JSC BASISBANK

Financial Statements and Auditors' Report

31 December 2003

PRICEWATERHOUSECOOPERS

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AUDITORS' REPORT

To the shareholders of JSC Basisbank:

We have audited the accompanying balance sheet of JSC Basisbank (the "Bank") as at 31 December 2003, and the related statements of income, of cash flows and of changes in shareholders' equity 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.

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 accompanying financial statements present fairly, in all material respects, the financial position of the Bank as at 31 December 2003 and the results of its operations and its cash flows for the year then ended in accordance with International Financial Reporting Standards.

19 March 2004
Paris, France

JSC Basisbank Balance Sheet as at 31 December 2003 (in thousands of Georgian Lari)

	Note	2003	2002
Assets			
Cash and cash equivalents	5	7,615	5,679
Mandatory cash balances with theNational Bank of Georgia		1,281	1,051
Trading securities	6	2,189	1,075
Loans and advances to customers	7	7,983	5,747
Investment securities available for sale	8	60	60
Other assets, including tax assets	9	264	13
Premises, equipment and investment property	10	1,305	1,248
Total assets		**20,697**	**14,873**
Liabilities			
Customer accounts	11	11,651	7,263
Other liabilities, including tax liabilities	12	115	136
Total liabilities		**11,766**	**7,399**
Shareholders' equity			
Share capital	13	5,025	5,025
Retained earnings	14	3,906	2,449
Total shareholders' equity		**8,931**	**7,474**
Total liabilities and shareholders' equity		**20,697**	**14,873**

JSC Basisbank Statement of Income for the Year Ended 31 December 2003 (in thousands of Georgian Lari)

	Note	**2003**	**2002**
Interest income	15	1,894	1,748
Interest expense	15	(396)	(217)
Net interest income		**1,498**	**1,531**
Provision for loan impairment	7	(362)	(256)
Net interest income after provision for loan impairment		**1,136**	**1,275**
Gains less losses arising from trading securities	6	576	-
Gains less losses arising from trading in foreign currencies	439	199	
Foreign exchange translation losses less gains		308)	(251)
Fee and commission income	16	569	397
Fee and commission expense	16	(207)	(161)
Other operating income		91	131
Operating income		**2,296**	**1,590**
Operating expenses	17	(649)	(487)
Profit before tax		**1,647**	**1,103**
Income tax expense	18	(190)	(185)
Net profit		**1,457**	**918**

JSC Basisbank Statement of Cash Flows for the Year Ended 31 December 2003 (in thousands of Georgian Lari)

	Note	2003	2002
Cash flows from operating activities			
Interest received		1,880	1,748
Interest paid		(359)	(217)
Income received from transactions in the trading securities		576	-
Fees and commissions received		569	397
Fees and commissions paid		(207)	(161)
Other operating income received		77	131
Operating expenses paid		(513)	(382)
Income tax paid		(183)	(185)
Cash flows from operating activities before changes in operating assets and liabilities		**1,840**	**1,331**
Changes in operating assets and liabilities			
Net increase in mandatory cash balances with the NBG		(230)	(463)
Net increase in loans and advances to customers		(2,584)	(1,961)
Net increase in trading securities		(1,114)	(478)
Net increase in other assets		(172)	(13)
Net increase in customer accounts		4,350	3,680
Net (decrease)/increase in other liabilities		(21)	68
Net cash from operating activities		**2,069**	**2,164**
Cash flows from investing activities			
Acquisition of premises, equipment and investment property		(204)	(542)
Acquisition of intangible assets		(74)	-
Sale of investments available for sale		-	3
Proceeds from disposal of premises, equipment and investment property		14	-
Net cash used in investing activities		**(264)**	**(539)**

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JSC Basisbank Statement of Cash Flows for the Year Ended 31 December 2003 (in thousands of Georgian Lari)

Effect of exchange rate changes on cash and cash equivalents			**131**	**(52)**
Net increase in cash and cash equivalents		**1,936**	**1,573**	
Cash and cash equivalents as at the beginning of the year	5	5,679	4,106	
Cash and cash equivalents as at the end of the year	5	**7,615**	**5,679**	

	Share Capital	Retained Earnings	Total Equity
Balance as at 31 December 2001	**5,025**	**1,531**	**6,556**
Net profit		918	918
Balance as at 31 December 2002	**5,025**	**2,449**	**7,474**
Net profit		1,457	1,457
Balance as at 31 December 2003	**5,025**	**3,906**	**8,931**

1 Principal Activities

JSC Basisbank (the "Bank") was established in November 1993 and received its licence (N173) from the National Bank of Georgia on 4 November 4 1993. The Bank provides retail and corporate banking services in the Republic of Georgia. The Bank's registered office is located at the following address: Ketevan Tsamebuli 1, 0103 Tbilisi, Georgia. The Bank has 3 branches as at 31 December 2003 (2002: 2 branches). The number of the Bank's employees as at 31 December 2003 was 33 (2002: 29).

2 Operating Environment of the Bank

The Republic of Georgia continues to display characteristics of an emerging market. These characteristics include, but are not limited to, the existence of a currency that is not freely convertible in most countries outside of the Republic of Georgia and restrictive currency controls. The tax legislation within the Republic of Georgia is subject to varying interpretations, and changes, which can occur frequently.

There is a considerable degree of uncertainty in the Republic of Georgia surrounding the continued success of domestic economic policy. Furthermore, the recoverability of the Bank's loans and advances extended to domestic clients as well as their financial situation and, consequently, their ability to repay the loans depends on future direction of the economic policy and certain steps, such as diversification of the loan portfolio by economic sectors, regions and types of loans, in order to avoid any potential losses. The future economic direction of the Republic of Georgia is largely dependent upon the effectiveness of economic, financial and monetary measures undertaken by the government, together with tax, legal, regulatory, and political developments.

Moreover, the need for further developments in the bankruptcy laws, the absence of formalised procedures for the registration and enforcement of collateral, and other legal and fiscal impediments contribute to the difficulties experienced by banks currently operating in the Republic of Georgia.

In addition, economic conditions continue to limit the volume of activity in the financial markets. Market quotations may not be reflective of the values for financial instruments, which would be determined in an efficient, active market involving willing buyers and willing sellers. Management has, therefore, used the best available information to adjust market quotations to reflect their best estimate of fair values, where considered necessary.

3 Basis of Preparation

Basis of preparation. These financial statements have been prepared in accordance with International Financial Reporting Standards ("IFRS") issued by the International Accounting Standards Board, including International Accounting Standards ("IAS") issued by the International Accounting Standards Committee and Interpretations issued by the Standing Interpretations Committee. The Bank maintains its accounting records in accordance with banking and accounting regulations of the Republic of Georgia. These financial statements have been prepared from those accounting records and adjusted as necessary in order to comply with IFRS.

These financial statements have been measured in the national currency of the Republic of Georgia, Georgian Lari ("GEL").

The preparation of these financial statements requires the use of estimates and assumptions that effect the reported amounts of assets and liabilities, disclosure of contingent assets and liabilities as at the date of the financial statements, and the reported amounts of revenues and expenses during the reported period. Although these estimates are based on Management's best knowledge of current events and actions, actual results ultimately may differ from those estimates.

Where necessary, corresponding figures have been adjusted to conform with changes in the presentation of the current year. Accrued interest income and accrued interest expense previously disclosed along with other assets and other liabilities, respectively, are presented within the related balance sheet items in these financial statements.

4 Significant Accounting Policies

Cash and cash equivalents. Cash and cash equivalents are items, which can be converted into cash within a day. All short term interbank placements, beyond overnight placements, are included in due from other banks. Amounts, which relate to funds that are of a restricted nature, are excluded from cash and cash equivalents.

Mandatory cash balances with the National Bank of Georgia. Mandatory cash balances with the NBG represent mandatory reserve deposits, which are not available to finance the Bank's day to day operations, and hence are not considered as part of cash and cash equivalents for the purposes of the cash flow statement.

Trading securities. Trading securities are securities, which are either acquired for generating a profit from short-term fluctuations in price or trader's margin, or are securities included in a portfolio, in which a pattern of short-term trading exists. The Bank classifies securities into trading securities if it has the intention to sell them within a short period after purchase, i.e. within 1 to 6 months.

Trading securities are initially recorded at cost (which includes transaction costs) and subsequently remeasured at fair value based on their market value or after the application of various valuation methodologies, including assumptions as to the future realisability of these securities. In determining market value, all trading securities are valued at the last trade price if quoted on an exchange or, if traded over-the-counter, at the last bid price.

All related realized and unrealised gains and losses are recorded within gains less losses arising from trading securities in the statement of income in the period in which the change occurs. Interest earned on trading securities is reflected in the statement of income as interest income on trading securities. Dividends received are included in dividend income within other operating income.

All purchases and sales of trading securities that require delivery within the time frame established by regulation or market convention (“regular way” purchases and sales) are recorded at trade date, which is the date that the Bank commits to purchase or sell the asset. Otherwise such transactions are treated as derivative instruments until settlement occurs.

Originated loans and advances and provisions for loan impairment. Loans originated by the Bank by providing money directly to the borrower or to a sub-participation agent at draw down, other than those that are originated with the intent of being sold immediately or in the short-term, which are recorded as trading assets, are categorised as originated loans.

Originated loans and advances are recorded when cash is advanced to borrowers. Initially, originated loans and advances are recorded at cost, which is the fair value of the consideration given, and subsequently are carried at amortised cost less provision for loan impairment. Amortised cost is based on the fair value of cash consideration given to originate those loans determinable by reference to market prices at origination date.

Loans originated at interest rates different from market rates are remeasured at origination to their fair value, being future interest payments and principal repayment(s) discounted at market interest rates for similar loans. The difference between the fair value and the nominal value at origination is credited or charged to the statement of income as gains on origination of assets at rates above market or losses on origination of assets at rates below market. Subsequently, the carrying amount of such loans is adjusted for amortization of the gains/losses on origination and the related income is recorded as interest income within the statement of income using the effective yield method.

A credit risk provision for loan impairment is established if there is objective evidence that the Bank will not be able to collect the amounts due according to original contractual terms. The amount of the provision is the difference between the carrying amount and estimated recoverable amount, calculated as the present value of expected cash flows, including amounts recoverable from guarantees and collateral, discounted at the instrument's original effective interest rate.

The provision for loan impairment also covers losses where there is objective evidence that probable losses are present in components of the loan portfolio at the balance sheet date. These have been estimated based upon historical patterns of losses in each component, the credit ratings assigned to the borrowers and reflect the current economic environment in which the borrowers operate.

When a loan is uncollectable, it is written off against the related provision for loan impairment. Such loans are written off after all the necessary procedures have been completed and the amount of the loss has been determined. Subsequent recoveries of amounts previously written off are credited to the provision for loan impairment in the statement of income.

If the amount of the provision for loan impairment subsequently decreases due to an event occurring after the write-down, the release of the provision is credited to the provision for loan impairment in the statement of income.

The Bank does not enter into transactions for purchases of loans with third parties.

Other credit related commitments. In the normal course of business, the Bank enters into other credit related commitments including letters of credit and guarantees. Specific provisions are recorded against other credit related commitments when losses are considered probable.

Investment securities available for sale. This classification includes investment securities which Management intends to hold for an indefinite period of time, that may be sold in response to needs for liquidity or changes in interest rates, exchange rates or equity prices. Management determines the appropriate classification of its investment securities at the time of purchase.

Investment securities available for sale are initially recorded at cost (which includes transaction costs) and subsequently remeasured to fair value based on quoted bid prices. Certain investment securities available for sale for which there is no available external independent quotation have been fair valued by Management on the basis of results of recent sales of equity interests in the investees between unrelated third parties, consideration of other relevant information such as discounted cash flows and financial data of the investees and application of other valuation methodologies.

Unrealised gains and losses arising from changes in the fair value of investment securities available for sale are recorded in the statement of income in the period in which they arise.

When the investment securities available for sale are disposed of, the related accumulated fair value adjustments are included in the statement of income as gains less losses arising from investment securities available for sale. Impairment and reversal of impairment of investment securities available for sale is recorded through the statement of income. An investment security available for sale is impaired if its carrying amount is greater than its estimated recoverable amount. The recoverable amount is the present value of expected future cash flows discounted at the current market rate of interest for a similar financial asset. Interest earned on investment securities available for sale is reflected in the statement of income as interest income on investment securities available for sale. Dividends received are included in dividend income within the statement of income.

All regular way purchases and sales of investment securities available for sale are recorded at trade date, which is the date that the Bank commits to purchase or sell the asset. All other purchases and sales are recorded as derivative forward transactions until settlement.

Premises and equipment. Premises and equipment are stated at cost less accumulated depreciation and provision for impairment, where required.

Construction in progress is carried at cost less provision for impairment where required. Upon completion, assets are transferred to premises and equipment at their carrying amount. Construction in progress is not depreciated until the asset is available for use.

At each reporting date the Bank assesses whether there is any indication of impairment of premises and equipment. If any such indication exists, the Bank estimates the recoverable amount, which is determined as the higher of an asset's net selling price or its value in use. Where the carrying amount of an asset is greater than its estimated recoverable amount, it is written down to its recoverable amount and the difference is charged to the statement of income. An impairment loss recorded for an asset in prior years is reversed if there has been a change in the estimates used to determine the assets recoverable amount.

Gains and losses on disposal of premises and equipment are determined by reference to their carrying amount and are taken into account in determining profit/(loss). Repairs and maintenance are charged to the statement of income when the expenditure is incurred.

Depreciation. Depreciation is applied on a straight line basis over the estimated useful lives of the assets using the following rates:

Buildings	2%
Furniture, fixture and other office equipment	10-20%
Computers and communication equipment	20%
Vehicles	20%

Investment property. Property held for long-term rental yields or capital appreciation purposes, which is not occupied by the Bank is classified as investment property.

Investment property comprises buildings. Investment property is carried at cost less accumulated depreciation and provision for impairment, if any. If an investment property becomes owner occupied, it is reclassified as premises and equipment and its carrying value at the date of reclassification becomes its cost for accounting purposes of subsequent recording.

Accrued interest income and accrued interest expense. Accrued interest income and accrued interest expense, including both accrued coupon and amortised discount, are included in the carrying values of related balance sheet items.

Income taxes. Taxation has been provided for in the financial statements in accordance with the legislation of the Republic of Georgia currently in force. Income tax expense in the statement of income for the year comprises current tax and changes in deferred tax. Current tax is calculated on the basis of the expected taxable profit for the year, using the tax rates enacted at the balance sheet date. Taxes, other than on income, are recorded within operating expenses.

Deferred income tax is provided, using the balance sheet asset and liability method, for all temporary differences arising between the tax basis of assets and liabilities and their carrying amounts for financial reporting purposes. Deferred tax assets are recorded to the extent that it is probable that future taxable profit will be available, against which the temporary differences can be utilised. Deferred tax assets and liabilities are measured at tax rates that are expected to apply to the period when the asset is realised or the liability is settled, based on tax rates that have been enacted or substantively enacted at the balance sheet date.

Income and expense recognition. Interest income and expense are recorded in the income statement for all interest bearing instruments on an accrual basis, using the effective yield method based on the actual purchase price. Interest income includes coupons earned on fixed income investment and trading securities and accrued discount and premium on treasury bills and other discounted instruments. When loans become doubtful of collection, they are written down to their recoverable amounts and interest is thereafter recorded based on the rate of interest that was used to discount the future cash flows for the purpose of measuring the recoverable amount.

Fees, commissions and other income and expense items are generally recorded on an accrual basis when the service has been provided. Loan origination fees for loans, which are probable of being drawn down, are deferred (together with related direct costs) and recorded as an adjustment to the effective yield on the loan. Commissions and fees arising from negotiating, or participating in the negotiation of a transaction for a third party, such as the acquisition of loans, shares or other securities or the purchase or sale of businesses, are recorded on completion of the underlying transaction. Portfolio and other management advisory and service fees are recorded based on the applicable service contracts.

JSC Basisbank Notes to the Financial Statements 31 December 2003 (in thousands of Georgian Lari)

Foreign currency translation. Transactions denominated in foreign currency are recorded at the exchange rate ruling on the transaction date. Exchange differences resulting from the settlement of transactions denominated in foreign currency are included in the statement of operations using the exchange rate ruling on that date.

Monetary assets and liabilities denominated in foreign currency are translated into GEL at the official exchange rate of the NBG at the balance sheet date. Foreign currency gains and losses arising from the translation of monetary assets and liabilities are reflected in the statement of income as foreign currency translation gains less losses. As at 31 December 2003, the principal rate of exchange used for translating foreign currency balances was USD 1 = 2.075 Georgian Lari and EUR 1 = 2.592 Georgian Lari (2002: USD 1 = 2.09 Georgian Lari and EUR 1 = 2.1763 Georgian Lari).

Offsetting. Financial assets and liabilities are offset and the net amount reported in the balance sheet only when there is a legally enforceable right to offset the recognised amounts, and there is an intention to either settle on a net basis, or to realise the asset and settle the liability simultaneously.

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

Staff costs related contributions. The Bank's contributions to the state pension and social insurance funds of the Republic of Georgia in respect of its employees are expensed as incurred and included into staff costs.

5 Cash and Cash Equivalents

	2003	**2002**
Cash on hand	1,908	1,497
Correspondent accounts with the NBG	452	231
Correspondent accounts and overnight placements with other banks		
- Republic of Georgia	167	48
- Other countries	5,088	3,903
Total cash and cash equivalents	**7,615**	**5,679**

Geographical, currency and interest rate analyses of cash and cash equivalents are disclosed in Note 19.

JSC Basisbank Notes to the Financial Statements 31 December 2003 (in thousands of Georgian Lari)

6 Trading Securities

	2003	2002
Treasury bills of the Ministry of Finance of the Republic of Georgia	2,185	1,075
Corporate shares	4	-
Total trading securities	**2,189**	**1,075**

Treasury bills are short term (from 1 to 6 months) treasury bills issued by the Ministry of Finance of the Republic of Georgia. Treasury bills are freely tradable in the Georgian Securities Market. Treasury bills outstanding as at 31 December 2003 mature between January 2004 and April 2004 and have an average yield to maturity of 19%.
As at 31 December 2003 the estimated fair value of trading securities was GEL 2,189 thousand (2002: GEL 1,075 thousand).
Geographical, currency and interest rate analyses of trading securities are disclosed in Note 19.

7 Loans and Advances to Customers

	2003	2002
Current loans	7,644	5,991
Overdue loans	1,008	88
Accrued interest income	35	21
Less: Provision for loan impairment	(704)	(353)
Total loans and advances to customers	**7,983**	**5,747**

Loans more than one day overdue according to their contractual maturity dates are classified as “overdue loans”.
Movements in the provision for loan impairment are, as follows:

	2003	2002
Provision for loan impairment as at 1 January	**353**	**239**
Provision for loan impairment during the year	362	256
Loans written off during the year as uncollectible	(88)	(142)
Recovery of loans previously written off as uncollectible	77	-
Provision for loan impairment as at 31 December	**704**	**353**

JSC Basisbank Notes to the Financial Statements 31 December 2003 (in thousands of Georgian Lari)

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

	2003		2002	
	Amount	**%**	**Amount**	**%**
Trade	3,635	42%	2,757	45%
Manufacturing	1,753	20%	1,392	23%
Construction	1,320	15%	717	12%
Consumer loans	788	9%	546	9%
Transport and Communication	221	3%	139	2%
Energy	103	1%	45	1%
Agriculture	85	1%	155	3%
Other	782	9%	349	5%
Total loans and advances to customers (gross amount)	**8,687**	**100%**	**6,100**	**100%**

As at 31 December 2003 the estimated fair value of loans and advances to customers was GEL 7,983 thousand (GEL 5,747 thousand). Geographical, currency, maturity and interest rate analyses of loans and advances to customers are disclosed in Note 19.

8 Investment Securities Available for Sale

As at 31 December 2003 investment securities available for sale are comprised of the following equity securities:

Company name	**Nature of business**	**Country of registration**	**2003**		**2002**	
			Amount	**%**	**Amount**	**%**
Basis LLC	Brokerage	Republic of Georgia	60	100	60	100
Total			**60**		**60**	

JSC Basisbank Notes to the Financial Statements 31 December 2003 (in thousands of Georgian Lari)

9 Other Assets, Including Tax Assets

	2003	2002
Fixed asset prepayments	143	-
Purchased computer software	72	1
Income tax prepayments	13	3
Deferred tax asset	-	1
Other	36	8
Total other assets	**264**	**13**

Purchased computer software is stated net of accumulated amortisation of GEL 2 thousand (2002: nil)
Geographical, currency and maturity analyses of other assets are disclosed in Note 19.

10 Premises, Equipment and Investment Property

	Investment property	Premises	Computers and communication equipment	Furniture, fixtures and others	Motor vehicles	Total
Net book amount as at 31 December 2002	**58**	**978**	**74**	**92**	**46**	**1,248**
Cost						
Opening balance	118	1,002	111	116	73	1,420
Transfers	-	-	10	(10)	-	-
Additions	114	-	39	24	27	204
Disposals	(39)	-	(1)	-	(30)	(70)
Closing balance	**193**	**1,002**	**159**	**130**	**70**	**1,554**
Accumulated depreciation						
Opening balance	60	24	37	24	27	172
Depreciation charge	56	20	27	17	14	134
Disposals	(39)	-	(1)	-	(17)	(57)
Closing balance	**77**	**44**	**63**	**41**	**24**	**249**

JSC Basisbank Notes to the Financial Statements 31 December 2003 (in thousands of Georgian Lari)

Net book amount as at 31 December 2003	**116**	**958**	**96**	**89**	**46**	**1,305**

Investment property comprises buildings, which are kept for capital appreciation purposes.

11 Customer Accounts

	2003	2002
Current accounts, including		
- corporate customers	2,982	3,352
- individuals	4,091	1,483
Deposits and savings accounts, including		
- corporate customers	55	435
- individuals	3,968	1,971
Accrued interest expense	59	22
Total customer accounts	**11,651**	**7,263**

Economic sector risk concentrations within customer accounts are, as follows:

	2003	%	2002	%
Individuals	8,118	70%	3,476	48%
Trade and services	1,776	15%	1,864	26%
Mining	573	5%	624	9%
Other	1,184	10%	1,299	17%
Total customer accounts	**11,651**	**100%**	**7,263**	**100%**

As at 31 December 2003 the estimated fair value of customer accounts was GEL 11,651 thousand (2002: GEL 7,263 thousand).
Geographical, currency, maturity and interest rate analyses of customer accounts are disclosed in Note 19.

JSC Basisbank Notes to the Financial Statements 31 December 2003 (in thousands of Georgian Lari)

12 Other Liabilities, Including Tax Liabilities

	2003	2002
Provisions for guarantees issued	41	57
Deferred tax liability	15	-
Other liabilities	59	79
Total other liabilities	**115**	**136**

Movements in provisions for guarantees are, as follows:

	2003	2002
Provision for guarantees issued as at 1 January	57	42
Additional provisions made during the year	59	15
Amounts used during the period	(75)	-
Provision for guarantees issued as at 31 December	**41**	**57**

Geographical, currency and maturity analyses of other liabilities are disclosed in Note 19.

13 Share Capital

The total number of authorised ordinary shares at year-end was 5,025 thousand shares (2002: 5,025 thousand shares) with a par value of GEL 1 per share (2002: GEL 1 per share). The Bank's capital was built-up as follows: GEL 22 thousand in kind and GEL 5,023 thousand in cash. All issued shares are fully paid. There are no preference shares in the share capital of the Bank.

14 Retained Earnings

In accordance with Georgian legislation, the Bank allocates profits as dividends or transfers them to reserves (fund accounts) on the basis of statutory accounting reports, prepared in accordance with Georgian accounting rules. The Bank's reserves under Georgian accounting rules as at 31 December 2003 are GEL 3,843 thousand (2002: GEL 2,455 thousand).

JSC Basisbank Notes to the Financial Statements 31 December 2003 (in thousands of Georgian Lari)

15 Interest Income and Expense

	2003	2002
Interest income		
Loans and advances to customers	1,525	1,324
Trading securities	271	360
Due from other banks	78	64
Correspondent accounts with other banks	20	-
Total interest income	**1,894**	**1,748**
Interest expense		
Customer accounts	(396)	(217)
Total interest expense	**(396)**	**(217)**
Net interest income	**1,498**	**1,531**

16 Fee and Commission Income and Expense

	2003	2002
Fee and commission income		
Cash transactions	516	362
Other	53	35
Total fee and commission income	**569**	**397**
Fee and commission expense		
Cash transactions	(123)	(86)
Other	(84)	(75)
Total fee and commission expense	**(207)**	**(161)**

JSC Basisbank Notes to the Financial Statements 31 December 2003 (in thousands of Georgian Lari)

17 Operating Expenses

	Note	2003	2002
Administrative expenses		210	171
Depreciation and amortisation	10	136	91
Staff costs		112	97
Security		71	61
State and local taxes		58	52
(Recovery of)/provisions for guarantees issued	12	(16)	15
Other		78	-
Total operating expenses		**649**	**487**

Staff costs include:

	2003	2002
Wages and salaries	68	59
Social security costs	44	38
Total staff costs	**112**	**97**

18 Income Taxes

	2003	2002
Current tax charge	174	175
Deferred taxation movement due to:		
- Origination and reversal of temporary differences	16	10
Income tax expense for the year	**190**	**185**

Income tax rate in the Republic of Georgia is 20%. Interest income on government treasury bonds is taxable at 10%. Trading income on government treasury bonds is not assessable for income tax purposes.
A reconciliation between the expected and the actual taxation charge is provided below.

	2003	2002
IFRS profit before taxation	**1,648**	**1,103**

JSC Basisbank Notes to the Financial Statements 31 December 2003 (in thousands of Georgian Lari)

Theoretical tax charge at the applicable statutory rate (2003: 20%; 2002: 20%)	330	221
Tax effect of income not assessable for tax purposes (trading profit on treasury bills)	(115)	-
Tax effect of income taxable at 10% (interest income on treasury bills)	(27)	(36)
Tax effect of non deductible expenses	2	-
Income tax expense for the year	**190**	**185**

Differences between IFRS and the Georgian statutory taxation regulations give rise to certain temporary differences between the carrying amount of certain assets and liabilities for financial reporting purposes and for income tax calculation purposes. The tax effect of the movement on these temporary differences is recorded at the rate of 20% (2002: 20%), except for interest income on state treasury bills, which is taxed at 10% (2002: 10%).

	2002	**Movement**	**2003**
Tax effect of deductible temporary differences			
Additional loans impairment provision	7	(7)	-
Accruals	6	-	6
Gross deferred tax asset	**13**	**(7)**	**6**
Tax effect of taxable temporary differences			
Additional depreciation on premises and equipment	12	9	21
Gross deferred tax liability	**12**	**9**	**21**
Total net deferred tax asset/(liability)	**1**	**(16)**	**(15)**

	2001	**Movement**	**2002**
Tax effect of deductible temporary differences			
Impairment losses on loans	6	1	7
Accrued expenses	8	(2)	6
Gross deferred tax asset	**14**	**(1)**	**13**

Tax effect of taxable temporary differences			
Premises and equipment (different depreciation rates)	3	9	12
Gross deferred tax liability	**3**	**9**	**12**
Total net deferred tax (liability)/asset	**11**	**(10)**	**1**

19 Financial Risk Management

The risk management function within the Bank is carried out in respect of financial risks (credit, market, geographical, currency, liquidity and interest rate), operational risks and legal risks. The primary objectives of the financial risk management function are to establish risk limits, and then ensure that exposure to risks stays within these limits. Risk assessment also forms the basis for optimal risk-adjusted capital allocation, transaction pricing and performance assessment. The operational and legal risk management functions are intended to ensure proper functioning of internal policies and procedures to minimize operational and legal risks.

Credit risk. The Bank takes on exposure to credit risk, which is the risk that 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 geographical and industry segments. Such risks are monitored on a revolving basis and subject to an annual or more frequent review. Limits on the level of credit risk by product, borrower and industry sector are approved regularly by the Management Board and Credit Committee.

The exposure to any one borrower is further restricted by sub-limits covering on and off-balance sheet exposures and daily delivery risk limits in relation to trading items. Actual exposures against limits are monitored daily.

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.

The Bank's maximum exposure to credit risk is primary reflected in the carrying amounts of financial assets on the balance sheet. The impact of possible netting of assets and liabilities to reduce potential credit exposure is not significant.

Credit risk for off-balance sheet financial instruments is defined as the possibility of sustaining a loss as a result of another party to a financial instrument failing to perform in accordance with the terms of the contract. The Bank uses the same credit policies in making conditional obligations as it does for on-balance sheet financial instruments through established credit approvals, risk control limits and monitoring procedures.

Market risk. The Bank takes on exposure to market risks. Market risks arise from open positions in interest rate, currency and equity products, all of which are exposed to general and specific market movements. The Management Board sets limits on the value of risk that may be accepted, which is monitored on a daily basis. However, the use of this approach does not prevent losses outside of these limits in the event of more significant market movements.

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Geographical risk. The geographical concentration of the Bank's assets and liabilities as at 31 December 2003 is set out below:

	Georgia	CIS	Non CIS	Total
Assets				
Cash and cash equivalents	2,378	354	4,883	7,615
Mandatory cash balances with the NBG	1,281	-	-	1,281
Trading securities	2,187	-	2	2,189
Loans and advances to customers	7,983	-	-	7,983
Investment securities available for sale	60	-	-	60
Other assets, including tax assets	229	-	35	264
Premises, equipment and investment property	1,305	-	-	1,305
Total assets	**15,423**	**354**	**4,920**	**20,697**
Liabilities				
Customer accounts	10,303	62	1,286	11,651
Other liabilities, including tax liabilities	110	5	-	115
Total liabilities	**10,413**	**67**	**1,286**	**11,766**
Net balance sheet position	**5,010**	**287**	**3,634**	**8,931**

The geographical concentration of the Bank's assets and liabilities as at 31 December 2002 is set out below:

	Georgia	CIS	Non CIS	Total
Net balance sheet position	**3,673**	**123**	**3,678**	**7,474**

Currency risk. The Bank takes on exposure to effects of fluctuations in the prevailing foreign currency exchange rates on its financial position and cash flows. The table below summarises the Bank's exposure to foreign currency exchange rate risk as at 31 December 2003. Included in the table are the Bank's assets and liabilities at their carrying amounts, categorised by currency. Foreign exchange denominated assets and liabilities give rise to foreign exchange exposure:

	GEL	USD	Other currencies	Total
Assets				
Cash and cash equivalents	682	5,557	1,376	7,615
Mandatory cash balances with the NBG	1,148	133	-	1,281
Trading securities	2,187	2	-	2,189
Loans and advances to customers	314	7,493	176	7,983
Investment securities available for sale	60	-	-	60
Other assets, including tax assets	257	6	1	264
Premises, equipment and investment property	1,305	-	-	1,305

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Total assets	**5,953**	**13,191**	**1,553**	**20,697**
Liabilities				
Customer accounts	1,171	9,284	1,196	11,651
Other liabilities, including tax liabilities	41	69	5	115
Total liabilities	**1,212**	**9,353**	**1,201**	**11,766**
Net balance sheet position	**4,741**	**3,838**	**352**	**8,931**

The Bank is required to maintain its foreign currency position within the limits set by the NBG.
As at 31 December 2002, the Bank had the following positions in currency

	GEL	USD	Other currencies	Total
Net balance sheet position	**2,870**	**4,433**	**171**	**7,474**

The Bank has extended loans and advances denominated in foreign currencies. Depending on the revenue stream of the borrower, the appreciation of the currencies against the Georgian Lari may adversely affect the borrowers' repayment ability and therefore increases the likelihood of future loan losses.

Liquidity risk. Liquidity risk is defined as the risk when the maturity of assets and liabilities does not match. The Bank is exposed to daily calls on its available cash resources from current accounts and loan draw downs. The Bank does not maintain cash resources to meet all of these needs as experience shows that a minimum level of reinvestment of maturing funds can be predicted with a high level of certainty. The liquidity risk is managed by the Asset and Liability Committee of the Bank.

The table below shows assets and liabilities as at 31 December 2003 by their remaining contractual maturity. Some of the assets, however, may be of a longer term nature; for example, loans are frequently renewed and, accordingly, short term loans can have a longer term duration.

The liquidity position of the Bank as at 31 December 2003 is set out below.

	Demand and less than 1 month	From 1to 3 months	From 3 to 12 months	More than 1 year	Overdue/ No stated maturity	Total
Assets						
Cash and cash equivalents	7,615	-	-	-	-	7,615
Mandatory cash balances with the NBG	1,281	-	-	-	-	1,281
Trading securities	324	1,427	434	4	-	2,189
Loans and advances to customers	1,280	1,542	2,263	2,898	-	7,983
Investment securities available for sale	-	-	-	-	60	60
Other assets, including tax assets	180	-	-	13	72	264
Premises, equipment and investment property	-	-	-	-	1,305	1,305
Total assets	**10,679**	**2,969**	**2,697**	**2,915**	**1,437**	**20,697**

JSC Basisbank Notes to the Financial Statements 31 December 2003 (in thousands of Georgian Lari)

Liabilities						
Customer accounts	7,749	1,168	2,313	421	-	11,651
Other liabilities, including tax liabilities	115	-	-	-	-	115
Total liabilities	**7,864**	**1,168**	**2,313**	**421**	**-**	**11,766**
Net liquidity gap	**2,815**	**1,801**	**384**	**2,494**	**1,437**	**8,931**
Cumulative liquidity gap as at 31 December 2003		**2,815**	**4,616**	**5,000**	**7,494**	**8,931**
Cumulative liquidity gap as at 31 December 2002		**2,931**	**2,981**	**4,509**	**6,224**	**7,474**

Mandatory cash balances with the NBG are included within demand and less than one month as the majority of liabilities to which this balance relates to are also included within this category.

The matching and/or 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 an uncertain term and of different types. An unmatched position potentially enhances profitability, but can also increase the risk of losses. The maturities of assets and liabilities and the ability to replace, at an acceptable cost, interest-bearing liabilities as they mature, are important factors in assessing the liquidity of the Bank and its exposure to changes in interest and exchange rates.

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

The Bank is exposed to interest rate risk, principally as a result of lending at fixed interest rates, in amounts and for periods, which differ from those of term borrowings at fixed interest rates. In practice, interest rates are generally fixed on a short-term basis. Also, interest rates that are contractually fixed on both assets and liabilities are usually renegotiated to reflect current market conditions.

The Management Board sets limits on the level of mismatch of interest rate repricing that may be undertaken, which is monitored daily. In the absence of any available hedging instruments, the Bank normally seeks to match its interest rate positions.

The table below summarises the Bank's exposure to interest rate risk. Included in the table are the Bank's assets and liabilities at carrying amounts, categorised by the earlier of contractual repricing or maturity dates.

	Demand and less than 1 month	From 1to 3 months	From 3 to 12 months	More than 1 year	Non-interest bearing	Total
Assets						
Cash and cash equivalents	-	-	-	-	7,615	7,615
Mandatory cash balances with the NBG	1,281	-	-	-	-	1,281
Trading securities 324	1,427	434	-	4	2,189	

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Loans and advances to customers	1,280	1,542	2,263	2,898	-	7,983
Investment securities available for sale	-	-	-	-	60	60
Other assets, including tax assets	-	-	-	-	264	264
Premises, equipment and investment property	-	-	-	-	1,305	1,305
Total assets	**2,885**	**2,969**	**2,697**	**2,898**	**9,248**	**20,697**
Liabilities						
Customer accounts	676	1,168	2,313	421	7,073	11,651
Other liabilities, including tax liabilities	-	-	-	-	115	115
Total liabilities	**676**	**1,168**	**2,313**	**421**	**7,188**	**11,766**
Net liquidity gap	**2,209**	**1,801**	**384**	**2,477**	**2,095**	**8,931**
Cumulative sensitivity gap as at 31 December 2003		**2,209**	**4,010**	**4,394**	**6,871**	**8,931**
Cumulative sensitivity gap as at 31 December 2002		**1,267**	**1,319**	**2,847**	**4,562**	**7,474**

The table below summarises the effective interest rates by major currencies for major monetary financial instruments. The analysis has been prepared using period-end effective contractual rates.

	2003			**2002**		
	USD	**GEL**	**Other currencies**	**USD**	**GEL**	**Other currencies**
Assets						
Mandatory cash balances with the NBG	2%	6%	-	1.5%	4.5%	-
Trading securities	-	49%	-	-	15%	-
Loans and advances to customers	21%	21%	17%	22%	20%	-
Liabilities						
Customer accounts	8%	7%	8%	9%	7%	10%

The sign "-" in the table above means that the Bank does not have the respective assets or liabilities in corresponding currency.

JSC Basisbank Notes to the Financial Statements 31 December 2003 (in thousands of Georgian Lari)

20 Contingencies, Commitments and Derivative Financial Instruments

Legal proceedings. From time to time and in the normal course of business, claims against the Bank are received. On the basis of own estimates and internal and external professional advice the Management is of the opinion that no material losses will be incurred and, accordingly, no provision has been made in these financial statements.

Tax legislation. Due to the presence in Georgian commercial legislation, and tax legislation in particular, of provisions allowing more than one interpretation, and also due to the practice developed in a generally unstable environment by the tax authorities of making arbitrary judgement of business activities, Management's judgement of the Bank's business activities may not coincide with the interpretation of the same activities by tax authorities.

The tax consequence of transactions for Georgian taxation purposes is frequently determined by the form, in which transactions are documented and the underlying accounting treatment prescribed by Georgian Accounting Rules. Accordingly, the Bank structures certain transactions so as to take advantage of such form driven determinations to reduce the overall effective tax rate of the Bank. The statement of income as presented in these financial statements includes reclassifications to reflect the underlying economic substance of those transactions. The effect of these reclassifications does not have an effect on the Bank's profit before taxation or the tax charge recorded in these financial statements.

The Bank's Management is confident that this ongoing restructuring of taxable income and deductible expenses is unlikely to result in additional tax liabilities. Accordingly, no provision for a potential tax liability, with regard to these transactions, has been recorded in the financial statements.

If a particular treatment was to be challenged by the tax authorities, the Bank may be assessed additional taxes, penalties and interest, which can be significant. Tax years remain open to review by the tax authorities for three years.

Capital commitments. As at 31 December 2003 the Bank had no significant capital commitments.

Credit related commitments. Outstanding credit related commitments are as follows:

	2003	**2002**
Unused credit lines	2,236	2,900
Guarantees issued	743	941
Total credit related commitments	**2,979**	**3,841**

The Bank makes commitment to grant loans to certain customers at a specified rate and during the fixed period of time. The Bank retains the right to refuse borrower to withdraw unused portion of loan if the borrower fails to perform certain conditions set out in the contracts.

The sources of funding of letter of guarantees issued by the Bank mainly are the credit lines granted to the same customers. Thereby the criteria of assessing the credit risk of commitments given is same as for loans. Blocked deposits and third party guarantees also serve as a collateral.

Derivative Financial Instruments. The Bank did not have any balances related to transactions in the derivative financial instruments either as at 31 December 2003 or 2002.

21 Fair Value of Financial Instruments

Fair value is the amount, at which a financial instrument could be exchanged in a current transaction between willing parties, other than in a forced sale or liquidation, and is best evidenced by a quoted market price.
The estimated fair values of financial instruments have been determined by the Bank using available market information, where it exists, and appropriate valuation methodologies. However, judgement is necessarily required to interpret market data to determine the estimated fair value. As described in more detail in Note 2, the Republic of Georgia continues to display some characteristics of an emerging market and economic conditions continue to limit the volume of activity in the financial markets. While Management has used available market information in estimating the fair value of financial instruments, the market information may not be fully reflective of the value that could be realised in the current circumstances.
While Management has used available market information in estimating the fair value of financial instruments, the market information may not be fully reflective of the value that could be realised in the current circumstances.
Financial instruments carried at fair value. Cash and cash equivalents, trading securities and investment securities available for sale are carried on the balance sheet at their fair value. As set out in Note 8, external independent market quotations were not available for certain investment securities available for sale. The fair value of these assets was determined by Management on the basis of results of recent sales of equity interests in the investees between unrelated third parties, consideration of other relevant information such as discounted cash flows and financial data of the investees and application of other valuation methodologies.
Loans originated carried at amortised cost less provision for impairment. The fair value of floating rate instruments is their carrying amount. The estimated fair value of fixed interest rate instruments is based on estimated future cash flows expected to be received discounted at current interest rates for new instruments with similar credit risk and remaining maturity. Refer to Note 7 for the estimated fair value of loans and advances to customers.
Liabilities carried at amortised cost. The fair value of instruments with a quoted market price is based on quoted market prices. The estimated fair value of instruments with no stated maturity is the amount repayable on demand. The estimated fair value of fixed interest rate instruments without a quoted market price is based on expected cash flows discounted at current interest rates for new instruments with similar credit risk and remaining maturity. Refer to Note 11 for the estimated fair value of customer accounts.

22 Related Party Transactions

For the purposes of these financial statements, 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 as defined by IAS 24 “Related Party Disclosures”. In considering each possible related party relationship, attention is directed to the substance of the relationship, not merely the legal form.
Banking transactions are entered into in the normal course of business with significant shareholders, directors, companies with which the Bank has significant shareholders in common and other related parties. These transactions include settlements, loans, deposit taking, guarantees, trade finance and foreign currency transactions. These transactions are priced predominantly at market rates. The outstanding balances at the year end and income and expense items for the year with related parties are, as follows:

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	2003	2002
Loans to related companies		
Loans outstanding at the year end		
(contractual interest rate: 2003: 18%-20%; 2002: 18%-20%)	521	586
Interest income for the year	116	98

In 2003 the total remuneration of members of the Board of Directors, including pension contributions, and discretionary compensation amounts to GEL 16 thousand (2002: GEL 16 thousand)