TBC BANK

AUDIT REPORT AND FINANCIAL STATEMENTS PREPARED UNDER INTERNATIONAL ACCOUNTING STANDARDS FOR THE YEAR ENDED 31 DECEMBER 1999

**Annual report
for the year ended 31 December 1999**

Independent auditors' report

To the Shareholders of TBC Bank

1. We have audited the accompanying balance sheet of TBC Bank as of 31 December 1999 and the related income statement, statement of changes in shareholders' equity and cash flow statement for the year then ended. These financial statements set out on pages 4 to 22 are the responsibility of the Bank's management. Our responsibility is to express an opinion on these financial statements based on our audit.

2. 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.

3. In our opinion the financial statements present fairly, in all material respects, the financial position of the Bank as at 31 December 1999, and of the results of its operations and changes in its cash flows for the year then ended, in accordance with International Accounting Standards.

PricewaterhouseCoopers
Coopers & Lybrand Audit
Paris, France
March 20, 2000

Rainer Stawinoga
Partner

Income statement

(all amounts expressed in thousands of Georgian Lari)	Notes	Year ended 31 December	
		1999	1998
Interest income	2	8 365	6 195
Interest expense	2	(2 425)	(1 657)
Net interest income		**5 940**	**4 538**
Fee and commission income, net	3	1 138	1 867
Other operating income	4	1 893	1 052
Operating income		**8 971**	**7 457**
Operating expenses	5	(4 104)	(2 402)
Increase in provisions for bad debts	6	(1 379)	(2 309)
Profit before tax		**3 488**	**2 746**
Income tax expense	7	(361)	(262)
Retained profit for the period		3 127	2 484

The following notes on pages 8 to 22 form an integral part of these financial statements and should be read in conjunction therewith.

Balance sheet

(all amounts expressed in thousands of Georgian Lari)	**Notes**	**As at 31 December**	
		1999	1998
ASSETS			
Cash and balances with the central bank	8	8 327	2 763
Due from other banks	9	13 626	9 567
Dealing securities		676	514
Loans and advances to customers	10	36 075	16 429
Investments securities	11	1 970	451
Property and equipment	12	3 094	3 004
Interest receivable and other assets	13	2 341	1 687
Total assets		**66 109**	**34 415**
LIABILITIES			
Due to other banks	14	23 392	7 888
Due to customers	15	30 809	17 476
Interest payable and other liabilities	16	1 345	1 613
Total liabilities		**55 546**	**26 977**
SHAREHOLDERS' EQUITY			
Ordinary shares	20	3 000	2 978
Reserves		7 563	4 460
Total shareholders' equity		**10 563**	**7 438**
Total equity and liabilities		**66 109**	**34 415**

The following notes on pages 8 to 22 form an integral part of these financial statements and should be read in conjunction therewith.

Statement of changes in shareholders' equity

(all amounts expressed in thousands of Georgian Lari)	Notes	Share capital	Share premium	Other reserves	Retained profits	Total equity
Balance at 1 January 1998						
– as previously reported		2 978	474	82	1 416	4 950
– effect of adopting IAS 12 revised	17	-	-	-	4	4
– as restated		2 978	474	82	1 420	4 954
Net profit – restated for the effect of IAS 12 revised.		-	-	-	2 484	2 484
Balance at 31 December 1998		**2 978**	**474**	**82**	**3 904**	**7 438**
Balance sheet at 1 January 1999						
– as previously reported		2 978	474	82	3 810	7 344
– effect of adopting IAS 12 revised		-	-	-	94	94
– as restated		2 978	474	82	3 904	7 438
– dividends paid		-	-		(24)	(24)
– share capital increase		22	-		-	22
Net profit		-	-		3 127	3 127
Balance at 31 December 1999		3 000	474	82	7 007	10 563

The following notes on pages 8 to 22 form an integral part of these financial statements and should be read in conjunction therewith.

Cash flow statement

(all amounts expressed in thousands of Georgian Lari)	Notes	Year ended 31 December	
		1999	1998
Cash flows from operating activities			
Profit for the year before tax		3 488	2 746
Increase in provisions for bad debts		1 379	1 588
Gains from dealing securities		(161)	-
Depreciation		297	165
Income taxes paid		(355)	(332)
Equity dividends paid		(24)	-
Cash flows from operating profits before changes in operating assets and liabilities		**4 624**	**4 167**
Changes in operating assets and liabilities:			
Net increase in mandatory reserve with the central bank		(2 546)	(136)
Net increase in loans and advances to banks		(440)	(293)
Net increase in loans and advances to customers		(20 158)	(7 927)
Net (increase)/decrease in government securities		(510)	440
Net increase in other assets		(791)	(87)
Net increase/(decrease) in deposits from other banks		11 351	(2 612)
Net increase in amounts due to customers		13 173	7 406
Net increase/(decrease) in other liabilities		(525)	486
Net cash flow from operating activities		**4 178**	**1 444**
Cash flows from investing activities			
Property and equipment, net		(724)	(926)
Purchases of equity investments		(993)	(681)
Net cash used in investing activities		**(1 717)**	**(1 607)**
Net cash flow from financing activities			
Net increase in borrowings from credit institutions		4 153	8 120
Net increase in equity		22	-
Net cash used in financing activities		**4 175**	**8 120**
Net increase in cash and cash equivalents		6,636	7 957
Cash and cash equivalents at beginning of year		**10 304**	**2 347**
Cash and cash equivalents at end of year	21	**16 940**	**10 304**

The following notes on pages 8 to 22 form an integral part of these financial statements and should be read in conjunction therewith.

1 Accounting policies

The principal accounting policies adopted in the preparation of these financial statements are set out below:

(1) Basis of presentation

The financial statements are prepared in accordance with and comply with International Accounting Standards ('IAS'), issued by the International Accounting Standards Committee. The accompanying financial statements are based on the statutory records of the Bank, which are maintained under the historical cost convention.

(2) Foreign currencies

Foreign currency transactions are accounted for at the exchange rates prevailing at the date of the transactions: gains and losses resulting from the settlement of such transactions and from the translation of monetary assets and liabilities denominated in foreign currencies, are recognised in the income statement. Such balances are translated at year-end exchange rates.

The exchange rate of the US dollar against the Georgian Lari evolved in 1999 as follows:

	GEL/USD
At 1 January 1999	1.80
Highest (at 23 February)	2.451
Lowest (at 4 January)	1.79
31 December 1999	1.93

(3) Interest income and expense

Interest income and expense are recognised in the income statement on an accruals basis. Interest income is suspended when loans are overdue by more than 60 days and is excluded from interest income until received.

(4) Deferred income taxes

Deferred income tax is provided, using the liability method, for all temporary differences arising between the tax bases of assets and liabilities and their carrying values for financial reporting purposes. Currently enacted tax rates are used to determine deferred income tax.

(5) Investment securities

Investment securities include equity securities and T-Bills of the government of Georgia which management intend to hold for capital growth purposes. Equity investments are stated at historical cost less any impairment. A reduction in carrying value is not taken into account unless it is considered to be permanent. Dividends received are included in other operating income.

(6) Dealing securities.

Dealing securities are stated at fair value based on estimated market prices.

(7) Loans and provisions for bad and doubtful debts

Loans are stated in the balance sheet at the amount of principal outstanding less any provision. Provisions for bad and doubtful debts are made, having regard to both general and specific risks. The specific element of the provisions relates to those loans that have been individually reviewed and specifically identified as bad or doubtful. The general element of the provisions relates to those existing losses which, although not yet specifically identified, are known from experience to be present at any year-end in the Bank's portfolio of loans and advances.

In determining the level of the provisions required management considers numerous factors including domestic economic conditions, the composition of the loan portfolio and prior bad debt experience. When a loan is deemed uncollectable, it is written off against the related provision for bad and doubtful debts.

(8) Property, plant and equipment

All property, plant and equipment are stated at historical cost less depreciation and correspondingly restated as explained below. Depreciation is calculated on the straight line method to write off the cost of each asset to their residual values over their estimated useful life as follows:

	1999
Buildings	30 years
Equipment	8 years
Furniture and fittings	5-8 years
Motor vehicles	4-5 years
Computers	3-5 years

Gains and losses on disposal of property and equipment are determined by reference to their carrying amount and are taken into account in determining operating profit. Repairs and renewals are charged to the income statement when the expenditure is incurred.

(9) Cash and cash equivalents

For the purposes of the cash flow statement, cash and cash equivalents comprise balances with less than 90 days maturity from the date of acquisition including: cash and balances with the Central Bank, and amounts due from other banks.

(10) Comparatives

Where necessary, comparative figures have been adjusted to conform with changes in presentation in the current year. In particular the comparatives have been adjusted to take into account the requirements of IAS 12 (revised) – Income Taxes.

(In the notes all amounts are shown in thousands of Georgian Lari unless otherwise stated)

2 Net interest income

	1999	1998
Interest and discount income		
Loans and advances to banks	973	435
Loans and advances to customers	7 392	5 760
	8 365	**6 195**
Interest expense		
Amounts due to banks	1 115	625
Amounts due to customers	1 310	1 032
	2 425	**1 657**

3 Net fees and commission income

	1999	1998
Fees and commission income	1 665	2 274
Fees and commission expense	(527)	(407)
	1 138	**1 867**

4 Other operating income

	1999	1998
Gains from dealing securities	161	-
Gains from dealing in foreign currency	1 704	964
Dividend income	28	-
Other	-	88
	1 893	**1 052**

5 Operating expenses

	1999	1998
Hired services	615	328
Staff costs, including:		
- Wages and salaries	1 380	745
- Social security costs	620	335
Advertising and marketing	182	183
Materials	498	175
Depreciation (Note 12)	297	165
Other	512	471
	4 104	**2 402**

The average number of persons employed by the Bank during the year was 134 (1998: 98)

6 Increase in provisions for bad debts

	1999	1998
Loans and advances to customers (Note 10)	2 064	2 486
Bank guarantees and letters of credit (Note 18)	51	-
Recoveries on loans previously written off	(736)	(177)
	1 379	**2 309**

7 Income tax expense

	1999	1998
Current tax	389	352
Deferred tax	(28)	(90)
	361	**262**

Taxation is payable at an effective rate of 10% (1998: 10 %) on taxable profits. The standard income tax rate in Georgia is 20%. Under the Georgian Law, the Bank enjoys a 50% tax exemption from the standard income tax rate due to the foreign equity participation in the Bank. This tax exemption is valid for the six-year period from 1995 to 2001. Afterwards, the Bank will be subject to the standard income tax rate for the country.

	1999	1998
Profit before tax	3 488	2 746
Prima facie tax calculated at a tax rate of 10% [1998: 10%]	348	275
Effect of deferred tax	28	90
Tax effect of items not assessable for tax purposes	(15)	(103)
Income tax expense	**361**	**262**

Further information about deferred tax is presented in Note 17.

8 Cash and balances with the central bank

	1999	1998
Cash in hand	1 919	441
Balances with the central bank	6 408	2 322
	8 327	2 763

Balances with the central bank include mandatory reserves of 4 018 KGEL (1998: 1 711 KGEL). These funds are not available to finance the day-to-day operations of the bank.

9 Due from other banks

	1999	1998
Loans and advances to other banks	965	554
Placements with other banks	12 661	9 013
	13 626	9 567

Balances placements with other banks include 994 KGEL, which are blocked under L/C and Guarantees. (1998: nil)

10 Loans and advances to customers

	1999	1998
Loans to private entities	34 350	15 774
Loans to individuals	4 115	2 533
Gross loans and advances	38 465	18 307
Less specific provisions for doubtful debts	(1 621)	(1 512)
Less general provision for doubtful debts	(769)	(366)
Net loans	36 075	16 429

10 Loans and advances to customers (continued)

Movement in provisions for doubtful debts was as follows:

	Provision
Balance at 1 January 1998	354
Loan loss provision expense	2 486
Bad debts written off	(962)
Balance at 31 December 1998	1 878
Doubtful debts expense	2 064
Bad debts written off	(1 552)
Balance at 31 December 1999	2 390

Economic sector risk concentrations within the customer loan portfolio were as follows:

	1999	1999 %	1998	1998 %
Trade	13 126	34.12	5 443	29.75
Services	4 767	12.39	3 034	16.58
Industries	8 544	22.21	3 598	19.66
Agriculture	891	2.32	482	2.63
Construction	3 236	8.41	1 355	7.41
Consumption	4 115	10.71	3 805	20.80
Other	3 786	9.84	590	3.17
Total	38 465	100	18 307	100

Loans and advances are further analysed as a part of the balance sheet in the following notes: Currency risk Note 22, Interest rate risk Note 23, and Liquidity risk Note 24.

11 Investment securities

	1999	1998
Equity securities	1 508	515
Government securities	510	-
Less provision for diminution in value	(48)	(64)
Net investments	1 970	451

The government securities are T-bills issued by the Government of Republic of Georgia. They are pledged under the borrowing from the National Bank of Georgia.

The equity securities are principally analyzed as follows:

Name	Nature of business	1999	1999 %	1998	1998 %
Microfinance bank	Banking	980	19.60	190	3.80
Bank of Georgia	Banking	315	3.85	123	1.53
Union Financial Corporation	Finance	130	20.00	146	20.00
Others		83	-	56	-
Total equity investments at cost		1 508		515	
Less provisions for diminution value		(48)		(64)	
Net investments		1 460		451	

12 Property and equipment

	Land and buildings	Fixtures and fittings	Machines and equipment	Vehicles	Intangible Assets	Assets in progress	Total
At 31 December 1998							
Gross book amount	2 238	334	382	181	30	158	3 323
Accumulated depreciation	(107)	(81)	(80)	(41)	(10)	-	(319)
Net book amount	2 131	253	302	140	20	158	3 004
Year ended December 1999							
Opening net book amount	2 131	253	302	140	20	158	3 004
Additions	295	128	176	14	112	17	7.
Disposals	(92)	(45)	(71)	(3)	(4)	(140)	(355)
Depreciation charge	(91)	(62)	(91)	(39)	(14)	-	(297)
Closing net book amount	2 243	274	316	112	114	35	3 094
At 31 December 1999							
Gross book amount	2 438	416	461	187	138	35	3 675
Accumulated depreciation	(195)	(142)	(145)	(75)	(24)	-	(581)
Net book amount	2 243	274	316	112	114	35	3 094

13 Interest receivable and other assets

	1999	1998
Accrued interest receivable	1 157	1 322
Deferred tax asset (Note 17)	122	94
Other	1 062	271
	2 341	1 687

14 Due to other banks

	1999	1998
Current accounts	1 325	6
Loans from other banks	22 067	7 882
	23 392	7 888

Loans from other banks include 12 035 KGEL borrowings from international credit institutions (1998: 7 882 KGEL)

15 Due to customers

	1999	1998
Current accounts, including		
-- from individuals	1 079	1 222
-- from companies and government organisations	16 641	8 535
	17 720	9 757
Deposits and savings accounts, including		
-- from individuals	8 955	3 836
-- from companies and government organisations	4 134	3 883
	13 089	7 719
	30 809	17 476

16 Interest payable and other liabilities

	1999	1998
Accrued interest payable	826	620
Provisions for bank guarantees (Note 18)	51	-
Accrued salary	139	303
Accrued audit expense	105	80
Other liabilities	224	610
	1 345	1 613

17 Deferred income taxes

The movement on the deferred income tax account is as follows:

	1999	1998
At beginning of year	94	4
Income statement credit	28	90
At end of year	122	94

Deferred income tax assets and liabilities are attributable to the following items:

	1999	1998
Deferred income tax liabilities		
Accrued interest and other assets	-	(105)
Deferred income tax assets		
Provision for loan losses	6	97
Depreciation	16	1
Accrued interest and other liabilities	100	101
Net deferred income tax asset	122	94

18 Contingent liabilities and commitments

<u>Credit related commitments.</u>

The following table indicates the contractual amounts of the Bank's off-balance sheet financial instruments that commit it to extend credit to customers.

	1999	1998
Guarantees and letters of credit	7 937	2 978
Commitments to extend credit	880	7 439
Provision for bank guarantees (Note 6)	(51)	
	8 766	10 417

19 Ordinary shares

At the end of 1999 the share capital of the bank was composed of 30 000 ordinary shares with par value 100 GEL each. (1998: 29 776 shares). All the shares have one voting right and equal right on dividend.

20 Provisions for losses

The overall provision for losses is summarised as follows:

	At Dec 31, 1998	Provisions charged / (recovered)	Written off	At Dec 31, 1999
Loans and advances to customers (note 10)	1 878	2 065	(1 553)	2 390
Investment securities (note 11)	64	(16)	-	48
Guarantees and L/G (note 18)	-	51	-	51
Total provisions	1 942	2 100	(1 553)	2 489

21 Cash and cash equivalents

For the purposes of the cash flow statement, cash and cash equivalents comprises the following balances with less than 90 days maturity:

	1999	1998
Cash in hand (Note 8)	1 919	441
Balances with the central bank (Note 8)	2 390	850
Due from other banks (Note 9)	12 631	9 013
	16 940	10 304

22 Currency risk

Concentrations of assets and liabilities

The Bank maintains the following significant currency positions:

	GEL	USD	Other	Total
As at 31 December 1999				
Assets				
Cash and balances with central bank	5,785	2,486	56	8,327
Due from other banks	-	12,310	1,316	13,626
Loans and advances to customers	1,536	34,431	108	36,075
T-Bonds	510	-	-	510
Dealing securities	676	-	-	676
Equity investments	1,375	85	-	1,460
Property and equipment	3,094	-	-	3,094
Other assets	230	2,111	-	2,341
Total assets	13,206	51,423	1,480	66,109
Liabilities				
Due to other banks	2,080	18,329	2,983	23,392
Due to customers	2,648	27,360	801	30,809
Interest payable and other liabilities	166	1,158	21	1,345
Total liabilities	4,894	46,847	3,805	55,546
Net position	8,312	4,576	(2,325)	10,563
As at 31 December 1998				
Total assets	7,243	26,921	251	34,415
Total liabilities	1,922	23,690	1,365	26,977
Net position	5,321	3,231	(1,114)	7,438

23 Interest rate risk

Interest sensitivity of assets and liabilities

The Bank is exposed to various risks associated with the effects of fluctuations in the prevailing levels of market interest rates on its financial position and cash flows. The table below summarises the Bank's exposure to interest rate risks. Included in the table are the Bank's assets and liabilities at carrying amounts, categorised by the earlier of contractual repricing or maturity dates.

As at 31 December 1999	Up to 3 months	3-12 months	1-5 years	Non-interest bearing	Total
Assets					
Cash and central bank balances	4,019	-	-	4,308	8,327
Due from other banks	772	58	-	12,796	13,626
Loans to customers	21,965	8,400	5,710	-	36,075
T-Bonds	510	-	-	-	510
Dealing securities	-	-	-	676	676
Investment securities	-	-	-	1,460	1,460
Property and equipment	-	-	-	3,094	3,094
Other assets	-	-	-	2,341	2,341
Total assets	27,266	8,458	5,710	24,675	66,109
Liabilities					
Due to other banks	16,765	2,321	2,981	1,325	23,392
Due to customers	7,006	5,853	270	17,680	30,809
Other liabilities	-	-	-	1,345	1,345
Total liabilities	23,771	8,174	3,251	20,350	55,546
Interest sensitivity gap	3,495	284	2,459		

The table below summarises the effective interest rate by major currencies for monetary financial instruments:

As at 31 December 1999	%	GEL	USD	Other
Assets				
Cash and balances with the central bank		10.0	0.0	0.0
Nostro accounts		0.0	5.2	0.0
Due from other banks		0.0	28.0	0.0
Loans and advances to customers		19.6	27.9	30.0
Liabilities				
Due to other banks		15.0	8.0	9.3
Loro accounts		0.0	0.0	0.0
Due to customers		9.0	10.8	0.0

24 Liquidity risk

Maturities of assets and liabilities

As at 31 December 1999	Up to 3 month	3-12 months	1-5 years	Over 5 years	Total
Assets					
Cash and central bank balances	8,327	-	-	-	8,327
Due from other banks	13,568	58	-	-	13,626
Loans to customers	21,965	8,400	5,710	-	36,075
T-Bonds	510	-	-	-	510
Dealing securities	212	464	-	-	676
Investment securities	-	-	-	1,460	1,460
Fixed assets	-	-	-	3,094	3,094
Other assets	1,808	533	-	-	2,341
Total assets	46,390	9,455	5,710	4,554	66,109
Liabilities					
Due to other banks	11,526	300	11,566	-	23,392
Due to customers	24,686	5,853	270	-	30,809
Other liabilities	981	364	-	-	1,345
Total liabilities	37,193	6,517	11,836	-	55,546
Net liquidity gap	9,197	2,938	(6,126)	4,554	10,563
Cumulative liquidity gap	9,197	12,135	6,009	10,563	-
As at 31 December 1998					
Total assets	26,071	2,733	1,641	3,970	34,415
Total liabilities	16,906	2,304	7,767	-	26,977
Net liquidity gap	9,165	429	(6 126)	3,970	7,438
Cumulative liquidity gap	9,165	9 594	3,468	7 438	-

The table above analyses assets and liabilities of the Bank into relevant maturity rankings based on the remaining period at balance sheet date to the contractual maturity date.

The matching and controlled mismatching of the maturities and interest rates of assets and liabilities is fundamental to the management of the Bank. It is unusual for banks ever to be completely matched since business transacted is often of uncertain term and of different types. An unmatched position potentially enhances profitability, but can also increase the risk of losses.

25 Related party transactions

Parties are considered to be related if one party has the ability to control the other party or exercise significant influence over the other party in making financial or operational decisions.

A number of banking transactions are entered into with related parties in the normal course of business. These transactions have been carried out on normal commercial terms and conditions and at market rates.

The total amount of loans to directors as at 31 December 1999 is GEL 1.1 million.

26 Post balance sheet events

TBC-Bank and DEG, a German Investment and Development Company, signed on 2 February 2000 two Credit Line Agreements in the total amount of EURO 2 million. Both Credit Line Agreements were signed for 8 years with a three-year grace period. TBC-Bank will utilize EURO 1 million to acquire and refurbish new offices of the bank's headquarters. The second credit line provides resources for financing the development of small and medium size private business in Georgia.