,347 GEL employee bonuses for 2002 (2001 – 647 GEL). Bonuses payable to members of the Board of Directors comprise 1,218 GEL.

NOTE 15 – AMOUNTS OWED TO CREDIT INSTITUTIONS

Amounts owed to credit institutions comprise:

	2002	2001
Borrowings from international credit institutions	17,267	15,221
Time deposits from other banks	956	10,237
Current accounts	2,397	491
Amounts owed to credit institutions	**20,620**	**25,949**

As of December 31, 2002, the estimated fair value of amounts owned to credit institutions was 21,628 GEL (2001 – 32,736 GEL). As of December 31, 2002 loans from other banks included 17,058 GEL (2001 – 15,221 GEL) of borrowings from Deutsche Investitions und Entwicklungsgesellschaft MBH, International Financial Corporation and European Bank for Reconstruction and Development.

NOTE 16 – AMOUNTS OWED TO CUSTOMERS

Amounts owed to customers comprise:

	2002	2001
Current accounts	53,143	25,572
Time deposits and saving accounts	80,381	44,526
Amounts owed to customers	**133,524**	**70,098**

Amounts owed to customers include 9,067 GEL of deposits blocked under Letters of Credit and Guarantees (2001 – 570 GEL).

(Thousands of Georgian Lari)

As of December 31, 2002, the estimated fair value of amounts owed to customers was 133,528 GEL (2001 – 69,575 GEL).

NOTE 17 – SHAREHOLDERS' EQUITY

The share capital of the Bank has been contributed by shareholders in both Georgian Lari and US dollars. Shareholders are entitled to dividends and capital distributions in Georgian Lari. As of December 31, 2002 and 2001, the charter fund comprised 50,000 common shares – authorized, issued and outstanding, with par value of 100 GEL per share.

During 2002, the Bank declared and paid dividends totaling 1,000 GEL.

NOTE 18 – FINANCIAL COMMITMENTS AND CONTINGENCIES

a) Credit related financial commitments

The credit related financial commitments as of December 31, 2002 and 2001 comprise:

	2002	**2001**
Guarantees	10,746	2,850
Letters of credit	4,375	570
Undrawn loan commitments	2,215	2,159
	17,336	**5,579**

In the normal course of business, the Bank makes commitments to grant loans at a specified rate of interest during a fixed period of time. The Bank's Management evaluated the likelihood of possible losses arising from credit related commitments and concluded that a provision of 424 GEL was necessary as of December 31, 2002 (2001 – 259 GEL).

b) Operating lease obligations

In the normal course of business, the Bank enters into operating lease agreements. Future minimum payments under non-cancelable operating leases are as follows:

	2002	**2001**
Not later than one year	251	167
Later than 1 year and not later than 5 years	477	495
Later than 5 years	166	393
	894	**1,055**

c) Legal

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

(Thousands of Georgian Lari)

NOTE 19 – SALARIES AND ADMINISTRATIVE EXPENSES

Salaries and administrative expenses comprise:

	2002	2001
Salaries and other benefits	4,956	3,141
Social security costs	1,475	985
Salaries	**6,431**	**4,126**
Occupancy	1,282	723
Business development	871	698
Communication and supplies	709	818
Professional services	644	545
Operating taxes	515	372
Other	294	297
Administrative expenses	**4,315**	**3,453**

The Bank does not have its own pension arrangements. However, Georgian Pension and Insurance Holding ("GPIH") – a local commercial pension fund, serves employees of the Bank at standard terms. The Bank serves as an agent. At the employees' standard contractual request, it deducts predefined portion of each employee's salary - based on the standard pension agreement between the employee and GPIH - and transfers the amounts to GPIH.

NOTE 20 – SUPPLEMENTARY CASH FLOW INFORMATION

Cash and cash equivalents as shown in the cash flow statements comprise:

	2002	2001
Cash and current account with National Bank	17,227	6,994
Amounts due from credit institutions:		
– Current accounts	27,450	15,232
– Time deposits and interbank loans with maturity less than three months	2,677	-
Cash and cash equivalents	**47,354**	**22,226**

During 2002, the Bank acquired 2,404 GEL of property and equipment through a non-cash transaction whereby it gained control of an investment previously classified as available-for-sale securities.

NOTE 21 – RISK MANAGEMENT POLICIES

Management of risk is fundamental to the banking business and is an essential element of the Bank's operations. The main risks inherent to the Bank's operations are those related to credit exposures, liquidity and market movements in interest rates and foreign exchange rates. A description of the Bank's risk management policies in relation to those risks follows.

Credit risk
The Bank is exposed to credit risk which is the risk that a counter party will be unable to pay amounts in full when due. The Bank structures the levels of credit risk it undertakes by placing limits on the amount of risk accepted in relation to one borrower, or groups of borrowers, and to industry and geographical segments. Such risks are monitored on a revolving basis and subject to an annual or more frequent review.

(Thousands of Georgian Lari)

Exposure to credit risk is managed through regular analysis of the ability of borrowers and potential borrowers to meet interest and capital repayment obligations and by changing these lending limits where appropriate. Exposure to credit risk is also managed in part by obtaining collateral and corporate and personal guarantees.

Credit-related commitments ensure that funds are available to a customer as required. Guarantees and standby letters of credit, which represent irrevocable assurances that the Bank will make payments in the event that a customer cannot meet its obligations to third parties, carry the same credit risk as loans. Documentary and commercial letters of credit, which are written undertakings by the Bank on behalf of a customer authorizing a third party to draw drafts on the Bank up to a stipulated amount under specific terms and conditions, are frequently fully or partially covered by the funds deposited by customers and therefore bear no credit risk.

With respect to undrawn loan commitments the Bank is potentially exposed to the credit risk equal to the total amount of such commitments.

The geographical concentration of monetary assets and liabilities follows.

	2002				**2001**			
	Georgia	**OECD**	**Other non -OECD**	**Total**	**Georgia**	**OECD**	**Other non -OECD**	**Total**
Assets								
Cash and due from National Bank	36,358	-	-	36,358	17,865	-	-	17,865
Due from credit institutions, net	4,782	27,907	489	33,178	1,412	10,965	3,067	15,444
Loans to customers, net	101,166	-	-	101,166	72,503	-	-	72,503
Investment securities, net	6,585	-	-	6,585	6,385	-	-	6,385
	148,891	**27,907**	**489**	**177,287**	**98,165**	**10,965**	**3,067**	**112,197**
Liabilities								
Amounts owed to credit institutions	1,385	19,228	7	20,620	1,788	24,151	10	25,949
Amounts owed to customers	133,524	-	-	133,524	64,178	-	5,920	70,098
	134,909	**19,228**	**7**	**154,144**	**65,966**	**24,151**	**5,930**	**96,047**
Net position	**13,982**	**8,679**	**482**	**23,143**	**32,199**	**(13,186)**	**(2,863)**	**16,150**

(Thousands of Georgian Lari)

Currency risk

The Bank is exposed to effects of fluctuation in the prevailing foreign currency exchange rates on its financial position and cash flows. The Board of Directors sets limits on the level of exposure by currencies (primarily US Dollar), by branches and in total. These limits also comply with the minimum requirements of NBG. The Bank's exposure to foreign currency exchange rate risk follows.

	2002			2001		
	Georgian Lari	**Foreign currencies**	**Total**	**Georgian Lari**	**Foreign currencies**	**Total**
Assets						
Cash and due from National Bank	30,069	6,289	36,358	14,500	3,365	17,865
Due from credit institutions, net	194	32,984	33,178	144	15,300	15,444
Loans to customers, net	646	100,520	101,166	233	72,270	72,503
Investment securities, net	6,585	-	6,585	6,385	-	6,385
All other assets	10,491	290	10,781	6,605	18	6,623
	47,985	**140,083**	**188,068**	**27,867**	**90,953**	**118,820**
Liabilities						
Amounts owed to credit institutions	93	20,527	20,620	325	25,624	25,949
Amounts owed to customers	14,772	118,752	133,524	7,017	63,081	70,098
All other liabilities	3,023	555	3,578	1,597	334	1,931
	17,888	**139,834**	**157,722**	**8,939**	**89,039**	**97,978**
Net balance sheet position	**30,097**	**249**	**30,346**	**18,928**	**1,914**	**20,842**

The Bank has extended loans and advances denominated in foreign currencies. Although these loans are generally funded by the same currencies, their appreciation against Georgian Lari can adversely affect the borrowers' repayment ability and therefore increases the likelihood of future loan losses.

Liquidity risk

The Bank is exposed to daily calls on its available cash resources from, current deposits, maturing deposits, loan draws, and guarantees. The Bank maintains liquidity management with the objective of ensuring that funds will be available at all times to honor cash flow obligations as they become due. The Bank's Assets and Liabilities Management Committee sets limits on the minimum proportion of maturing funds available to cover such cash outflows and on the minimum level of interbank and other borrowing facilities that should be in place to cover withdrawals at unexpected levels of demand.

(Thousands of Georgian Lari)

The actual maturities of monetary assets and liabilities as of December 31 follow.

2002

	On demand	Less than 1 month	1 to 3 months	3 months to 1 year	1 to 5 years	Over 5 years	Overdue	Total
Assets								
Cash and due from National Bank	17,227	19,131	-	-	-	-	-	36,358
Due from credit institutions, net	27,266	501	2,158	2,285	768	200	-	33,178
Loans to customers, net	-	23,469	18,667	35,831	22,477	139	583	101,166
Investment securities, net								
- available-for-sale	-	-	-	-	-	2,942	-	2,942
- held-to-maturity	-	2,420	1,223	-	-	-	-	3,643
	44,493	**45,521**	**22,048**	**38,116**	**23,245**	**3,281**	**583**	**177,287**
Liabilities								
Amounts owed to credit institutions	-	2,832	1,052	9,858	6,878	-	-	20,620
Amounts owed to customers	78,107	5,686	15,843	26,223	7,624	41	-	133,524
	78,107	**8,518**	**16,895**	**36,081**	**14,502**	**41**	**-**	**154,144**
Net position	**(33,614)**	**37,003**	**5,153**	**2,035**	**8,743**	**3,240**	**583**	**23,143**
Accumulated gap	***(33,614)***	***3,389***	***8,542***	***10,577***	***19,320***	***22,560***	***23,143***	

2001

	On demand	Less than 1 month	1 to 3 months	3 months to 1 year	1 to 5 years	Over 5 years	Overdue	Total
Assets								
Cash and due from National Bank	6,994	10,871	-	-	-	-	-	17,865
Due from credit institutions, net	15,192	24	228	-	-	-	-	15,444
Loans to customers, net	-	24,969	8,418	24,121	14,623	14	358	72,503
Investment securities, net								
- available-for-sale	-	-	-	-	-	6,385	-	6,385
	22,186	**35,864**	**8,646**	**24,121**	**14,623**	**6,399**	**358**	**112,197**
Liabilities								
Amounts owed to credit institutions	490	10,936	733	4,192	9,130	468	-	25,949
Amounts owed to customers	44,336	4,767	8,039	11,874	1,071	11	-	70,098
	44,826	**15,703**	**8,772**	**16,066**	**10,201**	**479**	**-**	**96,047**
Net position	**(22,640)**	**20,161**	**(126)**	**8,055**	**4,422**	**5,920**	**358**	**16,150**
Accumulated gap	***(22,640)***	***(2,479)***	***(2,605)***	***5,450***	***9,872***	***15,792***	***16,150***	

Interest rate risk

The Bank is exposed to the effects of fluctuations in the prevailing levels of market interest rates on its financial position and cash flows. Interest rate risk is measured by the extent to which changes in market interest rates impact margins and net income. To the extent the term structure of interest bearing assets differs from that of liabilities, net interest income will increase or decrease as a result of movements in interest rates. The Bank's expected repricing and maturity dates do not differ significantly from the contract dates, which are summarized in the liquidity risk table above.

Interest rate risk is managed by increasing or decreasing positions within limits specified by the Bank's management. These limits restrict the potential effect of movements in interest rates on interest margin and on the value of interest-sensitive assets and liabilities.

(Thousands of Georgian Lari)

The Bank's interest rate policy is reviewed and approved by the Bank's Assets and Liabilities Management Committee. The Bank's average effective interest rates as of December 31, 2002 and 2001 for monetary financial instruments follow.

	2002			**2001**		
	Georgian Lari	**US Dollars**	**Other foreign currencies**	**Georgian**	**US Dollars**	**Other foreign currencies**
Interest earning assets						
Amounts due from credit institutions	-	5.6%	-	4.5%	3.1%	4.1%
Loans to customers	18.3%	24.9%	17.8%	30.2%	23.1%	-
Investment securities:						
- available-for-sale	6.8%	-	-	-	-	-
- held-to-maturity	35.9%	-	-	-	-	-
Interest bearing liabilities						
Amounts owed to credit institutions	6.0%	6.8%	9.0%	-	8.0%	8.3%
Amounts owed to customers	12.0%	11.1%	7.0%	7.7%	9.1%	7.8%

NOTE 22 – RELATED PARTIES

Related parties, as defined by IAS 24, are those counter parties that represent:

(a) enterprises that directly, or indirectly through one or more intermediaries, control, or are controlled by, or are under common control with, the reporting enterprise. (This includes holding companies, subsidiaries and fellow subsidiaries);

(b) associates – enterprises in which the Bank has significant influence and which is neither a subsidiary nor a joint venture of the investor;

(c) individuals owning, directly or indirectly, an interest in the voting power of the Bank that gives them significant influence over the Bank, and anyone expected to influence, or be influenced by, that person in their dealings with the Bank;

(d) key management personnel, that is, those persons having authority and responsibility for planning, directing and controlling the activities of the Bank, including directors and officers of the Bank and close members of the families of such individuals; and

(e) enterprises in which a substantial interest in the voting power is owned, directly or indirectly, by any person described in (c) or (d) or over which such a person is able to exercise significant influence. This includes enterprises owned by directors or major shareholders of the Bank and enterprises that have a member of key management in common with the Bank.

In considering each possible related party relationship, attention is directed to the substance of the relationship, and not merely the legal form. As of December 31, 2002, the Bank had 6,849 GEL (2001 – 1,767 GEL) of transactions outstanding with related parties.

(Thousands of Georgian Lari)

These transactions comprise:

	2002			2001
	Related party transactions	**Percentage on normal conditions**	**Total asset, liability or expense category, gross**	**Related party transactions**
Loans to customers, gross	2,490	100%	107,166	1,129
Amounts owed to customers	2,902	100%	133,524	122
Provisions for other risks	181	-	525	181
Professional services expenses	253	-	644	392
Commitments and guarantees given	1,023	100%	10,746	124

Loans to customers consist of 1,895 GEL loans to private enterprises and 595 GEL to individuals.

The percentages indicated above represent the percentages of related parties transactions that have been entered into under normal commercial and banking terms and conditions.

As of December 31, 2002, members of the Supervisory Board owned 32,920 shares – 65.84% (30,420 shares – 60.84% in 2001) of the Bank. Also, as of December 31, 2002, members of the Supervisory Board and Management Boards had 404 GEL (2001 – 283 GEL) of loans due to the Bank.

NOTE 23 – CAPITAL ADEQUACY

The National Bank of Georgia requires banks to maintain a capital adequacy ratio of 8% (12% for 2001) of risk weighted assets. As of December 31, 2002 and 2001, the Bank's capital adequacy ratio on this basis exceeded the statutory minimum.

The Bank's international risk based capital adequacy ratio as of December 31, 2002 and 2001 was 22%, which exceed the minimum ratio of 8% recommended by the Basle Accord.

(end)