# Credit Bank of Moscow

Financial statements
as of December 31, 2003 and 2002

# Contents

# Independent Auditors' Report

To the Council of JSC "Credit Bank of Moscow"

We have audited the accompanying balance sheets of JSC "Credit Bank of Moscow" ("the Bank") as of December 31, 2003 and 2002, and the related statements of income and other comprehensive income, stockholders' equity and cash flows for the years 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 audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. 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 audits provide 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, 2003 and 2002, and the results of its operations and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

KPMG Limited

KPMG Limited
Moscow, Russian Federation
March 16, 2004

**Credit Bank of Moscow**
**Balance sheets**
**December 31, 2003 and 2002**
**(thousands of US Dollars)**

| | Notes | December 31, 2003 | December 31, 2002 |
|---|---|---|---|
| **Assets** | | | |
| Cash and due from Central Bank | 4 | 52,061 | 41,549 |
| Due from credit institutions, net | 5 | 42,903 | 18,124 |
| Trading securities | 6 | 22,354 | 16,475 |
| Loans to customers, net | 7 | 257,356 | 135,104 |
| Property and equipment | 8 | 2,907 | 2,045 |
| Other assets | 9 | 2,474 | 1,383 |
| **Total assets** | | **380,055** | **214,680** |
| **Liabilities** | | | |
| Deposits by credit institutions | 10 | 60,279 | 12,089 |
| Deposits by customers | 11 | 133,168 | 81,160 |
| Promissory notes and certificates of deposit | 12 | 93,330 | 51,218 |
| Deferred tax liability | 20 | 5,655 | 5,013 |
| Provisions, accruals and other liabilities | | 3,150 | 994 |
| **Total liabilities** | | **295,582** | **150,474** |
| **Stockholders' equity** | | | |
| Common stock | 13 | 23,340 | 21,898 |
| Additional paid-in capital | | 47,212 | 38,558 |
| Retained earnings | 14 | 8,287 | 3,750 |
| Other comprehensive income - cumulative translation adjustment | | 5,634 | - |
| **Total stockholders' equity** | | **84,473** | **64,206** |
| **Total liabilities and stockholders' equity** | | **380,055** | **214,680** |
| Commitments and contingencies | 21 | | |

**Signed on behalf of the Executive Management Board**

Andrey M. Donskikh — Chairman of the Executive Management Board

Olga I. Melnikova — Chief Accountant

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

## Credit Bank of Moscow
## Statements of income and other comprehensive income
## For the years ended December 31, 2003 and 2002
**(thousands of US Dollars, except per share data)**

| | Notes | 2003 | 2002 |
|---|---|---|---|
| Interest income | 15 | 29,411 | 22,268 |
| Interest expense | 15 | (7,371) | (2,756) |
| Net interest income | | 22,040 | 19,512 |
| Provision for credit impairment | 16 | (8,891) | (157) |
| **Net interest income after provision for credit impairment** | | **13,149** | **19,355** |
| Fees and commissions received | 17 | 8,438 | 6,396 |
| Securities trading profits, net | 18 | 417 | 237 |
| Other operating income | | 508 | 219 |
| Foreign exchange gains, net | | 927 | - |
| **Non interest income** | | **10,290** | **6,852** |
| Salaries and employment benefits | 19 | 8,972 | 6,466 |
| Administrative expenses | 19 | 7,451 | 4,362 |
| Foreign exchange losses, net | | - | 1,642 |
| Depreciation and amortization | | 853 | 545 |
| Other operating expenses | | 581 | 375 |
| **Non interest expense** | | **17,857** | **13,390** |
| **Income before income taxes** | | **5,582** | **12,817** |
| Income taxes | 20 | (1,045) | (4,003) |
| **Net income** | | **4,537** | **8,814** |
| Foreign currency translation adjustments | | 5,634 | - |
| **Other comprehensive income** | | **5,634** | **-** |
| **Comprehensive income** | | **10,171** | **8,814** |

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

# Credit Bank of Moscow
## Statements of changes in stockholders' equity and other comprehensive income
## For the years ended December 31, 2003 and 2002
**(thousands of US Dollars)**

| | Common stock | Additional paid-in capital | Unpaid common stock and additional paid-in capital | (Accumulated losses) / Retained earnings | Other comprehensive income - cumulative translation adjustment | Total stockholders' equity |
|---|---|---|---|---|---|---|
| **December 31, 2001** | **21,898** | **38,558** | **(11,021)** | **(5,064)** | **-** | **44,371** |
| Stock paid | - | - | 11,021 | - | - | 11,021 |
| Net income | - | - | - | 8,814 | - | 8,814 |
| **December 31, 2002** | **21,898** | **38,558** | **-** | **3,750** | **-** | **64,206** |
| Shares issued | 1,442 | 8,654 | - | - | - | 10,096 |
| Net income | - | - | - | 4,537 | - | 4,537 |
| Translation adjustment | - | - | - | - | 5,634 | 5,634 |
| **December 31, 2003** | **23,340** | **47,212** | **-** | **8,287** | **5,634** | **84,473** |

Translation adjustment has been shown net of deferred tax of USD 150 thousand at 31 December, 2003.

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

## Credit Bank of Moscow
## Statements of cash flow
## For the years ended December 31, 2003 and 2002
**(thousands of US Dollars)**

| | Notes | 2003 | 2002 |
|---|---|---|---|
| **CASH FLOWS FROM OPERATING ACTIVITIES** | | | |
| **Net income** | | 4,537 | 8,814 |
| *Adjustments to reconcile net income to net cash provided by operating activities:* | | | |
| Provision for loan impairment | | 8,891 | 157 |
| Depreciation and amortization | | 853 | 545 |
| Deferred taxes | | 492 | 3,626 |
| Accrued interest income | | (270) | (184) |
| Accrued interest expense | | 866 | 230 |
| Other non cash items | | - | 328 |
| **Operating cash flow before changes in operating assets and liabilities** | | **15,369** | **13,516** |
| | | | |
| **(Increase)/decrease in operating assets** | | | |
| Reserve deposits with the Central Bank of the Russian Federation | | (4,962) | (1,081) |
| Trading securities | | (5,879) | (13,000) |
| Loans to customers | | (129,205) | (53,344) |
| Other assets | | (821) | (211) |
| **Increase/(decrease) in operating liabilities** | | | |
| Deposits by credit institutions | | 48,190 | 8,882 |
| Deposits by customers | | 52,008 | 15,022 |
| Promissory notes and certificates of deposit | | 41,677 | 31,983 |
| Provisions, accruals and other liabilities | | (211) | 248 |
| | | | |
| Unrealised translation adjustment | | 5,784 | - |
| | | | |
| **Net cash from operations** | | **21,950** | **1,927** |
| | | | |
| **CASH FLOWS FROM INVESTING ACTIVITIES** | | | |
| Net purchase of property and equipment and intangible assets | | (1,715) | (505) |
| **Net cash from investing activities** | | **(1,715)** | **(505)** |
| | | | |
| **CASH FLOWS FROM FINANCING ACTIVITIES** | | | |
| Issue/payment of common stock | | 10,096 | 11,021 |
| **Net cash from financing activities** | | **10,096** | **11,021** |
| | | | |
| **Change in cash and cash equivalents** | | **30,331** | **12,443** |
| | | | |
| Cash and cash equivalents, beginning of the year | | 52,996 | 40,553 |
| **Cash and cash equivalents, end of the year** | 22 | **83,327** | **52,996** |
| | | | |
| *Supplemental information:* | | | |
| Interest paid during the period | | **(6,505)** | **(2,526)** |
| Income taxes paid during the period | | **(553)** | **(264)** |

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

(All amounts in thousands of US Dollars)

## NOTE 1 – BACKGROUND

### (a) Organization and operations

Credit Bank of Moscow (the "Bank") was formed on August 5, 1992 as an open joint stock company, then re-registered as a closed joint stock company under the laws of the Russian Federation. On August 18, 1999 the Bank was reorganized as an open joint stock company. The Bank's registered legal address is 4, Marshala Rybalko Str., Moscow, Russia. The Bank possesses a general banking license from the Central Bank of Russia (the "CBR"), granted on January 20, 2001. The Bank is among the 60 largest banks in Russia. The Bank's main office is in Moscow and it has 12 full service branches in Moscow.

At December 31, 2003 the stockholders of the Bank were as follows:

| | 2003 (voting and ownership rights) |
|---|---|
| Inform Personal | 26% |
| Centre Servicestroy | 15% |
| Yuriditcheskoye agentstvo | 15% |
| Capital MKB | 13% |
| MKB – Holding | 13% |
| Rossinform | 11% |
| Balansovoye planirovanie | 6% |
| Concern Rossium | 1% |
| **Total** | **100%** |

### (b) Operating environment

The Russian Federation has been experiencing political and economic instability change which has affected, and may continue to affect, the activities of enterprises operating in this environment. Consequently, operations in the Russian Federation involve risks which do not typically exist in other markets. The accompanying financial statements reflect management's assessment of the impact of the Russian business environment on the operations and the financial position of the Bank. The future business environment may differ from management's assessment.

## NOTE 2 – BASIS OF PREPARATION

### (a) Statement of compliance

The financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America ("US GAAP").

### (b) Reporting currency and translation into US dollars

Prior to December 31, 2002 Russian economy was considered to be hyperinflationary and the Bank used US Dollar as its functional and reporting currency. Starting January 1, 2003 the Russian economy is no longer considered to be hyperinflationary under Statement of Financial Accounting Standard 52 *Foreign Currency Translation.* Accordingly the Bank has conducted an assessment of its operations and determined the Russian Rouble to be its functional currency. Management of the Bank have elected to use US Dollar as the reporting currency in these financial statements.

The carrying values of all non-monetary assets, liabilities and equity items were translated and fixed in Russian Rubles at the rates effective at the date of transition to the Russian Ruble as the functional currency, January 1, 2003. For the year ended December 31, 2003 translation from functional to reporting currency was conducted as follows:

- all assets and liabilities are translated from the functional to the reporting currency at the exchange rate, effective at the reporting date;
- equity items are translated from functional to reporting currency at the historical exchange rates. Translation adjustments arising from translation of equity are included in Other Comprehensive Income in accordance with SFAS 52;
- income statement transactions are translated from functional to reporting currency at the approximate rates ruling at the dates of the transactions. Translation adjustments arising from translation of income and expenses are included in Other Comprehensive Income in accordance with SFAS 52.

The closing rate of exchange effective at December 31, 2003 and December 31, 2002 was 1 USD to 29.45 Rubles and 1 USD to 31.78 Rubles, respectively.

**(c) Convertibility of the Ruble**
The Russian Ruble is not a convertible currency outside the Russian Federation and, accordingly, any conversion of Russian Ruble amounts to US dollars should not be construed as a representation that Russian Ruble amounts have been, could be, or will be in the future, convertible into US dollars at the exchange rate shown, or at any other exchange rate.

**(d) Going concern**
The accompanying financial statements have been prepared on a going concern basis, which contemplates the realization of assets and the satisfaction of liabilities in the normal course of business. The accompanying financial statements do not include any adjustments should the Bank be unable to continue as a going concern.

## NOTE 3 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The following significant accounting policies have been applied in the preparation of the financial statements. These accounting policies have been consistently applied.

***a) Use of estimates***
Management of the Bank has made a number of estimates and assumptions relating to the reporting of assets and liabilities and the disclosure of contingent assets and liabilities to prepare these financial statements in conformity with accounting principles generally accepted in the United States of America.  Actual results could differ from those estimates.

***b) Loans to customers***

The carrying amounts of the Bank's loans are reviewed at each balance sheet date to determine whether there is any indication of impairment. If any such indication exists, the loans' recoverable amounts are estimated.

An impairment loss is recognized whenever the carrying amount of a loan exceeds its recoverable amount.

The recoverable amount of loans is calculated as the present value of expected future cash flows, discounted at the original effective interest rate inherent in the loan.

***c) Due from credit institutions***

In the normal course of business, the Bank lends or deposits funds for various periods with other credit institutions. Impairment losses for placements with banks and other credit institutions is calculated in accordance with the policy similar to the one applied to loans to customers (refer 3(b) above).

***d) Trading securities***

Trading securities are carried at market value with the gains and losses recognized in the statement of income.

Included in securities trading profits are realized gains and losses from recording the results of sales and unrealized gains and losses resulting from market value adjustments of trading equity securities.

Included in interest income is coupon income, amortization of premiums and discounts and realized and unrealized gains and losses related to trading debt securities.

***e) Repurchase and reverse repurchase agreements***

Repurchase and reverse repurchase agreements are utilized by the Bank as an element of its treasury management and trading business. Repurchase agreements are accounted for as financing transactions. As financing transactions, the related securities are recorded in the Bank's accounts and the related payable is included as an amount due to credit institutions or customers, respectively. Any related expense arising from the pricing spreads for the underlying securities is recognized as interest expense.

Reverse repurchase agreements are accounted for as loans and advances to banks or customers, respectively. Any related income arising from the pricing spreads for the underlying securities is recognized as interest income.

***f) Property and equipment***

Property and equipment are recorded at historical cost less accumulated depreciation (refer below) and impairment losses (refer accounting policy (*h*)). Depreciation is provided to write off the cost on a straight-line basis over the estimated useful economic life of the asset. The economic lives are as follows:

| | **Years** |
|---|---|
| Buildings | 50 |
| Furniture and equipment | 6 |
| Computers | 4 |
| Vehicles | 5 |
| Other | 5 |

***g) Intangible assets***

Intangible assets are recorded at historical cost less accumulated amortization and impairment losses (refer accounting policy (*h*)). Amortization is provided to write off the cost on a straight-line basis over the estimated useful economic life of the asset. The majority of intangible assets is represented by accounting software.

***h) Impairment of property and equipment***

The Bank accounts for long lived assets in accordance with Statement of Financial Accounting Standards ("SFAS") No. 144 *Accounting for the Impairment or Disposal of Long-Lived Assets*.

Under this standard the carrying value of the asset is considered to be impaired when the anticipated undiscounted future cash flow from such asset is separately identifiable, and is less than the carrying value.

In that event, an impairment loss is recognized based on the amount by which the carrying value exceeds the fair market value of the asset. Impairment losses are recognized in the income statement. Fair market value is determined primarily using anticipated cash flows discounted at a rate commensurate with the risk involved.

***i) Interest bearing liabilities***

Interest-bearing liabilities are recognized initially at cost, net of any transaction costs incurred. Subsequent to initial recognition, interest-bearing liabilities are stated at amortized cost with any difference between cost and redemption value being recognized in the income statement over the period of the borrowings.

***j) Income and expense recognition***

Income and expenses are recognized on an accrual basis.

***k) Dividends***

Dividends are recognized as a liability in the period in which they are declared.

(All amounts in thousands of US Dollars)

***l) Taxes***

Income taxes are accounted for under the asset and liability method in accordance with Statement of Financial Accounting Standards ("SFAS") No. 109 *Accounting for Income Taxes*. Deferred tax assets and liabilities are recognized for the future tax consequences attributable to temporary differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases and operating loss and tax credit carryforwards. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the enactment date.

Russia also has various other operating taxes, which are assessed on the Bank's activities. These taxes are included as a component of non-interest expense.

***m) Statement of cash flows***

The Bank considers cash on hand, correspondent account with CBR and due from credit institutions with original maturities of three months or less to be cash equivalents.

## NOTE 4 – CASH AND DUE FROM CENTRAL BANK

Cash and due from Central Bank comprise:

| | December 31, 2003 | December 31, 2002 |
|---|---|---|
| Correspondent account with CBR | 29,489 | 22,042 |
| Obligatory reserve deposits with CBR | 11,639 | 6,677 |
| Cash on hand | 10,933 | 12,830 |
| **Cash and due from Central Bank** | **52,061** | **41,549** |

The obligatory reserve deposits are mandatory non-interest bearing deposits calculated in accordance with regulations issued by the CBR, the withdrawal of which is restricted, based on either a reduction in the Bank's deposit base or a reduction in the required level of reserves. The correspondent account with CBR represents balances held with the CBR related to settlement activity, and was available for withdrawal at period end.

Information about the currency breakdown and maturity profile of cash and due from Central Bank is presented in note 26 to these financial statements.

(All amounts in thousands of US Dollars)

### NOTE 5 – DUE FROM CREDIT INSTITUTIONS, NET

Due from credit institutions comprise:

| | December 31, 2003 | December 31, 2002 |
|---|---|---|
| Current accounts | 42,830 | 17,811 |
| Time deposits | 75 | 316 |
| Less: Provision for losses | (2) | (3) |
| **Due from credit institutions** | **42,903** | **18,124** |

Information about the currency breakdown, maturity profile and effective interest rates on amounts due from credit institutions is presented in note 26 to these financial statements.

## Concentration of balances due from credit institutions

As at 31 December 2003 the Bank maintained current accounts with 3 banks (31 December 2002: 2 banks) whose balances exceeded 10% of Bank's equity. The gross value of these balances as of 31 December 2003 and 2002 was USD 28,585 thousand and USD 7,849 thousand, respectively.

### NOTE 6 – TRADING SECURITIES

Trading securities, at fair value, consist of the following:

| | December 31, 2003 | December 31, 2002 |
|---|---|---|
| Debt instruments | | |
| Corporate promissory notes and bonds | 15,655 | 10,219 |
| Fixed income state debt securities (OFZ) | 1,710 | 4,014 |
| Municipal state bonds | 3,619 | 1,725 |
| Marketable equity securities | 1,370 | 517 |
| **Trading securities** | **22,354** | **16,475** |

Information about the currency breakdown, maturity profile and effective interest rates on Bank's trading securities is presented in note 26 to these financial statements.

(All amounts in thousands of US Dollars)

## NOTE 7 – LOANS TO CUSTOMERS, NET

The Bank's loan portfolio has been extended to private enterprises and individuals only. Loans to customers are made principally within the Russian Federation to the entities, which operate in the following economic sectors:

| | December 31, 2003 | December 31, 2002 |
|---|---|---|
| **Corporate banking** | | |
| Consumer electronics and computers | 44,771 | 28,601 |
| Food products | 42,039 | 22,546 |
| Hygiene products and consumer chemicals | 18,304 | 8,662 |
| Sporting goods | 16,699 | 5,539 |
| Construction materials | 15,025 | 15,257 |
| Paper and stationery | 11,948 | 9,529 |
| Light industry | 10,155 | 7,226 |
| Furniture | 8,753 | 8,273 |
| Machinery | 7,289 | 2,727 |
| Metal products | 4,670 | 3,279 |
| Medical goods | 3,806 | 3,642 |
| Oil products | 3,404 | 3,296 |
| Other customer goods | 5,086 | 1,058 |
| Other corporate | 25,262 | 15,739 |
| | **217,211** | **135,374** |
| **Retail banking** | | |
| Consumer loans | 52,458 | 5,089 |
| | **269,669** | **140,463** |
| Less – Provision for loan impairment | (12,313) | (5,359) |
| **Loans to customers, net** | **257,356** | **135,104** |

Information about the currency breakdown, maturity profile and effective interest rates on Bank's loan portfolio is presented in note 26 to these financial statements.

Information about the breakdown of the provision for loan impairment by corporate and retail lending is presented in Note 16 to these financial statements.

### Significant credit exposures

As at December 31, 2003 the Bank had two groups of borrowers (December 31, 2002: one) whose loans balances exceeded 10% of equity. The gross value of these loans as of December 31, 2003 was USD 30,023 thousand (December 31, 2002: USD 8,130 thousand).

(All amounts in thousands of US Dollars)

## NOTE 8 – PROPERTY AND EQUIPMENT

Property and equipment comprise:

| | December 31, 2003 | December 31, 2002 |
|---|---|---|
| Land and buildings | 867 | 758 |
| Fixtures and fittings | 4,693 | 3,218 |
| | **5,560** | **3,976** |
| Less - accumulated depreciation | (2,653) | (1,931) |
| **Property and equipment** | **2,907** | **2,045** |

## NOTE 9 – OTHER ASSETS

Other assets comprise:

| | December 31, 2003 | December 31, 2002 |
|---|---|---|
| Accrued interest receivable | 874 | 604 |
| Trade debtors and prepayments | 643 | 218 |
| Prepaid expenses | 381 | 76 |
| Intangibles | 241 | 182 |
| Other | 335 | 303 |
| **Other assets** | **2,474** | **1,383** |

## NOTE 10 – DEPOSITS BY CREDIT INSTITUTIONS

Deposits by credit institutions comprise:

| | December 31, 2003 | December 31, 2002 |
|---|---|---|
| Demand deposits | 20,345 | 2,621 |
| Time deposits | 39,934 | 9,468 |
| **Deposits by credit institutions** | **60,279** | **12,089** |

Information about the currency breakdown, maturity profile and effective interest rates on deposits by credit institutions is presented in note 26 to these financial statements.

### Concentration of deposits from credit institutions

As at December 31, 2003 the Bank had balances of 3 banks (December 31, 2002: 2 banks) whose deposits' balances exceeded 10% of equity. The gross value of these balances as of December 31, 2003 was USD 13,582 thousand in respect of demand deposits and USD 15,002 thousand in respect of time deposits (December 31, 2002: USD 7,849 thousand – all demand deposits).

(All amounts in thousands of US Dollars)

## NOTE 11 – DEPOSITS BY CUSTOMERS

Deposits by customers comprise:

| | December 31, 2003 | December 31, 2002 |
|---|---|---|
| Demand deposits | 79,705 | 52,580 |
| Time deposits | 53,463 | 28,580 |
| **Deposits by customers** | **133,168** | **81,160** |

### Concentrations of current accounts and customer deposits

As at December 31, 2003 and 2002, there were no demand or time deposits from customers, which individually exceeded 10% of equity.

Information about the currency breakdown, maturity profile and effective interest rates on deposits by customers is presented in note 26 to these financial statements.

## NOTE 12 – PROMISSORY NOTES AND CERTIFICATES OF DEPOSIT

| | December 31, 2003 | December 31, 2002 |
|---|---|---|
| Promissory notes issued – nominal value | 59,883 | 47,532 |
| Unamortized discount on promissory notes | (622) | (719) |
| | 59,261 | 46,813 |
| Certificates of deposit | 34,069 | 4,405 |
| | **93,330** | **51,218** |

Information about the currency breakdown, maturity profile and effective interest rates on promissory notes and certificates of deposit is presented in note 26 to these financial statements.

## NOTE 13 – COMMON STOCK

The stockholders' equity of the Bank has been contributed by stockholders in Rubles. Stockholders are entitled to dividends and capital distributions in the currency in which their contribution was made.

Issued, outstanding and paid stock comprised 393,289,502 shares (December 31, 2002: 350,289,502 shares) with par value of 1 RUR per share. For the purposes of these financial statements stockholders' equity was translated into US dollars using the exchange rates ruling at the dates of its contribution.

(All amounts in thousands of US Dollars)

## NOTE 14 – RETAINED EARNINGS

The Bank's distributable reserves are determined according to legislation in the Russian Federation. In accordance with the legislation of the Russian Federation, as of the balance sheet date, net income and retained earnings available for distribution amount to USD 5,145 thousand (December 31, 2002: USD 2,430 thousand).

## NOTE 15 – NET INTEREST INCOME

Net interest income comprises:

| | December 31, 2003 | December 31, 2002 |
|---|---|---|
| **Interest income** | | |
| Loans to customers | 25,569 | 19,707 |
| Debt securities | 3,571 | 2,123 |
| Due from credit institutions | 271 | 438 |
| | **29,411** | **22,268** |
| **Interest expense** | | |
| Deposits by customers | (3,447) | (1,439) |
| Promissory notes and certificates of deposit | (3,517) | (1,096) |
| Deposits by credit institutions | (407) | (221) |
| | **(7,371)** | **(2,756)** |
| **Net interest income** | **22,040** | **19,512** |

## NOTE 16 – PROVISION FOR CREDIT IMPAIRMENT

Provisions for impairment in the income statement represent the charge required in the current year to establish the total provision for impairment.

In 2003 the Bank has significantly expanded its retail banking operations (See Note 7), and further growth of these operations is expected in 2004. Also in 2004 the Bank plans to run various SME lending programs. The Bank has introduced a credit-scoring system to manage credit risks associated with this business. The retail loan portfolio is mostly represented by car loans. These loans are fully covered by collateral of cars and additionally secured by car insurance and life insurance of borrowers. Although 99% of these loans were classified as "standard" as of December 31, 2003, given the vast expansion of retail customer base and the absence of reliable credit history for this base, management considers retail lending business more risky and thus decided to increase the level of provisioning rate on "standard" retail loan portfolio as compared to "standard" provisioning rate on loans to corporate customers.

(All amounts in thousands of US Dollars)

The breakdown of the loan loss provisions by type is presented in the following table:

| | Loans to customers, corporate | Loans to customers, retail | Due from credit institutions | Off balance sheet items | Total allowance |
|---|---|---|---|---|---|
| **December 31, 2002** | **5,191** | **168** | **3** | **183** | **5,545** |
| Provisions charged / recovered | 3,893 | 3,061 | (1) | 1,938 | 8,891 |
| **December 31, 2003** | **9,084** | **3,229** | **2** | **2,121** | **14,436** |

The estimate of loan losses includes consideration of specific loss exposures identified with respect to individual credits as well as judgmental consideration of risk factors unique to the Bank's loan portfolio and the economy in which the borrowers operate.

## NOTE 17 – FEES AND COMMISSIONS RECEIVED

Fees and commissions received comprise:

| | 2003 | 2002 |
|---|---|---|
| Settlements and wire transfers | 3,608 | 3,360 |
| Cash operations | 1,957 | 1,052 |
| Guarantees issued | 512 | 850 |
| Other | 2,361 | 1,134 |
| **Fees and commissions received** | **8,438** | **6,396** |

## NOTE 18 – SECURITIES TRADING PROFITS, NET

Securities trading profits comprise:

| | 2003 | 2002 |
|---|---|---|
| Gains from operations with equity securities | 481 | 325 |
| Losses from operations with equity securities | (64) | (88) |
| **Securities trading profits, net** | **417** | **237** |

(All amounts in thousands of US Dollars)

## NOTE 19 – SALARIES, EMPLOYMENT BENEFITS AND ADMINISTRATIVE EXPENSES

Salaries, employment benefits and administrative expenses comprise:

| | 2003 | 2002 |
|---|---|---|
| Salaries | 8,659 | 6,201 |
| Social security costs | 313 | 265 |
| **Salaries and employment benefits** | **8,972** | **6,466** |
| | | |
| Occupancy | 2,761 | 1,881 |
| Business development | 1,643 | 443 |
| Operating taxes | 1,617 | 1,110 |
| Communications | 581 | 467 |
| Other | 849 | 461 |
| **Administrative expenses** | **7,451** | **4,362** |

The Bank does not have pension arrangements separate from the State pension system of the Russian Federation. The Russian Federation system requires current contributions by the employer calculated as a percentage of current gross salary payments; such expense is charged to the income statement in the period the related compensation is earned by the employee. The Bank does not have any stock option plans.

## NOTE 20 –INCOME TAXES

The provision for income taxes comprises:

| | 2003 | 2002 |
|---|---|---|
| Current tax charge | 553 | 377 |
| Deferred taxation | 492 | 3,626 |
| **Taxation** | **1,045** | **4,003** |

Russian legal entities must report taxable income and remit income taxes thereon to the appropriate authorities. The current year income tax rate for the Bank is 24%.

The effective income tax rate differs from the statutory income tax rates. A reconciliation of the provision for income taxes based on statutory rates with the actual provision for income taxes follows:

(All amounts in thousands of US Dollars)

| | 2003 | 2002 |
|---|---|---|
| Income before tax | 5,582 | 12,817 |
| Applicable statutory tax rate | 24% | 24% |
| Income tax using the applicable tax rate | 1,340 | 3,076 |
| Non-deductible costs/(non-taxable income) | (295) | 927 |
| | **1,045** | **4,003** |

Accumulated temporary differences between the carrying amounts of assets and liabilities reflected in these financial statements and their bases for local taxation purposes give rise to a net deferred tax liability of USD 5,655 thousand as of December 31, 2003 (2002: USD 5,013 thousand). This deferred tax liability is attributable to the following items, listed below at their tax effected values:

| | December 31, 2003 | December 31, 2002 |
|---|---|---|
| Property and equipment | (51) | (128) |
| **Deferred tax assets** | **(51)** | **(128)** |
| Provisions | 5,581 | 5,116 |
| Other | 125 | 25 |
| **Deferred tax liabilities** | **5,706** | **5,141** |
| **Net deferred tax liability** | **5,655** | **5,013** |

The USD 150 thousand increase in the deferred tax liability resultant of from the change in the functional currency at January 1, 2003 was included directly in other comprehensive income in stockholders' equity. The remaining net change in the deferred tax liability has been recognised in the income statement.

The applicable deferred tax rate for the Bank is 24% (2002: 24%).

## NOTE 21 – COMMITMENTS AND CONTINGENCIES

*a) Financial commitments*

Undrawn loan commitments and guarantees at December 31, 2003 and 2002 comprise:

| | December 31, 2003 | December 31, 2002 |
|---|---|---|
| **Commitments given** | | |
| Undrawn loan commitments | 11,073 | 39,925 |
| Guarantees | 34,127 | 8,303 |
| | **45,200** | **48,228** |

(All amounts in thousands of US Dollars)

At December 31, 2003 the Bank provided for potential losses on guarantees in the amount of USD 2,121 thousand (December 31, 2002: USD 183 thousand).

*c) Legal*

Bank management is unaware of any significant actual, pending or threatened claims against the Bank.

*d) Insurance*

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

*e) Tax*

The taxation system in the Russian Federation is relatively new and is characterized by numerous taxes and frequently changing legislation which is often unclear, contradictory, and subject to interpretation. Often, differing interpretations exist among numerous taxation authorities and jurisdictions. Taxes are subject to review and investigation by a number of authorities, who are enabled by law to impose severe fines, penalties and interest charges.

These facts may create tax risks in the Russian Federation substantially more significant than in other countries. Management believes that it has adequately provided for tax liabilities based on its interpretation of tax legislation. However, the relevant authorities may have differing interpretations and the effects could be significant.

## NOTE 22 – CASH AND CASH EQUIVALENTS

Cash and due from Central Bank comprise:

| | **December 31, 2003** | **December 31, 2002** |
|---|---:|---:|
| Cash on hand | 10,933 | 12,830 |
| Correspondent account with the CBR | 29,489 | 22,042 |
| Due from credit institutions with the original maturity of less then 3 months | 42,905 | 18,124 |
| **Cash and cash equivalents** | **83,327** | **52,996** |

(All amounts in thousands of US Dollars)

## NOTE 23 – RELATED PARTIES

The outstanding balances and related average interest rates as of December 31, 2003 and 2002 with related parties are as follows:

| | December 31, 2003 | | December 31, 2002 | |
|---|---|---|---|---|
| | Amount | Average effective interest rate | Amount | Average effective interest rate |
| *Assets* | | | | |
| Loans to customers, gross | 18,764 | 12.9% | 7,032 | 21.1% |
| Due from credit institutions | - | - | 40 | 0.0% |
| *Liabilities* | | | | |
| Deposits by customers | 820 | 2.1% | 639 | 10.0% |
| Deposits by credit institutions | - | - | 401 | 1.0% |

Material amounts included in the income statements for years ended December 31, 2003 and 2002 in relation to transactions with related parties are as follows:

| | Year ended December 31, 2003 | Year ended December 31, 2002 |
|---|---|---|
| Interest income on loans to customers | 1,661 | 1,037 |

## NOTE 24 – CAPITAL ADEQUACY

The Bank's risk based capital adequacy ratio as at December 31, 2003 and 2002 was 28% and 33%, respectively, which exceeds the minimum ratio of 8% recommended by the Basle Accord.

## NOTE 25 – FAIR VALUE OF FINANCIAL INSTRUMENTS

The following disclosure of the estimated fair value of financial instruments is made in accordance with the requirements of SFAS No.107. The Bank has performed an assessment of its financial instruments to determine whether it is practicable within the constraints of timeliness and cost to determine their fair values with sufficient reliability.

(All amounts in thousands of US Dollars)

The Bank has concluded that due to the lack of liquidity and published "indicator interest rates" in the Russian markets, and the fact that some of its transactions are with related parties and of a specialized nature, it is not possible to determine the fair value of the obligatory reserve deposits with CBR, loans to customers, deposits by customers, promissory notes and certificates of deposit.

The financial assets and financial liabilities that the Bank does believe it is able to estimate fair values for are as follows:

| | December 31, 2003 | | December 31, 2002 | |
|---|---|---|---|---|
| | Carrying value | Fair value | Carrying value | Fair value |
| **Financial Assets** | | | | |
| Cash and correspondent account with CBR | 40,422 | 40,422 | 34,872 | 34,872 |
| Due from credit institutions, net | 42,903 | 42,903 | 18,124 | 18,124 |
| Trading securities | 22,354 | 22,354 | 16,475 | 16,475 |
| **Financial Liabilities** | | | | |
| Deposits by credit institutions | 60,279 | 60,279 | 12,089 | 12,089 |

The following methods and assumptions were used to estimate the fair value of each class of financial instruments:

Cash and correspondent account with CBR, due from credit institutions and deposits by credit institutions: the carrying amounts approximate fair value because of the short maturity of these instruments.

Trading securities: the fair values are based on quoted market prices for these or similar instruments.

This estimate of fair value is intended to approximate the amount at which the above listed assets could be exchanged in a current transaction between willing parties. However given the uncertainties and the use of subjective judgment, the fair value should not be interpreted as being realizable in an immediate settlement of the instruments.

## NOTE 26 – 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 counterparty 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.

Exposure to credit risk is managed through regular analysis of the ability of borrowers and potential borrowers to meet interest and principal 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.

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 usually bear limited credit risk.

With respect to undrawn loan commitments the Bank is potentially exposed to loss in an amount equal to the total amount of such commitments. However, the likely amount of loss is less than that, since most commitments are contingent upon certain conditions set out in the loan agreements. The geographical concentration of monetary assets and liabilities follows:

(All amounts in thousands of US Dollars)

| | December 31, 2003 | | | | December 31, 2002 | | | |
|---|---|---|---|---|---|---|---|---|
| | **Russia** | **OECD** | **Other non-OECD** | **Total** | **Russia** | **OECD** | **Other non-OECD** | **Total** |
| **Assets** | | | | | | | | |
| Cash and due from CBR | 49,482 | 2,579 | - | 52,061 | 36,357 | 5,186 | 6 | 41,549 |
| Due from credit institutions, gross | 35,210 | 7,690 | 5 | 42,905 | 9,007 | 9,107 | 13 | 18,127 |
| Trading securities | 22,354 | - | - | 22,354 | 16,475 | - | - | 16,475 |
| Loans to customers, gross | 269,639 | - | 30 | 269,669 | 140,463 | - | - | 140,463 |
| | **376,685** | **10,269** | **35** | **386,989** | **202,302** | **14,293** | **19** | **216,614** |
| **Liabilities** | | | | | | | | |
| Deposits by credit institutions | 38,862 | 17,411 | 4,006 | 60,279 | 8,931 | 2,157 | 1,001 | 12,089 |
| Deposits by customers | 131,955 | 106 | 1,107 | 133,168 | 80,415 | 5 | 740 | 81,160 |
| Promissory notes and certificates of deposit | 93,330 | - | - | 93,330 | 51,218 | - | - | 51,218 |
| | **264,147** | **17,517** | **5,113** | **286,777** | **140,564** | **2,162** | **1,741** | **144,467** |
| **Net position** | **112,538** | **(7,248)** | **(5,078)** | **100,212** | **61,738** | **12,131** | **(1,722)** | **72,147** |

## 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. These limits also comply with the minimum requirements of the Central Bank of Russia. The Bank's exposure to foreign currency exchange rate risk is as follows:

| | December 31, 2003 | | | | December 31, 2002 | | | |
|---|---|---|---|---|---|---|---|---|
| | **USD** | **Rubles** | **Other currencies** | **Total** | **USD** | **Rubles** | **Other currencies** | **Total** |
| **Assets** | | | | | | | | |
| Cash and due from CBR | 1,886 | 49,482 | 693 | 52,061 | 4,736 | 36,358 | 455 | 41,549 |
| Due from credit institutions, gross | 7,274 | 34,967 | 664 | 42,905 | 8,722 | 8,619 | 786 | 18,127 |
| Trading securities | 48 | 22,306 | - | 22,354 | 41 | 16,434 | - | 16,475 |
| Loans to customers, gross | 96,054 | 165,200 | 8,415 | 269,669 | 47,575 | 85,314 | 7,574 | 140,463 |
| | **105,262** | **271,955** | **9,772** | **386,989** | **61,074** | **146,725** | **8,815** | **216,614** |
| **Liabilities** | | | | | | | | |
| Deposits by credit institutions | 30,520 | 22,299 | 7,460 | 60,279 | 8,636 | 395 | 3,058 | 12,089 |
| Deposits by customers | 36,329 | 89,703 | 7,136 | 133,168 | 24,894 | 54,402 | 1,864 | 81,160 |
| Promissory notes and certificates of deposit | 14,284 | 70,812 | 8,234 | 93,330 | 19,630 | 29,569 | 2,019 | 51,218 |
| | **81,133** | **182,814** | **22,830** | **286,777** | **53,160** | **84,366** | **6,941** | **144,467** |
| **Net position** | **24,129** | **89,141** | **(13,058)** | **100,212** | **7,914** | **62,359** | **1,874** | **72,147** |

(All amounts in thousands of US Dollars)

## Liquidity risk

The Bank is exposed to daily calls on its available cash resources from overnight deposits, current deposits, maturing deposits, loan draw downs and guarantees. The Bank maintains liquidity management with the objective of ensuring that funds will be available at all times to honor all cash flow obligations as they become due. The Bank's Asset and Liability 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.

The contractual maturities of monetary assets and liabilities as of June 30, 2003 and December 31, 2002 are as follows:

**December 31, 2003**

| | Less than 1 month | 1 – 6 months | 6 months to 1 year | Over 1 year | No maturity | Overdue | Total |
|---|---|---|---|---|---|---|---|
| **Assets** | | | | | | | |
| Cash and due from CBR | 40,422 | - | - | - | 11,639 | - | 52,061 |
| Due from credit institutions, gross | 42,905 | - | - | - | - | - | 42,905 |
| Trading securities | 1,235 | 6,624 | 3,981 | 9,139 | 1,375 | - | 22,354 |
| Loans to customers, gross | 58,146 | 118,954 | 36,740 | 55,180 | - | 649 | 269,669 |
| | **142,708** | **125,578** | **40,721** | **64,319** | **13,014** | **649** | **386,989** |
| **Liabilities** | | | | | | | |
| Deposits by credit institutions | 38,867 | 17,504 | - | 3,908 | - | - | 60,279 |
| Deposits by customers | 85,640 | 37,659 | 9,776 | 93 | - | - | 133,168 |
| Promissory notes and certificates of deposit | 37,046 | 50,476 | 5,808 | - | - | - | 93,330 |
| | **161,553** | **105,639** | **15,584** | **4,001** | **-** | **-** | **286,777** |
| **Net position** | **(18,845)** | **19,939** | **25,137** | **60,317** | **13,014** | **649** | **100,212** |
| ***Accumulated gap*** | **(18,845)** | **1,094** | **26,231** | **86,548** | **99,562** | **100,211** | |

**December 31, 2002**

| | Less than 1 month | 1 – 6 months | 6 months to 1 year | Over 1 year | No maturity | Overdue | Total |
|---|---|---|---|---|---|---|---|
| **Assets** | | | | | | | |
| Cash and due from CBR | 34,872 | - | - | - | 6,677 | - | 41,549 |
| Due from credit institutions, gross | 18,127 | - | - | - | - | - | 18,127 |
| Trading securities | 908 | 6,093 | 7,807 | 1,150 | 517 | - | 16,475 |
| Loans to customers, gross | 46,730 | 52,672 | 30,900 | 9,663 | - | 498 | 140,463 |
| | **100,637** | **58,765** | **38,707** | **10,813** | **7,194** | **498** | **216,614** |
| **Liabilities** | | | | | | | |
| Deposits by credit institutions | 10,603 | - | 328 | 1,158 | - | - | 12,089 |
| Deposits by customers | 61,770 | 13,231 | 6,043 | 116 | - | - | 81,160 |
| Promissory notes and certificates of deposit | 29,604 | 16,984 | 4,630 | - | - | - | **51,218** |
| | **101,977** | **30,215** | **11,001** | **1,274** | **-** | **-** | **144,467** |
| **Net position** | **(1,340)** | **28,550** | **27,706** | **9,539** | **7,194** | **498** | **72,147** |
| ***Accumulated gap*** | **(1,340)** | **27,210** | **54,916** | **64,455** | **71,649** | **72,147** | |

(All amounts in thousands of US Dollars)

The maturity gap analysis does not reflect the historical stability of current accounts, whose liquidation has historically taken place over a longer period than that indicated in the table above. The table is based upon these accounts' entitlement to withdraw on demand.

### 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 disclosed 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.

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 at December 31, 2003 and 2002 for interest bearing financial instruments follow.

| | **December 31, 2003** | | | **December 31, 2002** | | |
|---|---|---|---|---|---|---|
| | **US Dollars** | **Rubles** | **Other foreign currencies** | **US Dollars** | **Rubles** | **Other foreign currencies** |
| **Interest earning assets** | | | | | | |
| Due from credit institutions | 0.1% | 0.0% | 0.0% | 0.2% | 0.3% | 1.3% |
| Trading securities – government bonds | 7.3% | 4.3% | - | 6.7% | 12.9% | - |
| Trading securities – corporate notes and municipal bonds | - | 9.8% | - | - | 15.9% | - |
| Loans to customers | 12.9% | 10.7% | 8.6% | 16.5% | 13.5% | 14.3% |
| **Interest bearing liabilities** | | | | | | |
| Deposits by credit institutions | 3.0% | 0.1% | 3.2% | 0.4% | 1.0% | 4.2% |
| Deposits by customers | 5.6% | 3.0% | 6.9% | 5.7% | 1.0% | 7.0% |
| Promissory notes and certificates of deposit | 6.3% | 10.8% | 4.6% | 8.0% | 14.5% | 3.3% |