Grant Thornton

Financial Statements and Independent Auditor's Report

"Prometey Bank" limited liability company

31 December 2012

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Statement of comprehensive income

In thousand Armenian drams	Notes	**Year ended December 31, 2012**	Year ended December 31, 2011
Interest and similar income	6	**4,571,429**	3,432,633
Interest and similar expense	6	**(1,657,330)**	(984,748)
Net interest income		**2,914,099**	2,447,885
Fee and commission income	7	**206,213**	162,694
Fee and commission expense	7	**(153,959)**	(177,752)
Net fee and commission income		**52,254**	(15,058)
Net trading income	8	**458,860**	488,318
Gains less losses on investments available for sale		**35,882**	5,447
Other income	9	**142,973**	82,235
Impairment charge for credit losses	10	**(65,881)**	(262,657)
Staff costs	11	**(958,727)**	(687,718)
Depreciation of property and equipment	20	**(142,729)**	(129,974)
Amortization of intangible assets	21	**(8,157)**	(7,989)
Other expenses	12	**(513,902)**	(456,027)
Profit before income tax		**1,914,672**	1,464,462
Income tax expense	13	**(411,916)**	(307,298)
Profit for the year		**1,502,756**	1,157,164
Other comprehensive income:			
Net unrealized gains/(losses) from changes in fair value		**(30,194)**	125,669
Net gains realized to net profit on disposal of available-for-sale instruments		**(21,206)**	(7,401)
Income tax relating to components of other comprehensive income		**10,280**	(23,653)
Other comprehensive income for the year, net of tax		**(41,120)**	94,615
Total comprehensive income for the year		**1,461,636**	1,251,779

The accompanying notes on pages 8 to 53 are an integral part of these financial statements.

Statement of financial position

In thousand Armenian drams	Notes	As of December 31, 2012	As of December 31, 2011
ASSETS			
Cash and balances with CBA	14	**12,203,920**	6,470,118
Trading securities	15	**-**	759,718
Amounts due from other financial institutions	16	**4,635,188**	1,885,764
Derivative financial assets	17	**965**	1,627
Loans and advances to customers	18	**28,654,441**	25,544,487
Investments available for sale	19	**592,086**	2,142,147
Investments held to maturity	19	**203,433**	487,199
Securities pledged under repurchase agreements	29	**5,333,454**	1,453,378
Property, plant and equipment	20	**1,862,120**	1,714,530
Intangible assets	21	**36,368**	41,375
Assets held for sale	23	**1,707,242**	153,127
Other assets	22	**138,868**	176,467
TOTAL ASSETS		**55,368,085**	40,829,937
LIABILITIES AND EQUITY			
Liabilities			
Amounts due to the CBA	24	**8,830,551**	4,647,273
Amounts due to financial institutions	25	**240,448**	770,693
Amounts due to customers	26	**20,545,822**	11,411,425
Securities issued	27	**5,081,903**	4,849,906
Derivative financial liabilities	17	**595**	642
Current income tax liabilities		**162,177**	198,131
Deferred income tax liabilities	13	**9,842**	27,928
Other liabilities	28	**266,247**	155,075
Total liabilities		**35,137,585**	22,061,073
Equity			
Charter capital	30	**14,400,000**	14,400,000
Statutory general reserve		**52,075**	52,075
Other reserves		**69,136**	110,256
Retained earnings		**5,709,289**	4,206,533
Total equity		**20,230,500**	18,768,864
TOTAL LIABILITIES AND EQUITY		**55,368,085**	40,829,937

The financial statements from pages 3 to 53 were signed by the Bank's Chairman of the Executive Board and Chief Accountant on 17 April 2013. The accompanying notes on pages 8 to 53 are an integral part of these financial statements.

Emil Soghomonyan
Chairman of the Executive Board

Alvard Mkrtumyan
Chief accountant

Statement of changes in equity

In thousand Armenian drams	Charter capital	Statutory general reserve	Revaluation reserve of securities available for sale	Retained earnings	Total
Balance as of January 1, 2011	7,200,000	52,075	15,641	3,049,369	10,317,085
Increase in charter capital	7,200,000	-	-	-	7,200,000
Transactions with owners	7,200,000	-	-	-	7,200,000
Profit for the year	-	-	-	1,157,164	1,157,164
Other comprehensive income:					
Net unrealized gains from changes in fair value	-	-	125,669	-	125,669
Net gains realized to net profit on available for sale investments	-	-	(7,401)	-	(7,401)
Income tax relating to components of other comprehensive income			(23,653)		(23,653)
Total comprehensive income for the year	-	-	94,615	1,157,164	1,251,779
Balance as of December 31, 2011	**14,400,000**	**52,075**	**110,256**	**4,206,533**	**18,768,864**
Profit for the year	**-**	**-**	**-**	**1,502,756**	**1,502,756**
Other comprehensive income:					
Net unrealized losses from changes in fair value	**-**	**-**	**(30,194)**	**-**	**(30,194)**
Net gains realized to net profit on available for sale investments	**-**	**-**	**(21,206)**	**-**	**(21,206)**
Income tax relating to components of other comprehensive income	**-**	**-**	**10,280**	**-**	**10,280**
Total comprehensive income for the year	**-**	**-**	**(41,120)**	**1,502,756**	**1,461,636**
Balance as of December 31, 2012	**14,400,000**	**52,075**	**69,136**	**5,709,289**	**20,230,500**

Statement of cash flows

In thousand Armenian drams	**Year ended December 31, 2012**	Year ended December 31, 2011
Cash flows from operating activities		
Profit before tax	**1,914,672**	1,464,462
Adjustments for		
Increase in provision for impairment	**65,881**	262,657
Amortization and depreciation allowances	**150,886**	137,963
Loss from impairment of fixed assets	**46**	-
Recovery of loans previously written off	**-**	50
Interest receivable	**(35,071)**	(339,831)
Interest payable	**66,328**	313,040
Net gain from change in fair value of trading instruments	**-**	(38,216)
(Gains)/loss from currency translation of non-trading assets and liabilities	**11,521**	(450)
Net gain from change in fair value of derivative financial instruments	**(370)**	(985)
Cash flows from operating activities before changes in operating assets and liabilities	**2,173,893**	1,798,690
(Increase)/decrease in operating assets		
Derivative financial instruments	**1,627**	**-**
Amounts due from other financial institutions	**(1,854,505)**	58,247
Acquisition of trading securities	**759,718**	(721,502)
Loans and advances to customers	**(4,132,094)**	(10,092,908)
Securities pledged under repurchase agreements	**(3,880,076)**	(990,397)
Securities available for sale	**1,498,661**	(906,977)
Other assets	**39,287**	(161,954)
Increase/(decrease) in operating liabilities		
Amounts due to financial institutions	**(677,108)**	87,932
Repurchase agreements with CBA	**4,180,759**	1,033,406
Amounts due to customers	**7,880,276**	3,851,422
Other liabilities	**87,724**	91,880
Derivative financial instruments	**(642)**	-
Net cash flow from/(used in) operating activities before income tax	**6,077,520**	(5,952,161)
Income tax paid	**(455,676)**	(206,872)
Net cash from/(used in) operating activities	**5,621,844**	(6,159,033)
Cash flows from investing activities		
Repayment of investment securities	**283,766**	65,802
Purchase of property and equipment	**(290,365)**	(261,887)
Proceeds from sale of property and equipment	**-**	409
Purchase of intangible assets	**(3,150)**	(1,872)
Net cash used in investing activities	**(9,749)**	(197,548)
Cash flow from financing activities		
Issue of charter capital	**-**	7,200,000
Redemption of debt securities issued	**-**	(3,483,511)
Loans redeemed from financial institutions	**-**	(40,901)
Loans received from the CBA	**-**	3,600,000
Other long term loans	**921,859**	-
Net cash from financing activities	**921,859**	7,275,588
Net increase in cash and cash equivalents	**6,533,954**	919,007

In thousand Armenian drams	**Year ended December 31, 2012**	Year ended December 31, 2011
Cash and cash equivalents at the beginning of the year	**6,496,136**	5,671,737
Exchange differences on cash and cash equivalents	**187,509**	(94,608)
Cash and cash equivalents at the end of the year (Note 14)	**13,217,599**	6,496,136

Supplementary information:

Interest received	**3,397,562**	3,170,600
Interest paid	**(1,591,003)**	(900,996)

Accompanying notes to the financial statements

1 Principal activities

“Prometey Bank” LLC (the “Bank”) is a limited liability company, which was incorporated in the Republic of Armenia on 01.06.1990. The Bank is regulated by the legislation of RA and conducts its business under license number 27, granted on 02.10.1991 by the Central Bank of Armenia (the “CBA”).

The Bank accepts deposits from the public and extends credits, transfers payments in Armenia and abroad, exchanges currencies and provides other banking services to its commercial and retail customers.

The head office of the Bank and its 7 branches are located in Yerevan; one branch is located in Gyumri and another branch is located in Abovyan.

The registered office of the Bank is located at: 44/2 Hanrapetutyan str. Yerevan 0010, Republic of Armenia.

On April 9, 2013 **Moody's Investors Service** international reputable rating company has reconfirmed Prometey Bank's **"B1"** long-term local and foreign currency deposit rating with negative outlook, as well as a **"E+"** standalone bank financial strength rating (BFSR) with stabile outlook.

2 Armenian business environment

Armenia continues to undergo political and economic changes. As an emerging market, Armenia does not possess a developed business and regulatory infrastructure that generally exists in a more mature free market economy. In addition, economic conditions continue to limit the volume of activity in the financial markets, which may not be reflective of the values for financial instruments. The main obstacle to further economic development is a low level of economic and institutional development, along with a centralized economic base.

There are still uncertainties about the economic situation of countries, collaborating with the RA, due to the forecasted slowdown in the world economy, which may lead to the shortage of money transfers from abroad, as well as to the decline in the prices of mining products, upon which the economy of Armenia is significantly dependant. In times of more severe market stress the situation of Armenian economy and of the Bank may be exposed to deterioration. However, as the number of variables and assumptions involved in these uncertainties is big, management cannot make a reliable estimate of the amounts by which the carrying amounts of assets and liabilities of the Bank may be affected.

Accordingly, the financial statements of the Bank do not include the effects of adjustments, which might have been considered necessary.

3 Basis of preparation

3.1 Statement of compliance

The financial statements of the Bank have been prepared in accordance with International Financial Reporting Standards (“IFRS”) as developed and published by the International Accounting Standards Board (IASB), and Interpretations issued by the International Financial Reporting Interpretations Committee (“IFRIC”).

3.2 Basis of measurement

The financial statements have been prepared on a fair value basis for financial assets and liabilities at fair value through profit or loss and available for sale assets, except those for which a reliable measure of fair value is not available. Other financial assets and liabilities are stated at amortized cost and non-financial assets and liabilities are stated at historical cost.

3.3 Functional and presentation currency

Functional currency of the Bank is the currency of the primary economic environment in which the Bank operates. The Bank's functional currency and the Bank's presentation currency is Armenian Drams ("AMD"), since this currency best reflects the economic substance of the underlying events and transactions of the Bank. The Bank prepares statements for regulatory purposes in accordance with legislative requirements of the Republic of Armenia. These financial statements are based on the Bank's books and records as adjusted and reclassified in order to comply with IFRS. The financial statements are presented in thousands of AMD, which is not convertible outside Armenia.

3.4 Changes in accounting policies

In the current year the Bank has adopted all of the new and revised Standards and Interpretations issued by the International Accounting Standards Board (the "IASB") and International Financial Reporting Interpretations Committee (the "IFRIC") of the IASB that are relevant to its operations and effective for annual reporting periods beginning on January 1, 2012. Standards and interpretations effective in the current year have had no impact on the Bank's published financial statements.

3.5 Standards, amendments and interpretations not yet applied by the Bank

At the date of authorization of these financial statements, certain new standards, amendments and interpretations to the existing Standards have been published but are not yet effective. The Bank has not early adopted any of these pronouncements.

Management anticipates that all of the pronouncements will be adopted in the Bank's accounting policy for the first period beginning after the effective date of the pronouncement. Information on new standards, amendments and interpretations that are expected to be relevant to the Bank's financial statements is provided below. Certain other new standards and interpretations have been issued but are not expected to have a material impact on the Bank's financial statements.

New standards, amendments and interpretations to the existing Standards that are not yet effective

IAS 32 (Amendment) *Offsetting Financial Assets and Financial Liabilities*

The amendments to IAS 32 add application guidance to address inconsistencies in applying IAS 32's criteria for offsetting financial assets and financial liabilities in the following two areas:

- The meaning of 'currently has a legally enforceable right of set-off': the amendments clarify that a right of set-off is required to be legally enforceable in the normal course of business, the event of default and the event of insolvency or bankruptcy of the entity and all of the counterparties, and that the right must also exist for all counterparties.
- Since there was diversity in practice related to the interpretation of 'simultaneous settlement' in IAS 32, the IASB has therefore clarified the principle behind net settlement and included an example of a gross settlement system with characteristics that would satisfy the IAS 32 criterion for net settlement.

The amendments are effective for annual reporting periods beginning on or after 1 January 2014 and are required to be applied retrospectively.

IFRS 7 (Amendment) *Offsetting Financial Assets and Financial Liabilities*

The amendment adds qualitative and quantitative disclosures to IFRS 7 relating to gross and net amounts of recognized financial instruments that are (a) set off in the statement of financial position and (b) subject to enforceable master netting arrangements and similar agreements, even if not set off in the statement of financial position.

The amendments are effective for annual reporting periods beginning on or after 1 January 2013, and are required to be applied retrospectively.

IFRS 9 *Financial Instruments*

The IASB aims to replace IAS 39 Financial Instruments: Recognition and Measurement in its entirety. IFRS 9 is being issued in phases. To date, the chapters dealing with recognition, classification, measurement and derecognition of financial assets and liabilities have been issued. Further chapters dealing with impairment methodology and hedge accounting are still being developed.

The IASB has issued an amendment to IFRS 9 which deferred the mandatory effective date of IFRS from 1 January 2013 to 1 January 2015. This means that all the phases of the project to replace IAS 39 will now have the same mandatory effective date. The amendments also provide relief from the requirement to restate comparative financial statements for the effect of applying IFRS 9. This relief was originally only available to companies that chose to apply IFRS 9 prior to 2012. Additional transition disclosures will now be required to help understand the initial application of the Standard.

Management have yet to assess the impact of this new standard on the Bank's financial statements.

IFRS 12 *Disclosure of Interests in Other Entities*

IFRS 12 integrates and makes consistent the disclosure requirements for various types of investments, including unconsolidated structured entities. It introduces new disclosure requirements about the risks to which an entity is exposed from its involvement with structured entities. The standard is effective for annual periods beginning on or after 1 January 2013.

IFRS 13 *Fair Value Measurement*

IFRS 13 does not affect which items are required to be fair-valued, but clarifies the definition of fair value and provides related guidance and enhanced disclosures about fair value measurements. It is applicable for annual periods beginning on or after 1 January 2013. This IFRS shall be applied prospectively and no need to present comparative information provided for periods before initial application of this IFRS. The Bank's management have yet to assess the impact of this new standard on the financial statements.

IAS 1 *Presentation of Financial Statements*

The IAS 1 Amendments require an entity to group items presented in other comprehensive income into those that, in accordance with other IFRSs: (a) will not be reclassified subsequently to profit or loss and (b) will be reclassified subsequently to profit or loss when specific conditions are met. It is applicable for annual periods beginning on or after 1 July 2012. The Bank's management expects this will change the current presentation of items in other comprehensive income; however, it will not affect the measurement or recognition of such items.

Annual Improvements to IFRSs 2009-2011 Cycle

The amendments to IFRSs contained in Annual Improvements 2009-2011 Cycle are effective for annual periods beginning on or after January 1, 2013, although early application is permitted.

The brief descriptions of the issues addressed are presented below:

IAS 1 *Presentation of Financial Statements*

The amendment provides clarification of the requirements for comparative information when an entity provides a third statement of financial position either as required by IAS 8 or voluntarily.

The following issues are addressed for opening statement of financial position

- Comparative information for the opening statement of financial position is required when an entity changes accounting policies, or makes retrospective restatements or reclassifications, in accordance with IAS 8, and
- The appropriate date for the opening statement of financial position is the beginning of the preceding period. Related notes to this opening statement of financaila position are no longer required to be presented

The amendment also clarifies issues related to comparative information beyond the minimum requirements, particularly

- addresses whether an entity should be required to present a complete set of financial statement when it provides financial statements beyond the minimum comparative information requirements (i.e., additional comparative information)
- explains that additional financial statement information need not be presented in the form of a complete set of financial statements for periods beyond the minimum requirements. Any additional information presented should however be presented in accordance with IFRSs and the entity should present comparative information in the related notes for that additional information.

IAS 16 *Property, plant and Equipment*

The amendment addresses the classification of servicing equipment. It clarifies that major spare parts, stand-by equipment and servicing equipment should be classified as property, plant and equipment when they meet the definition of property, plant and equipment in IAS 16 and as inventory otherwise.

IAS 32 *Financial Instruments: Presentation*

The amendment clarifies that income tax relating to distribution to equity holders and to transaction costs of an equity transaction should be accounted for in accordance with IAS 12 Income Taxes.

4 Summary of significant accounting policies

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

4.1 Recognition of income and expenses

Revenue is recognized to the extent that it is probable that the economic benefits will flow to the Bank and the revenue can be reliably measured. Expense is recognized to the extent that it is probable that the economic benefits will flow from the Bank and the expense can be reliably measured. The following specific criteria must also be met before revenue is recognized:

Interest income and expense

Interest income and expense for all interest-bearing financial instruments, except for those classified as held for trading or designated at fair value through profit or loss, are recognised within "interest income" and "interest expense" in the income statement using the effective interest method.

Once the recorded value of a financial asset or a group of similar financial assets has been reduced due to an impairment loss, interest income continues to be recognized using the original effective interest rate applied to the new carrying amount.

Fee and commission income and expenses

Loan origination fees for loans issued to customers are deferred (together with related direct costs) and recognised as an adjustment to the effective yield of the loans. Fees, commissions and other income and expense items are generally recorded on an accrual basis when the service has been provided. Portfolio and other management advisory and service fees are recorded based on the applicable service contracts. Asset management fees related to investment funds are recorded over the period the service is provided. The same principle is applied for wealth management, financial planning and custody services that are continuously provided over an extended period of time.

Dividend income

Revenue is recognized when the Bank's right to receive the payment is established.

Net trading income

Net trading income comprises gains less losses related to trading assets and liabilities, and includes all realized and unrealized fair value changes, interest, dividends and foreign exchange differences related to trading assets and liabilities. Net trading income also includes gains less losses from trading in foreign currencies.

Rental income

Rental income arising on investment properties is accounted for on a straight-line basis over the lease term on ongoing leases and is recorded in the income statement in "Other income".

4.2 Foreign currency translation

Transactions in foreign currencies are initially recorded in the functional currency rate ruling at the date of the transactions. Gains and losses resulting from the translation of trading assets are recognised in the comprehensive statement of income in net trading income, while gains less losses resulting from translation of non-trading assets are recognized in the statement of income in other income or other expense. Monetary assets and liabilities denominated in foreign currencies are retranslated at the functional currency rate of exchange ruling at the balance sheet date.

Changes in the fair value of monetary securities denominated in foreign currency classified as available for sale are analysed between translation differences resulting from changes in the amortised cost of the security and other changes in the carrying amount of the security. Translation differences related to changes in the amortised cost are recognised in profit or loss, and other changes in the carrying amount are recognised in other comprehensive income.

Non-monetary items that are measured in terms of historical cost in a foreign currency are translated using the exchange rates as the dates of the initial transactions. Non-monetary items measured at fair value in a foreign currency are translated using the exchange rates at the date when the fair value was determined. Translation differences on non-monetary items, such as equities held at fair value through profit or loss, are reported as part of the fair value gain or loss. Translation differences on non-monetary items, such as equities classified as available-for-sale financial assets, are included in the fair value reserve in equity.

Differences between the contractual exchange rate of a certain transaction and the prevailing average exchange rate on the date of the transaction are included in gains less losses from trading in foreign currencies in net trading income.

The exchange rates at year-end used by the Bank in the preparation of the financial statements are as follows:

	December 31, 2012	December 31, 2011
AMD/1 US Dollar	**403.58**	385.77
AMD/1 Euro	**532.24**	498.72

4.3 Taxation

Income tax on the profit for the year comprises current and deferred tax. Income tax is recognized in the comprehensive income statement except to the extent that it relates to items recognized directly in equity, in which case it is recognized in equity.

Current tax is the expected tax payable on the taxable income for the year, using tax rates enacted or substantially enacted at the balance sheet date, and any adjustment to tax payable in respect of previous years. In the case when financial statements are authorized for issue before appropriate tax returns are submitted, taxable profits or losses are based on estimates. Tax authorities might have more stringent position in interpreting tax legislation and in reviewing tax calculations. As a result tax authorities might claim additional taxes for those transactions, for which they did not claim previously. As a result significant additional taxes, fines and penalties could arise. Tax review can include 3 calendar years immediately preceding the year of a review. In certain circumstances tax review can include even more periods.

Deferred tax assets and liabilities are calculated in respect of temporary differences using the liability method. Deferred income taxes are provided for all temporary differences arising between the tax bases of assets and liabilities and their carrying values for financial reporting purposes, except where the deferred income tax arises from the initial recognition of goodwill or of an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit nor taxable profit or loss.

A deferred tax asset is recorded only to the extent that it is probable that taxable profit will be available against which the deductible temporary differences can be utilized. Deferred tax assets and liabilities are measured at tax rates that are expected to apply to the period when the asset is realized or the liability is settled, based on tax rates that have been enacted or substantively enacted at the balance sheet date.

Deferred income tax is provided on temporary differences arising on investments in subsidiaries, associates and joint ventures, except where the timing of the reversal of the temporary difference can be controlled and it is probable that the temporary difference will not reverse in the foreseeable future.

The Republic of Armenia also has various operating taxes, which are assessed on the Bank’s activities. These taxes are included as a component of other expenses in the comprehensive statement of income.

4.4 Cash and cash equivalents

Cash and cash equivalents comprise cash on hand, balances on correspondent accounts with the Central Bank of Armenia (excluding those funds deposited for the settlement of ArCa payment cards), and amounts due from other banks, which can be converted into cash at short notice and which are subject to an insignificant risk of changes in value.

Cash and cash equivalents are carried at amortised cost.

4.5 Amounts due from other financial institutions

In the normal course of business, the Bank maintains advances or deposits for various periods of time with other banks. Loans and advances to banks with a fixed maturity term are subsequently measured at amortized cost using the effective interest method. Those that do not have fixed maturities are carried at amortized cost based on maturities estimated by management. Amounts due from other financial institutions are carried net of any allowance for impairment losses.

4.6 Financial instruments

The Bank recognizes financial assets and liabilities on its balance sheet when it becomes a party to the contractual obligation of the instrument. Regular way purchases and sales of financial assets and liabilities are recognised using settlement date accounting. Regular way purchases of financial instruments that will be subsequently measured at fair value between trade date and settlement date are accounted for in the same way as for acquired instruments.

When financial assets and liabilities are recognised initially, they are measured at fair value, plus, in the case of investments not at fair value through profit or loss, directly attributable transaction costs.

After initial recognition all financial liabilities, other than liabilities at fair value through profit or loss (including held for trading) are measured at amortized cost using effective interest method. After initial recognition financial liabilities at fair value through profit or loss are measured at fair value.

The Bank classified its financial assets into the following categories: loans and receivables, financial instruments at fair value through profit or loss, available-for-sale financial instruments and held-to-maturity investments. The classification of investments between the categories is determined at acquisition based on the guidelines established by the management. The Bank determines the classification of its financial assets after initial recognition and, where allowed and appropriate, re-evaluates this designation at each financial year-end.

Financial assets at fair value through profit or loss

This category has two subcategories: financial assets held for trading and those designated at fair value through profit or loss. A financial asset is classified in this category if acquired for the purpose of selling in the short-term or if so designated by management from the initial acquisition of that asset.

In the normal course of business, the Bank enters into various derivative financial instruments including futures, forwards, swaps and options in the foreign exchange and capital markets. Such financial instruments are held for trading and are initially recognised in accordance with the policy for initial recognition of financial instruments and are subsequently measured at fair value. The fair values are estimated based on quoted market prices or pricing models that take into account the current market and contractual prices of the underlying instruments and other factors. Derivatives are carried as assets when their fair value is positive and as liabilities when it is negative. Gains and losses resulting from these instruments are included in the statement of income as gains less losses from trading securities or gains less losses from foreign currencies dealing, depending on the nature of the instrument.

Derivative instruments embedded in other financial instruments are treated as separate derivatives if their risks and characteristics are not closely related to those of the host contracts and the host contracts are not carried at fair value with unrealised gains and losses reported in income. An embedded derivative is a component of a hybrid (combined) financial instrument that includes both the derivative and a host contract with the effect that some of the cash flows of the combined instrument vary in a similar way to a stand-alone derivative.

Financial assets and financial liabilities are designated at fair value through profit or loss when:

- Doing so significantly reduces measurement inconsistencies that would arise if the related derivatives were treated as held for trading and the underlying financial instruments were carried at amortised cost for such as loans and advances to customers or banks and debt securities in issue;
- Certain investments, such as equity investments, that are managed and evaluated on a fair value basis in accordance with a documented risk management or investment strategy and reported to key management personnel on that basis are designated at fair value through profit and loss; and
- Financial instruments, such as debt securities held, containing one or more embedded derivatives significantly modify the cash flows, are designated at fair value through profit and loss.

Derivatives are also classified as held for trading unless they are designated as effective hedging instruments. Gains or losses on financial assets held for trading are recognised in the statement of income.

Held-to-maturity investments

Held-to-maturity investments are financial assets with fixed or determinable payments and fixed maturities that the Bank's management has the positive intention and ability to hold to maturity. Were the Bank to sell other than insignificant amount of held-to-maturity assets not close to their maturity, the entire category would be reclassified as available-for-sale. Held-to-maturity investments are carried at amortized cost using the effective interest rate method, less any allowance for impairment.

Loans and receivables

Loans and receivables are financial assets with fixed or determinable payments, which arise when the Bank provides money directly to a debtor with no intention of trading the receivable.

Loans granted by the Bank with fixed maturities are initially recognized at fair value plus related transaction costs. Where the fair value of consideration given does not equal the fair value of the loan, for example where the loan is issued at lower than market rates, the difference between the fair value of consideration given and the fair value of the loan is recognized as a loss on initial recognition of the loan and included in the comprehensive income statement as losses on origination of assets. Subsequently, the loan carrying value is measured using the effective interest method. Loans to customers that do not have fixed maturities are accounted for under the effective interest method based on expected maturity. Loans to customers are carried net of any allowance for impairment losses.

Available-for-sale financial instruments

Investments available for sale represent debt and equity investments that are intended to be held for an indefinite period of time, which may be sold in response to needs for liquidity or changes in interest rates, exchange rates or equity prices. After initial recognition available-for sale financial assets are measured at fair value with gains or losses being recognised as a separate component of other comprehensive income until the investment is derecognised or until the investment is determined to be impaired at which time the cumulative gain or loss previously reported in equity is included in the comprehensive statement of income. However, interest calculated using the effective interest method is recognised in the comprehensive statement of income. Dividends on available-for-sale equity instruments are recognised in profit or loss when the Bank's right to receive payment is established.

The fair value of investments that are actively traded in organised financial markets is determined by reference to quoted market bid prices at the close of business on the balance sheet date. For investments where there is no active market, fair value is determined using valuation techniques. Such techniques include using recent arm's length market transactions, reference to the current market value of another instrument, which is substantially the same, and discounted cash flow analysis. Otherwise the investments are stated at cost less any allowance for impairment.

4.7 Impairment of financial assets

The Bank assesses at each balance sheet date whether a financial asset or group of financial assets is impaired.

Assets carried at amortized cost

A financial asset or a group of financial assets is impaired and impairment losses are incurred only if there is objective evidence of impairment as a result of one or more events that occurred after the initial recognition of the asset ("loss event") and that loss event (or events) has an impact on the estimated future cash flows of the financial asset or group of financial assets that can be reliably estimated.

Criteria used to determine that there is objective evidence of an impairment loss may include indications that the borrower or a group of borrowers is experiencing significant financial difficulty (for example, equity ratio, net income percentage of sales), default or delinquency in interest or principal payments, breach of loan covenants or conditions, deterioration in the value of collateral, the probability that they will enter bankruptcy or other financial reorganization and where observable data indicate that there is a measurable decrease in the estimated future cash flows, such as changes in arrears or economic conditions that correlate with defaults.

The Bank first assesses whether objective evidence of impairment exists individually for financial assets that are individually significant, and individually or collectively for financial assets that are not individually significant. If it is determined that no objective evidence of impairment exists for an individually assessed financial asset, whether significant or not, the asset is included in a group of financial assets with similar credit risk characteristics and that group of financial assets is collectively assessed for impairment. Assets that are individually assessed for impairment and for which an impairment loss is or continues to be recognised are not included in a collective assessment of impairment.

If there is objective evidence that an impairment loss on financial assets carried at amortised cost has been incurred, the amount of the loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows (excluding future credit losses that have not been incurred) discounted at the financial asset's original effective interest rate (i.e. the effective interest rate computed at initial recognition). The carrying amount of the asset shall be reduced through use of an allowance account. The amount of the loss shall be recognised in the comprehensive statement of income. If a loan or held-to-maturity investment has a variable interest rate, the discount rate for measuring any impairment loss is the current effective interest rate determined under the contract. The Bank may measure impairment on the basis of an instrument's fair value using an observable market price.

The calculation of the present value of the estimated future cash flows of a collateralised financial asset reflects the cash flows that may result from foreclosure less costs for obtaining and selling the collateral, whether or not the foreclosure is probable.

For the purpose of a collective evaluation of impairment, financial assets are grouped on the basis of the Bank’s internal credit grading system that considers credit risk characteristics such as asset type, industry, geographical location, collateral type, past-due status and other relevant factors.

Future cash flows in a group of financial assets that are collectively evaluated for impairment are estimated on the basis of the contractual cash flows of the assets in the group and historical loss experience for assets with credit risk characteristics similar to those in the group. Historical loss experience is adjusted on the basis of current observable data to reflect the effects of current conditions that did not affect the period on which the historical loss experience is based and to remove the effects of conditions in the historical period that do not currently exist.

Estimates of changes in future cash flows for groups of assets should reflect and be directionally consistent with changes in related observable data from period to period (for example, changes in unemployment rates, property prices, payment status, or other factors indicative of changes in the probability of losses in the group and their magnitude). The methodology and assumptions used for estimating future cash flows are reviewed regularly by the Bank to reduce any differences between loss estimates and actual loss experience.

Loans together with the associated allowance are written off when there is no realistic prospect of future recovery and all collateral has been realized or has been transferred to the Bank. If, in a subsequent year, the amount of the estimated impairment loss increases or decreases because of an event occurring after the impairment was recognized, the previously recognized impairment loss is increased or reduced by adjusting the allowance account. If future write-off is later recovered, the recovery is credited to the allowance account.

Renegotiated loans
Where possible, the Bank seeks to restructure loans rather than to take possession of collateral. This may involve extending the payment arrangements and the agreement of new loan conditions. Once the terms have been renegotiated, the loan is no longer considered past due. Management continuously reviews renegotiated loans to ensure that all criteria are met and that future payments are likely to occur. The loans continue to be subject to an individual or collective impairment assessment, calculated using the loan’s original effective interest rate.

Available-for-sale financial assets
If an available-for-sale asset is impaired, an amount comprising the difference between its cost (net of any principal payment and amortisation) and its current fair value, less any impairment loss previously recognised in the statement on income, is transferred from equity to the statement of income. Reversals of impairment in respect of equity instruments classified as available-for-sale are not recognised in the statement of income but accounted for in other comprehensive income in a separate component of equity. Reversals of impairment losses on debt instruments are reversed through the comprehensive statement of income if the increase in fair value of the instrument can be objectively related to an event occurring after the impairment loss was recognised in profit or loss.

4.8 Derecognition of financial assets and liabilities

Financial assets

A financial asset (or, where applicable a part of a financial asset or part of a group of similar financial assets) is derecognised where:

- the rights to receive cash flows from the asset have expired;
- the Bank has transferred its rights to receive cash flows from the asset, or retained the right to receive cash flows from the asset, but has assumed an obligation to pay them in full without material delay to a third party under a 'pass-through' arrangement; and
- the Bank either (a) has transferred substantially all the risks and rewards of the asset, or (b) has neither transferred nor retained substantially all the risks and rewards of the asset, but has transferred control of the asset.

Where the Bank has transferred its rights to receive cash flows from an asset and has neither transferred nor retained substantially all the risks and rewards of the asset nor transferred control of the asset, the asset is recognised to the extent of the Bank's continuing involvement in the asset. Continuing involvement that takes the form of a guarantee over the transferred asset is measured at the lower of the original carrying amount of the asset and the maximum amount of consideration that the Bank could be required to repay.

Where continuing involvement takes the form of a written and/or purchased option (including a cash-settled option or similar provision) on the transferred asset, the extent of the Bank's continuing involvement is the amount of the transferred asset that the Bank may repurchase, except that in the case of a written put option (including a cash-settled option or similar provision) on an asset measured at fair value, the extent of the Bank's continuing involvement is limited to the lower of the fair value of the transferred asset and the option exercise price.

Financial liabilities

A financial liability is derecognised when the obligation under the liability is discharged or cancelled or expires.

Where an existing financial liability is replaced by another from the same lender on substantially different terms, or the terms of an existing liability are substantially modified, such an exchange or modification is treated as a derecognition of the original liability and the recognition of a new liability, and the difference in the respective carrying amounts is recognised in the statement of income.

4.9 Repurchase and reverse repurchase agreements

Sale and repurchase agreements ("repos") are treated as secured financing transactions. Securities sold under sale and repurchase agreements are retained in the balance sheet and, in case the transferee has the right by contract or custom to sell or repledge them, reclassified as securities pledged under sale and repurchase agreements and faced as the separate balance sheet item. The corresponding liability is presented within amounts due to financial institutions or customers. Securities purchased under agreements to resell ("reverse repo") are recorded as amounts due from other financial institutions or loans and advances to customers as appropriate and are not recognized on the balance sheet. The difference between sale and repurchase price is treated as interest and accrued over the life of repo agreements using the effective yield method.

4.10 Securities lending and borrowing

Securities lending and borrowing transactions are usually collateralised by securities or cash. The transfer of the securities to counterparties is only reflected in the statement of financial position if the risks and rewards of ownership are also transferred. Cash advanced or received as collateral is recorded as an asset or liability.

Securities borrowed are not recognized in the statement of financial position, unless they are sold to third parties, in which case the obligation to return the securities is recorded as a trading liability and measured at fair value with any gains or losses included in "Net trading income".

4.11 Leases

Operating - Bank as leasee

Leases of assets under which the risks and rewards of ownership are effectively retained by the lessor are classified as operating leases. Lease payments under an operating lease are recognised as expenses on a straight-line basis over the lease term and included into other operating expenses.

Operating - Bank as leaser

The Bank presents assets subject to operating leases in the balance sheets according to the nature of the asset. Lease income from operating leases is recognised in statement of income on a straight-line basis over the lease term as other income. The aggregate cost of incentives provided to lessees is recognised as a reduction of rental income over the lease term on a straight-line basis. Initial direct costs incurred specifically to earn revenues from an operating lease are added to the carrying amount of the leased asset.

4.12 Property, plant and equipment

Property, plant and equipment ("PPE") are recorded at historical cost less accumulated depreciation. If the recoverable value of PPE is lower than its carrying amount, due to circumstances not considered to be temporary, the respective asset is written down to its recoverable value. Land is carried at historical cost. It has unlimited useful life and thus is not depreciated.

Depreciation is calculated using the straight-line method based on the estimated useful life of the asset. The following depreciation rates have been applied:

	Useful life (years)	Rate (%)
Buildings	40	2.5
Computers	3	33.3
Vehicles	5	20
Other fixed assets	5	20

Leasehold improvements are capitalized and depreciated over the shorter of the lease term and their useful lives on a straight-line basis. Assets under the course of construction are accounted based on actual expenditures less any impairment losses. Upon completion of construction assets are transferred to property plant and equipment and accounted at their carrying amounts. Assets under the course of construction are not depreciated until they are ready for usage.

Repairs and maintenance are charged to the comprehensive income statement during the period in which they are incurred. The cost of major renovations is included in the carrying amount of the asset when it is incurred and when it satisfies the criteria for asset recognition. Major renovations are depreciated over the remaining useful life of the related asset.

Gains and losses on disposals are determined by comparing proceeds with carrying amount and are included in operating profit.

4.13 Intangible assets

Intangible assets include computer software, licences and other.

Intangible assets acquired separately are measured on initial recognition at cost. Following initial recognition, intangible assets are carried at cost less any accumulated amortisation and any accumulated impairment losses. The useful lives of intangible assets are assessed to be either finite or indefinite. Intangible assets with finite lives are amortised on a straight-line basis over the useful economic lives of 10 years and assessed for impairment whenever there is an indication that the intangible asset may be impaired. Amortisation periods and methods for intangible assets with finite useful lives are reviewed at least at each financial year-end.

Intangible assets with indefinite useful lives are not amortised, but tested for impairment annually either individually or at the cash-generating unit level. The useful life of an intangible asset with an indefinite life is reviewed annually to determine whether indefinite life assessment continues to be supportable.

Costs associated with maintaining computer software programmes are recorded as an expense as incurred.

4.14 Assets held for sale

A non-current asset is classified as held for sale if it is highly probable that the asset’s carrying amount will be recovered through a sale transaction rather than through continuing use. Such sale transaction shall be principally completed within one year from the date of classification of an asset as held for sale.

Assets held for sale are measured at the lower of their carrying amount and fair value less costs to sell. If the fair value less costs to sell of an asset held for sale is lower than its carrying amount, an impairment loss is recognized in the income statement as loss from assets held for sale. Any subsequent increase in an asset’s fair value less costs to sell is recognized to the extent of the cumulative impairment loss that was previously recognized in relation to that specific asset.

4.15 Grants

Grants relating to the assets are included in other liabilities and are credited to the income statement on a straight line basis over the expected lives of the related assets.

4.16 Borrowings

Borrowings, which include amounts due to the Central Bank and Government, amounts due to financial institutions, amounts due to customers, debt securities issued and subordinated debt are initially recognised at the fair value of the consideration received less directly attributable transaction costs. After initial recognition, borrowings are subsequently measured at amortised cost using the effective interest method. Gains and losses are recognised in the comprehensive statement of income when the liabilities are derecognised as well as through the amortisation process.

4.17 Pensions

The Bank does not have any pension arrangements separate from the State pension system of the Republic of Armenia, which requires current contributions by the employer calculated as a percentage of current gross salary payments; such expense is charged in the period the related salaries are earned. In addition, the Bank has no post-retirement benefits or significant other compensated benefits requiring accrual.

4.18 Financial guarantees

Financial guarantee contracts are contracts that require the issuer to make specified payments to reimburse the holder for a loss it incurs because a specified debtor fails to make payments when due, in accordance with the terms of a debt instrument. Such financial guarantees are given to banks, financial institutions and other bodies on behalf of customers to secure loans, overdrafts and other banking facilities.

Financial guarantees are initially recognized in the financial statements at fair value, in "Other liabilities", being the premium received. Following initial recognition, the Bank's liability under each guarantee is measured at the higher of the amortised premium and the best estimate of expenditure required to settle any financial obligation arising as a result of the guarantee.

4.19 Provisions

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

4.20 Charter capital

External costs directly attributable to the issue of new shares, other than on a business combination, are shown as a deduction from the proceeds in equity. Any excess of the fair value of consideration received over the par value of shares issued is recognised as additional paid-in capital.

Dividends

Dividends are recognised as a liability and deducted from equity at the balance sheet date only if they are declared before or on the balance sheet date. Dividends are disclosed when they are proposed before the balance sheet date or proposed or declared after the balance sheet date but before the financial statements are authorised for issue.

4.21 Offsetting

Financial assets and liabilities, and income and expenses, are offset and the net amount reported in the financial statements sheet when there is a legally enforceable right to set off the recognised amounts and there is an intention to settle on a net basis, or realise the asset and settle the liability simultaneously.

5 Critical accounting estimates and judgements

The preparation of financial statements in conformity with IFRS requires management to make judgments, estimates and assumptions that affect the application of policies and the reported amounts of assets and liabilities, income and expense. The estimates and associated assumptions are based on historical experience and various other factors that are believed to be reasonable under the circumstances, the results of which form the basis of making the judgements about carrying values of assets and liabilities that are not readily apparent from other sources. Although these estimates are based on management's best knowledge of current events and actions, actual results ultimately may differ from these estimates.

The most significant areas of judgements and estimates with regards to these financial statements are presented below:

Classification of investment securities

Securities owned by the Bank comprise Armenian state and corporate bonds, securities issued by the Central Bank of Armenia and corporate shares. Upon initial recognition, the Bank designates securities as financial assets with recognition of changes in fair value through profit or loss, held to maturity financial assets or available-for-sale financials assets recognition of changes in fair value through equity.

Related party transactions

In the normal course of business the Bank enters into transactions with its related parties. These transactions are priced predominantly at market rates. Judgement is applied in determining if transactions are priced at market or non-market interest rates, where there is no active market for such transactions. The basis for judgement is pricing for similar types of transactions with unrelated parties and effective interest rate analysis.

Allowance for impairment of loans and receivables

The Bank reviews its problem loans and advances at each reporting date to assess whether there are objective criteria of depreciation. In particular, judgement by management is required in the estimation of the amount and timing of future cash flows when determining the level of allowance required. Such estimates are based on assumptions about a number of factors and actual results may differ, resulting in future changes to the allowance.

In addition to specific allowances against individually significant loans and advances, the Bank also makes a collective impairment allowance against exposures which, although not specifically identified as requiring a specific allowance, have a greater risk of default than when originally granted. This take into consideration factors such as any deterioration in country risk, industry, and technological obsolescence, as well as identified structural weaknesses or deterioration in cash flows.

Tax legislation

Armenian tax legislation is subject to varying interpretations. Refer to Note 31.

Impairment of available-for-sale equity investments

The Bank determined that available-for-sale equity investments are impaired when there has been a significant or prolonged decline in the fair value below its cost. This determination of what is significant or prolonged required judgement. In making this judgement, the Bank evaluates among other factors, the volatility in share price. In addition, impairment may be appropriate when there is evidence of deterioration in the financial health of the investee, industry and sector performance, changes in technology, and operational or financing cash flows.

6 Interest and similar income and expense

In thousand Armenian drams	2012	2011
Loans and advances to customers	**3,755,739**	2,787,920
Investment securities	**577,149**	418,008
Amounts due from financial institutions	**35,724**	6,903
Reverse repurchase transactions	**167,225**	216,330
Other interest income	**6,923**	3,472
Accrued interest on individually impaired assets	**28,669**	-
Total interest and similar income	**4,571,429**	3,432,633
Amounts due to customers	**704,317**	275,757
Debt securities issued	**358,037**	192,886
Amounts due to financial institutions	**463,284**	435,317
Repurchase transactions	**131,692**	77,881
Other interest expenses	**-**	2,907
Total interest and similar expense	**1,657,330**	984,748

7 Fee and commission income and expense

In thousand Armenian drams	2012	2011
Cash collection	**20,012**	16,584
Wire transfer fees	**106,272**	77,245
Plastic cards operations	**43,744**	34,076
Other fees and commissions	**36,185**	34,789
Total fee and commission income	**206,213**	162,694
Wire transfer fees	**27,295**	24,830
Cash operations	**84,747**	108,739
Other expenses	**41,917**	44,183
Total fee and commission expense	**153,959**	177,752

8 Net trading income

In thousand Armenian drams	2012	2011
Gains less losses from trading in foreign currencies	**338,715**	382,863
Gains less losses from change in fair value of trading assets	**67,240**	38,216
Gains less losses from change in fair value of derivative instruments	**370**	985
Net gain/(loss) from derivative instruments	**(107)**	2,871
Interest income from trading bonds	**52,642**	63,383
Total net trading income	**458,860**	488,318

9 Other income

In thousand Armenian drams	2012	2011
Fines and penalties received	**123,427**	32,384
Income from operating lease	**5,057**	16,211
Income from issue of warranties and letters of credit	**12,157**	12,166
Gains less losses from grants relating to assets	**2,074**	2,074
Foreign currency translation net gains of non-trading assets and liabilities	**-**	450
Gain on sale of confiscated property held for sale	**-**	18,794
Other income	**258**	156
Total other income	**142,973**	82,235

10 Impairment charge of impairment for credit losses

In thousand Armenian drams	2012	2011
Loans and advances to customers (Note 18)	**65,881**	262,657
Total impairment charge of impairment for credit losses	**65,881**	262,657

11 Staff costs

In thousand Armenian drams	2012	2011
Wages and salaries	**889,451**	632,959
Social security contributions	**69,276**	54,759
Total staff costs	**958,727**	687,718

12 Other expenses

In thousand Armenian drams	2012	2011
Repair and maintenance expenses of tangible assets	**50,462**	48,066
Advertising costs	**43,546**	50,981
Business trip expenses	**14,800**	3,025
Communications	**78,589**	63,506
Operating lease	**56,268**	71,872
Taxes, other than income tax, duties	**28,021**	25,400
Consulting and other services	**17,340**	16,164
Security	**43,294**	33,368
Representative and public relations expenses	**86,996**	71,700
Office supplies	**29,960**	26,249
Penalties paid	**96**	2,788
Deposit guarantee fund expenses	**17,454**	8,613
Cash collection expenses	**24,246**	13,385
Financial system mediator expenses	**4,279**	2,907
Loss from impairment of PPE	**46**	-
Net losses from foreign currency translation of non trading assets and liabilities	**11,521**	-
Other expenses	**6,984**	18,003
Total other expense	**513,902**	456,027

13 Income tax expense

In thousand Armenian drams	2012	2011
Current tax expense	415,489	322,395
Adjustments of current income tax of previous years	4,233	-
Deferred tax	(7,806)	(15,097)
Total income tax expense	411,916	307,298

The corporate income tax within the Republic of Armenia is levied at the rate of 20% (2011: 20%). Differences between IFRS and RA statutory tax regulations give rise to certain temporary differences between the carrying value of certain assets and liabilities for financial reporting purposes and for profit tax purposes. Deferred income tax is calculated using the principal tax rate of 20%.

Numerical reconciliation between the tax expenses and accounting profit is provided below:

In thousand Armenian drams	2012	Effective rate (%)	2011	Effective rate (%)
Profit before tax	1,914,672		1,464,462	
Income tax at the rate of 20%	382,934	20	292,892	20
Non-deductible expenses	17,043	2	14,496	1
Foreign exchange gains	2,230	-	(90)	-
Other taxable income	5,476	-	-	-
Adjustments of current income tax of previous years	4,233	-	-	-
Income tax expense	411,916	22	307,298	21

Deferred tax calculation in respect of temporary differences:

In thousand Armenian drams	2011	Recognized in comprehensive income statement	Recognized in equity	2012
Other liabilities	3,892	10,017	-	13,909
Capital investments in leased fixed assets	6,225	(2,728)	-	3,497
Gross deferred tax asset	10,117	7,289	-	17,406
Loans and advances to customers	(2,209)	(7,312)	-	(9,521)
Trading securities	(5,875)	5,875	-	-
Other assets	(2,397)	1,954	-	(443)
Available for sale investments	(27,564)	-	10,280	(17,284)
Total deferred tax liabilities	(38,045)	517	10,280	(27,248)
Net deferred tax liability	(27,928)	7,806	10,280	(9,842)

In thousand Armenian drams	2010	Recognized in comprehensive income statement	Recognized in equity	2011
Other liabilities	2,089	1,803	-	3,892
Capital investments in leased fixed assets	3,902	2,323	-	6,225
Gross deferred tax asset	5,991	4,126	-	10,117
Loans and advances to customers	(18,028)	15,819	-	(2,209)
Trading securities	-	(5,875)	-	(5,875)
Other assets	(3,424)	1,027	-	(2,397)
Investment securities available for sale	(3,911)	-	(23,653)	(27,564)
Total deferred tax liability	(25,363)	10,971	(23,653)	(38,045)
Net deferred tax liability	(19,372)	15,097	(23,653)	(27,928)

14 Cash, cash equivalents and balances with CBA

In thousand Armenian drams	**2012**	2011
Cash on hand	**4,381,509**	2,269,215
Correspondent account with the CBA	**7,509,911**	3,833,905
Included in cash and cash equivalents	**11,891,420**	6,103,120
Deposits with the CBA	**312,500**	366,998
Total cash and balances with the CBA	**12,203,920**	6,470,118
Cash and balances with the CBA, included in cash flow	**11,891,420**	6,103,120
Placements with other banks (Note 16)	**1,326,179**	393,016
Total cash and cash equivalents	**13,217,599**	6,496,136

As at 31 December 2012 correspondent account with Central Bank of Armenia represents the obligatory minimum reserve deposits with the CBA, which is computed at 8% of certain obligations of the Bank denominated in Armenian drams and 12% of certain obligations of the Bank, denominated in foreign currency and amounts to AMD 2,940,346 thousand (2011: AMD 1,931,202 thousand). There are no restrictions on the withdrawal of funds from the CBA, however, if minimum average requirement is not met, the Bank could be subject to penalties. Cash on hand, other money market placements, correspondent account, deposited funds with CBA and mandatory reserve deposits are non-interest bearing.

Deposited funds with CBA include a guaranteed deposit for settlements via ArCa payment system.

The following non-cash transaction took place during 2012:

- Repayment of loan obligations through fixed assets in the amount of AMD 1,808,923 thousand (2011: AMD 153,127 thousand).

15 Trading securities

In thousand Armenian drams	2012	2011
Securities issued by the Ministry of Finance	-	759,718
Trading securities	-	759,718

Nominal interest rates and maturities of these securities are as follows:

In thousand Armenian drams	2012		2011	
	%	Maturity	%	Maturity
Securities issued by the Ministry of Finance	-	-	11-13.5	2015-2028

As at 31 December 2011 accrued interest income on debt securities amounts to AMD 28,594 thousand.

16 Amounts due from other financial institutions

In thousand Armenian drams	2012	2011
Correspondent accounts with financial institutions	1,326,179	393,016
Included in cash and cash equivalents	1,326,179	393,016
Loans	1,004,395	-
Deposits	48,509	71,490
Reverse repurchase agreements	2,201,826	1,369,374
Other accounts	54,279	51,884
	3,309,009	1,492,748
Total amounts due from other financial institutions	4,635,188	1,885,764

As at 31 December 2012 correspondent accounts with financial institutions in the amount of AMD 944,034 thousand (71%) (2011: AMD 232,517 thousand (59%)) were due from one commercial bank, which represent significant concentration.

Fair value of assets pledged and carrying value of loans under reverse repurchase agreements as of 31 December 2012 are presented as follows:

In thousand Armenian drams	2012		2011	
	Fair value of collateral	Carrying value of loans	Fair value of collateral	Carrying value of loans
Securities issued by the RA Ministry of Finance	2,286,549	2,201,826	1,418,647	1,369,374
Total assets pledged and loans under reverse repurchase agreements	2,286,549	2,201,826	1,418,647	1,369,374

Deposits in financial institutions represent deposits with regard to Migom payment system and Kompania BKS system for carrying out operations for the Bank's clients in the securities' market.

Other amounts as at 31 December 2012 represent guarantee amounts issued by the Bank in the amount of AMD 54,279 thousand for carrying out transactions via Master Card payment system (2011: AMD 51,884 thousand).

17 Derivative financial instruments

In thousand Armenian drams	**2012**			2011		
	Notional amount	**Fair value of assets**	**Fair value of liabilities**	Notional amount	Fair value of assets	Fair value of liabilities
Derivatives held for trading						
Spot transactions-currency	**1,279,349**	**965**	**595**	520,452	1,627	642
Total derivative financial instruments	**1,279,349**	**965**	**595**	520,452	1,627	642

All spot transactions of the Bank were signed with foreign counterparties.

18 Loans and advances to customers

In thousand Armenian drams	**2012**	2011
Loans and overdrafts	**28,974,113**	25,802,682
Less allowance for loan impairment	**(319,672)**	(258,195)
Total loans and advances to customers	**28,654,441**	25,544,487

As of 31 December 2012 accrued interest income included in loans and advances to customers amounted to AMD 233,606 thousand (2011: AMD 204,879 thousand).

As of 31 December 2012 the effective interest rates on loans and advances to customers ranged from 10.4 to 25 % for loans in AMD (2011: from 10 to 24 %) and from 11.5 to 21.7 % for loans in USD, EUR and other freely convertible currencies (2011: from 11 to 22 %).

As of December 31, 2012, the Bank had a concentration of loans represented by AMD 12,486,825 thousand due from the ten largest third party entities and parties related with them (43% of gross loan portfolio) (2011: AMD 11,769,046 thousand or 46% extended to 10 borrowers and parties related with them). An allowance of AMD 124,868 thousand (2011: AMD 117,690 thousand) was made against these loans.

Reconciliation of loans and advances by industry sectors is as follows:

In thousand Armenian drams	**Industry**	**Construction**	**Trading**	**Consumer**	**Agri-culture**	**Mortgage**	**Other**	**2012 Total**
Loans	**7,544,689**	**5,712,156**	**6,760,224**	**2,881,124**	**470,985**	**1,721,362**	**3,883,573**	**28,974,113**
Less allowance for loan impairment	**(94,995)**	**(59,654)**	**(70,118)**	**(28,811)**	**(4,710)**	**(21,055)**	**(40,329)**	**(319,672)**
Net loans	**7,449,694**	**5,652,502**	**6,690,106**	**2,852,313**	**466,275**	**1,700,307**	**3,843,244**	**28,654,441**

In thousand Armenian drams	Industry	Construction	Trading	Consumer	Agriculture	Mortgage	Other	2011 Total
Loans	6,605,572	5,160,973	6,501,370	1,926,624	87,611	1,112,556	4,407,976	25,802,682
Less allowance for loan impairment	(66,090)	(51,611)	(65,017)	(19,366)	(878)	(11,146)	(44,087)	(258,195)
Net loans	6,539,482	5,109,362	6,436,353	1,907,258	86,733	1,101,410	4,363,889	25,544,487

Reconciliation of allowance account for losses on loans and advances by industry sectors and the collective impairment is as follows:

In thousand Armenian drams	**Industry**	**Construction**	**Trading**	**Consumer**	**Agri-culture**	**Mortgage**	**Other**	**2012 Total**
At 1 January 2012	**66,090**	**51,611**	**65,017**	**19,366**	**878**	**11,146**	**44,087**	**258,195**
Charge/(reversal) for the year	**28,905**	**8,043**	**5,101**	**13,823**	**3,832**	**9,909**	**(3,732)**	**65,881**
Amounts written off	**-**	**-**	**-**	**(8,025)**	**-**	**-**	**(26)**	**(8,051)**
Recoveries	**-**	**-**	**-**	**3,647**	**-**	**-**	**-**	**3,647**
At 31December 2012	**94,995**	**59,654**	**70,118**	**28,811**	**4,710**	**21,055**	**40,329**	**319,672**
Individual impairment	**20,112**	**-**	**2,937**	**-**	**-**	**4,053**	**1,969**	**29,071**
Collective impairment	**74,883**	**59,654**	**67,181**	**28,811**	**4,710**	**17,002**	**38,360**	**290,601**
	94,995	**59,654**	**70,118**	**28,811**	**4,710**	**21,055**	**40,329**	**319,672**
Gross amount of loans individually determined to be impaired, before deducting any individually assessed impairment allowance	**56,353**	**-**	**42,168**	**-**	**-**	**21,145**	**47,623**	**167,289**

In thousand Armenian drams	Industry	Construction	Trading	Consumer	Agri-culture	Mortgage	Other	2011 Total
At 1 January 2011	39,812	45,037	28,931	19,268	757	10,915	15,040	159,760
Charge for the year	26,278	169,851	36,086	1,043	121	231	29,047	262,657
Amounts written off	-	(163,277)	-	(995)	-	-	-	(164,272)
Recoveries	-	-	-	50	-	-	-	50
At 31 December 2011	66,090	51,611	65,017	19,366	878	11,146	44,087	258,195
Collective impairment	66,090	51,611	65,017	19,366	878	11,146	44,087	258,195

Loans and advances by customer profile may be specified as follows:

In thousand Armenian drams	2012	2011
Privately held companies	**22,171,363**	20,454,545
Individuals	**4,592,083**	3,039,493
Sole proprietors	**2,204,779**	2,306,543
Non-commercial institutions	**5,888**	2,101
	28,974,113	25,802,682
Less allowance for loan impairment	**(319,672)**	(258,195)
Total loans and advances to customers	**28,654,441**	25,544,487

Loans to individuals comprise the following products:

In thousand Armenian drams	2012	2011
Mortgage loans	**1,721,362**	1,112,556
Consumer loans	**1,307,285**	845,293
Car loans	**825,155**	823,736
Other	**738,281**	257,908
Total loans and advances to individuals (gross)	**4,592,083**	3,039,493

At 31 December 2012 and 2011 the estimated fair value of loans and advances to customers approximates it carrying value. Refer to Note 33.

Credit, currency and interest rate analyses of loans and advances to customers are disclosed in Note 35. Information on related parties is disclosed in Note 32.

Maturity analysis of loans and advances to customers are disclosed in Note 34.

19 Investment securities

In thousand Armenian drams	Available-for-sale	Held-to-maturity	2012 Total	Available-for-sale	Held-to-maturity	2011 Total
Unquoted investments						
Shares of Armenian companies	**42,825**	**-**	**42,825**	42,825	-	42,825
Securities issued by the RA Ministry of Finance	**532,209**	**196,170**	**728,379**	2,036,570	463,674	2,500,244
Accrued interest	**17,052**	**7,263**	**24,315**	62,752	23,525	86,277
Total investments	**592,086**	**203,433**	**795,519**	2,142,147	487,199	2,629,346

All debt securities have fixed coupons.

The Bank has not reclassified any financial assets measured at amortised cost to fair value during the year (2011: nil).

The fair value of unquoted available-for-sale debt securities is measured using a valuation technique, which uses current market rates to discount future cash flows of the financial instruments.

All unquoted available-for-sale equities are recorded at cost since its fair value cannot be reliably estimated. There is no market for these investments and the Bank intends to hold it for the long term.

Available for sale securities, including securities pledged under repurchase agreements by interest rates and maturity date comprise:

In thousand Armenian drams	**2012**		2011	
	%	**Maturity**	%	Maturity
Securities issued the RA Ministry of Finance	**13.62-15.04**	**2014-2028**	12.08-13.06	2013-2018

Debt securities available for sale at fair value of AMD 3,560,370 thousand (2011: AMD 1,453,378 thousand) were pledged to third parties in sale and repurchase agreements for periods not exceeding six months. These have been reclassified as securities pledged under repurchase agreements on the face of the balance sheet (Note 29).

Held-to-maturity securities at amortised cost of AMD 1,773,084 thousand (2011: nil) were pledged to third parties in sale and repurchase agreements for periods not exceeding six months. These have been reclassified as securities pledged under repurchase agreements on the face of the balance sheet (Note 29).

Held-to-maturity securities

In thousand Armenian drams	**2012**	2011
Nominal value	**200,000**	**550,000**
Discount	**(3,830)**	**(86,326)**
Accrued interest	**7,263**	**23,525**
Total investments held to maturity	**203,433**	**487,199**

Held-to-maturity securities, including securities pledged under repurchase agreements by profitability and maturity date comprise:

In thousand Armenian drams	**2012**		2011	
	%	**Maturity**	%	Maturity
Securities issued the RA Ministry of Finance	**13.62-15.04**	**2014-2028**	15.41	2021

20 Property, plant and equipment

In thousand Armenian drams	Land and buildings	Capital expenditures	Machinery and equipment	Vehicles	Office equipment	Assets under construc-tion	Total
COST							
At January 1, 2011	1,786,916	47,453	184,407	91,119	312,770	-	2,422,665
Additions	-	68,421	59,012	4,423	47,798	82,233	261,887
Disposals	-	-	(23,614)	-	-	-	(23,614)
At December 31, 2011	**1,786,916**	**115,874**	**219,805**	**95,542**	**360,568**	**82,233**	**2,660,938**
Additions	**139,285**	**23,897**	**70,950**	**1,288**	**54,945**	**-**	**290,365**
Disposals	**-**	**-**	**(2,864)**	**-**	**(2,150)**	**-**	**(5,014)**
Adjustment	**29,413**	**(29,413)**	**-**	**-**	**-**	**-**	**-**
Reclassification	**82,233**	**-**	**-**	**-**	**-**	**(82,233)**	**-**
At December 31, 2012	**2,037,847**	**110,358**	**287,891**	**96,830**	**413,363**	**-**	**2,946,289**
DEPRECIATION							
At January 1, 2011	373,850	22,920	133,919	57,217	251,733	-	839,639
Charge for the year	43,207	9,609	26,828	18,336	31,994	-	129,974
Disposals	-	-	(23,205)	-	-	-	(23,205)
At December 31, 2011	**417,057**	**32,529**	**137,542**	**75,553**	**283,727**	**-**	**946,408**
Charge for the year	**45,437**	**18,304**	**42,905**	**10,364**	**25,719**	**-**	**142,729**
Disposals	**-**	**-**	**(2,864)**	**-**	**(2,104)**	**-**	**(4,968)**
At December 31, 2012	**462,494**	**50,833**	**177,583**	**85,917**	**307,342**	**-**	**1,084,169**
CARRYING VALUE							
At December 31, 2012	**1,575,353**	**59,525**	**110,308**	**10,913**	**106,021**	**-**	**1,862,120**
At December 31, 2011	1,369,859	83,345	82,263	19,989	76,841	82,233	1,714,530
At December 31, 2010	1,413,066	24,533	50,488	33,902	61,037	-	1,583,026

The management believes that the fair value of the buildings approximates their carrying amounts.

As at 31 December 2012 and 2011, the Bank does not possess any fixed assets pledged as security for liabilities or whose title is otherwise restricted.

Fully depreciated items

As at 31 December 2012 fixed assets included fully depreciated assets in amount of AMD 427,474 thousand (2011: AMD 361,137 thousand).

Fixed assets in the phase of installation

As at 31 December 2012 fixed assets included assets in the phase of installation in amount of AMD 23,349 thousand (2011: AMD 229 thousand), which are not amortized and are classified in accordance with their type.

Contractual commitments

As at 31 December 2012 the Bank had no contractual commitments (2011: AMD 67,599 thousand).

21 Intangible assets

In thousand Armenian drams	Trademarks, licenses and patents	Acquired software licenses	Other	Total
At January 1, 2011	16,088	32,167	53,077	101,332
Additions	972	900	-	1,872
At December 31, 2011	**17,060**	**33,067**	**53,077**	**103,204**
Additions	**1,810**	**1,340**	**-**	**3,150**
At December 31, 2012	**18,870**	**34,407**	**53,077**	**106,354**
AMORTISATION				
At January 1, 2011	520	25,869	27,451	53,840
Amortisation charge	1,646	1,044	5,299	7,989
At December 31, 2011	**2,166**	**26,913**	**32,750**	**61,829**
Amortisation charge	**1,779**	**1,079**	**5,299**	**8,157**
At December 31, 2012	**3,945**	**27,992**	**38,049**	**69,986**
CARRYING VALUE				
At December 31, 2012	**14,925**	**6,415**	**15,028**	**36,368**
At December 31, 2011	14,894	6,154	20,327	41,375
At December 31, 2010	15,568	6,298	25,626	47,492

As at 31 December 2012 and 2011, the Bank does not possess any intangible assets pledged as security for liabilities or whose title is otherwise restricted.

Contractual commitments

As at 31 December 2012 the Bank had no contractual commitments (As at 31 December 2011: nil).

22 Other assets

In thousand Armenian drams	2012	2011
Prepayments and other debtors	**37,303**	51,908
Other receivables	**85,323**	110,822
Other prepaid taxes	**5,431**	195
Materials	**8,586**	10,110
Other	**2,225**	3,432
Total other assets	**138,868**	176,467

Other amounts receivable represent amounts receivable for transactions through payment systems.

23 Assets held for sale

Details of financial and non-financial confiscated assets serving as collateral for loans issued by the Bank at 31 December are presented below.

In thousand Armenian drams	2012	2011
Real estate	**1,682,341**	153,127
Other	**24,901**	-
Total	**1,707,242**	153,127

It is the Bank's policy to properly and timely dispose the collateral. The Bank does not principally use non-cash collaterals for carrying out its activity. Assets are measured at the lower of carrying amount and fair value less costs to sell.

24 Amounts due to the CBA

In thousand Armenian drams	2012	2011
Subordinated debt	**3,611,809**	3,613,414
Loans under repurchase agreements	**5,218,742**	1,033,859
Total amounts due to the CBA	**8,830,551**	4,647,273

The subordinated debt was issued within April-September 2011 with a maturity period up to 31 December 2016 and an interest rate of 8%.

The Bank has not had any defaults of principal, interest or other breaches with respect to its liabilities during the reporting period (2011: nil).

25 Amounts due to financial institutions

In thousand Armenian drams	2012	2011
Correspondent accounts of other banks	**1,444**	1,444
Current accounts of other financial institutions	**15,703**	10,815
Loans and deposits from financial institutions	**223,301**	354,850
Loans under repurchase agreements	**-**	403,584
Total amounts due to financial institutions	**240,448**	770,693

All deposits from financial institutions have fixed interest rates.

As of 31 December 2012 the effective interest rates on amounts due to financial institutions were 10% for borrowings in AMD (2011: 8%).There are no obligations in USD, EUR and other freely convertible currencies (2011: from 7 to 7.5 %).

The Bank has not had any defaults of principal, interest or other breaches with respect to its liabilities during the period (2011: nil).

26 Amounts due to customers

In thousand Armenian drams	2012	2011
Government of the RA		
Received loans	**1,034,284**	109,391
	1,034,284	109,391
Corporate customers		
Current/Settlement accounts	**7,191,271**	4,460,977
Time deposits	**513,890**	427,434
	7,705,161	4,888,411
Retail customers		
Current/Demand accounts	**1,369,621**	1,404,276
Time deposits	**10,436,756**	5,009,347
	11,806,377	6,413,623
Total amounts due to customers	**20,545,822**	11,411,425

Loans from the Government of the RA include loans received within the scope of "Small and medium business loan project" and "Economy stabilization fund" of German-Armenian fund.

At 31 December 2012 the aggregate balance of top ten customers of the Bank (including related parties, see Note 32) amounts to AMD 11,388,055 thousand (2011: AMD 6,023,754 thousand) or 58% of total customer accounts (2011: 53%).

As of 31 December 2012 the effective interest rates on amounts due to customers ranged from 8% to 10% for borrowings in AMD (2011: from 8% to 10%) and from 3.5% to 9 % for borrowings in USD, EUR and other freely convertible currencies (2011: from 3.5 to 9%).

The Bank has not had any defaults of principal, interest or other breaches with respect to its liabilities during the period (2011: nil).

27 Debt securities issued

In thousand Armenian drams	**2012**	2011
Interest bearing securities	**4,839,866**	4,618,550
Accrued interests	**242,037**	231,356
Total debt securities issued	**5,081,903**	4,849,906

Debt securities were issued in USD. Debt securities in the amount of 2,000 thousand US dollars were issued in 2008, at an annual interest rate of 6% and maturity of up to 5 years. Debt securities in the amount of 10,000 thousand US dollars were issued in 2009, at an annual interest rate of 10.1% and maturity of up to 7 years.

The Bank's issued interest-bearing bonds are not intended for circulation in secondary market.

The Bank has not had any defaults of principal, interest or other breaches with respect to its liabilities during the period (2011: nil).

28 Other liabilities

In thousand Armenian drams	**2012**	2011
Accounts payables	**15,177**	11,375
Tax payable, other than income tax	**116,834**	63,351
Grants related to assets	**60,150**	62,224
Due to personnel	**65,643**	14,631
Other	**8,443**	3,494
Total other liabilities	**266,247**	155,075

Grants related to assets

In thousand Armenian drams	**2012**	2011
At January 1	**62,224**	64,298
Recognition of income (Note 9)	**(2,074)**	(2,074)
At December 31	**60,150**	62,224

29 Securities pledged under repurchase agreements

In thousand Armenian drams	Asset		Liability	
	2012	2011	**2012**	2011
Investments available for sale (Note 19,24,25)	**3,560,370**	1,453,378	**3,489,417**	1,437,443
Investments held-to-maturity (Note 19,24)	**1,773,084**	-	**1,729,325**	-
	5,333,454	1,453,378	**5,218,742**	1,437,443

The pledged securities are financial assets pledged under repurchase agreements with other banks, with the right to sell or re-pledge by the counterparty.

30 Equity

As at 31 December 2012 the Bank's registered and paid-in charter capital was AMD 14,400,000 thousand.

The respective participants as at 31 December 2012 and 2011 may be specified as follows:

In thousand Armenian drams	**2012**	
	Paid-in charter capital	**% of total paid-in capital**
"ZakNefteGazStroy Prometey" OJSC	**6,642,000**	**46.125**
Vazgen Gevorgyan	**561,600**	**3.9**
"Prometey City" LLC	**7,196,400**	**49.975**
	14,400,000	**100**

In 2011 the participants of the Bank have increased their charter capital by AMD 7,200,000.

The charter capital of the Bank was contributed by the participants in Armenian Drams and they are entitled to dividends and any capital distribution in Armenian Drams.

As at 31 December 2012, the Bank did not possess any of its own shares.

Distributable among participants reserves equal the amount of retained earnings, determined according to the Armenian legislation. Non-distributable reserves are represented by a reserve fund, which is created as required by the statutory regulations, in respect of general banking risks, including future losses and other unforeseen risks or contingencies. The reserve has been created in accordance with the Bank's statutes that provide for the creation of a reserve for these purposes of not less than 5 % of the Bank's charter capital reported in statutory books.

31 Contingent liabilities and commitments

Tax and legal matters

The taxation system in Armenia is characterized by frequently changing legislation, which is often unclear, contradictory and subject to interpretation. Often, differing interpretations exist among various taxation authorities and jurisdictions.

Often tax authorities claim additional taxes for transactions and accounting methods, for which they did not claim previously. As a result additional fines and penalties could arise. Tax review can include 3 calendar years immediately preceding the year of a review. In certain circumstances tax review can include earlier periods.

Management believes that the Bank has complied with all regulations and has completely settled all its tax liabilities.

Management also believes that the ultimate liability, if any, arising from legal actions and complaints taken against the Bank, will not have a material adverse impact on the financial condition or results of future operations of the Bank.

Loan commitment, guarantee and other financial facilities

In the normal course of business, the Bank is a party to financial instruments with off-balance sheet risk in order to meet the needs of its customers. These instruments, involving varying degrees of credit risk, are not reflected in the statement of financial position.

As of 31 December the nominal or contract amounts were:

In thousand Armenian drams	**2012**	2011
Undrawn loan commitments	**774,946**	560,731
Guarantees	**372,479**	533,372
Total commitments and contingent liabilities	**1,147,425**	1,094,103

The maximum exposure to credit risk of Loan commitments, guarantee and other financial facilities is best represented by the total amount of these commitments and contingent liabilities.

Operating lease commitments – Bank as a lessee

In the normal course of business the Bank enters into commercial lease agreements for office equipment, central office and branch facilities.

The future aggregate minimum lease payments under non-cancellable operating leases are as follows:

In thousand Armenian drams	**2012**	2011
Not later than 1 year	**89,040**	74,581
Later than 1 year and not later than 5 years	**121,898**	117,674
Later than 5 years	**5,945**	15,530
Total operating lease commitments	**216,883**	207,785

Capital commitments

Information on capital commitments is disclosed in Notes 20 and 21.

Insurance

The insurance industry in Armenia 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 business interruption, or for 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.

Starting 2005 the Bank is member of the obligatory deposit insurance system. The system operates under the Armenian laws and regulations and is governed by the Law on Guarantee of Physical Persons Deposits. Insurance covers Bank's liabilities to individual depositors for the amount up to AMD 4,000 thousand (up to AMD 2,000 thousand for deposits in foreign currency) for each individual in case of business failure and revocation of the banking license.

32 Transactions with related parties

In accordance with IAS 24 *Related Party Disclosures*, parties are considered to be related if one party has ability to control the other party or exercise significant influence over the other party in making financial or operational decisions. For the purpose of the present financial statements, related parties include participants, members of Bank's Management as well as other persons and enterprises related with and controlled by them respectively.

The ultimate participant of the Bank is Vazgen Gevorgyan, who is related with other shareholders of the Bank.

A number of banking transactions are entered into with related parties in the normal course of business. These include loans, deposits and other transactions. These transactions were carried out on commercial terms and at market rates.

The volumes of related party transactions, outstanding balances at the year end, and related expense and income for the year are as follows:

In thousand Armenian drams	**2012**		2011	
	Participants and parties related with them	**Key management personnel and parties related with them**	Participants and parties related with them	Key management personnel and parties related with them
Loans and advances to customers				
Loans outstanding at January 1, gross	**1,714,720**	**46,816**	1,024,625	63,004
Loans issued during the year	**422,343**	**264,419**	1,689,304	151,853
Loan repayments during the year	**(1,185,829)**	**(206,798)**	(999,209)	(168,041)
Loans outstanding at December 31, gross	**951,234**	**104,437**	1,714,720	46,816
Less: allowance for loan impairment	**(9,512)**	**(1,044)**	(17,147)	(468)
Loans outstanding at December 31	**941,722**	**103,393**	1,697,573	46,348
Interest income on loans	**175,558**	**7,671**	250,859	7,759
Impairment charge for credit losses/(reversal)	**(7,635)**	**576**	6,901	(162)
Amounts due to customers				
Deposits at January 1	**799,323**	**249,619**	689,179	39,798
Deposits received during the year	**4,217,775**	**1,400,580**	5,214,974	1,084,162
Deposits repaid during the year	**(4,263,617)**	**(1,271,853)**	(5,104,830)	(874,341)
Deposits at December 31	**753,481**	**378,346**	799,323	249,619
Interest expense on deposits	**59,602**	**19,514**	50,345	5,280
Debt securities issued				
Issued at January 1	**-**	**-**	3,634,400	-
Issued during the year	**-**	**-**	-	-
Redeemed during the year	**-**	**-**	(3,634,400)	-
Issued at December 31	**-**	**-**	-	-
Interest expense on debt securities issued	**-**	**-**	201	-
Income statement items				
Commission income	**1,682**	**537**	591	479
Other income	**937**	**135**	3,358	293
Commission expenses	**-**	**-**	4	12
Other operating expenses	**121**	**77**	150	10

Compensation of key management personnel was comprised of the following:

In thousand Armenian drams	2012	2011
Salaries and other short-term benefits	**366,284**	363,685
Social security costs	**21,295**	23,326
Total key management compensation	**387,579**	387,011

The loans issued to directors and other key management personnel (and close family members) are repayable monthly over 11 years and have interest rates of 10.4-21.9% (2011: 10-20%). The loans advanced to the directors during the year are collateralised by real estates, precious metals, vehicles. The fair value of those collaterals was AMD 1,756,744 thousand (2011: AMD 2,660,353 thousand).

33 Fair value of Financial instruments

Financial instruments not measured at fair value

The fair value of financial assets and liabilities, not presented on the balance sheet at their fair value, are presented below with their carrying values:

In thousand Armenian drams	2012		2011	
	Carrying value	**Fair value**	Carrying value	Fair value
FINANCIAL ASSETS				
Cash and balances with CBA	**12,203,920**	**12,203,920**	6,470,118	6,470,118
Amounts due from other financial institutions	**4,635,188**	**4,635,188**	1,885,764	1,885,764
Loans and advances to customers	**28,654,441**	**28,654,441**	25,544,487	25,544,487
Security pledged under repurchase agreements	**1,773,084**	**1,773,372**	-	-
Investments held to maturity	**203,433**	**204,998**	487,199	486,918
Other assets	**85,323**	**85,323**	110,822	110,822
FINANCIAL LIABILITIES				
Amounts due to the CBA	**8,830,551**	**8,830,551**	4,647,273	4,647,273
Amounts due to financial institutions	**240,448**	**240,448**	770,693	770,693
Amounts due to customers	**20,545,822**	**20,545,822**	11,411,425	11,411,425
Issued debt securities	**5,081,903**	**5,081,903**	4,849,906	4,849,906

Amounts due from and to financial institutions

For assets and liabilities maturing within one month, the carrying amount approximates fair value due to the relatively short-term maturity of these financial instruments. For the assets and liabilities maturing in over one month, the fair value was estimated as the present value of estimated future cash flows discounted at the appropriate year-end market rates, which are mainly the same as current interest rates.

Loans and advances to customers

The fair value of floating rate instruments is normally 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. Discount rates used depend on credit risk of the counterparty and ranged from 10.47% to 24.36% per annum.

Investment securities held to maturity

Market values have been used to determine the fair value of investment securities held-to-maturity traded on an active market. For securities that are not traded on an active market, the fair value was estimated as the present value of estimated future cash flows discounted at the year-end market rates.

Other borrowings

The estimated fair value of fixed interest-bearing deposits and other borrowings not quoted in an active market is based on discounted cash flows using interest rates for new debts with similar remaining maturity.

33.1 Fair Value Hierarchy

Financial assets and liabilities measured at fair value in the statement of financial position are presented below. This hierarchy groups financial assets and liabilities into three levels based on the significance of inputs used in measuring the fair value of the financial assets and liabilities. The fair value hierarchy has the following levels:

- Level 1: quoted prices (unadjusted) in active markets for identical assets or liabilities

- Level 2: inputs other than quoted prices included within Level 1 that are observable for the asset and liability, either directly (i.e. as prices) or indirectly (i.e. derived from prices)

- Level 3: inputs for the asset or liability that are not based on observable market data (unobservable inputs).

In thousand Armenian drams				**2012**
	Level 1	**Level 2**	**Level 3**	**Total**
FINANCIAL ASSETS				
Unquoted securities and bonds	**-**	**549,261**	**-**	**549,261**
Securities pledged under repurchase agreements	**-**	**3,560,370**	**-**	**3,560,370**
Derivative financial assets	**-**	**965**	**-**	**965**
Total	**-**	**4,110,596**	**-**	**4,110,596**
FINANCIAL LIABILITIES				
Derivative financial liabilities	**-**	**595**	**-**	**595**
Total	**-**	**595**	**-**	**595**
NET FAIR VALUE		**4,110,001**		**4,110,001**

In thousand Armenian drams				2011
	Level 1	**Level 2**	**Level 3**	**Total**
FINANCIAL ASSETS				
Unquoted securities and bonds	-	2,859,040	-	2,859,040
Securities pledged under repurchase agreements	-	1,453,378		1,453,378
Derivative financial assets	-	1,627	-	1,627
Total	-	4,314,045	-	4,314,045
FINANCIAL LIABILITIES				
Derivative financial liabilities	-	642	-	642
Total	-	642	-	642
NET FAIR VALUE	-	4,313,403	-	4,313,403

Unlisted equity investments.

The fair value of Bank's investment in "ArCa" and "ACRA" unlisted equity investments cannot be reliably measured and is therefore excluded from this disclosure. Refer to note 19 for further information about this equity investment.

The methods and valuation techniques used for the purpose of measuring fair value are unchanged compared to the previous reporting period.

34 Maturity analysis of assets and liabilities

The table below shows an analysis of assets and liabilities analyzed according to when they are expected to be recovered or settled. See Note 35.3 for the Bank's contractual undiscounted repayment obligations.

In thousand Armenian drams								2012
	Demand and less than 1 month	**From 1 to 3 months**	**From 3 to 12 months**	**Subtotal less than 12 months**	**From 1 to 5 years**	**More than 5 years**	**Subtotal over 12 months**	**Total**
ASSETS								
Cash and balances with CBA	11,891,420	-	-	*11,891,420*	-	312,500	*312,500*	12,203,920
Amounts due from other financial institutions	1,326,179	2,254,730	200,000	*3,780,909*	800,000	54,279	*854,279*	4,635,188
Derivative financial assets	965	-	-	*965*	-	-	-	965
Loans and advances to customers	926,712	1,132,849	5,312,898	*7,372,459*	12,938,276	8,343,706	*21,281,982*	28,654,441
Investments available for sale	-	10,649	6,402	*17,051*	325,327	249,708	*575,035*	592,086
Investments held to maturity	-	7,263	-	*7,263*	196,170	-	*196,170*	203,433
Securities pledged under repurchase agreements	2,201,236	-	3,132,218	*5,333,454*	-	-	-	5,333,454
Other assets	85,323	-	-	*85,323*	-	-	-	85,323
	16,431,835	3,405,491	8,651,518	*28,488,844*	14,259,773	8,960,193	*23,219,966*	51,708,810
LIABILITIES								
Amounts due to the CBA	5,230,545	-	-	*5,230,545*	3,600,006	-	*3,600,006*	8,830,551
Derivative financial instruments	595	-	-	*595*	-	-	-	595
Amounts due to financial institutions	17,147	53,962	169,339	*240,448*	-	-	-	240,448
Amounts due to customers	8,598,684	1,585,465	5,443,256	*15,627,405*	4,918,417	-	*4,918,417*	20,545,822
Debt securities issued	-	-	833,920	*833,920*	4,247,983	-	*4,247,983*	5,081,903
	13,846,971	1,639,427	6,446,515	*21,932,913*	12,766,406	-	*12,766,406*	34,699,319
Net position	2,584,864	1,766,064	2,205,003	*6,555,931*	1,493,367	8,960,193	*10,453,560*	17,009,491
Accumulated gap	2,584,864	4,350,928	6,555,931		8,049,298	17,009,491		

In thousand Armenian drams								2011
	Demand and less than 1 month	From 1 to 3 months	From 3 to 12 months	Subtotal less than 12 months	From 1 to 5 years	More than 5 years	Subtotal over 12 months	Total
ASSETS								
Cash and balances with CBA	6,470,118	-	-	6,470,118	-	-	-	6,470,118
Trading securities	-	-	-	-	-	759,718	759,718	759,718
Amounts due from other financial institutions	1,885,764	-	-	1,885,764	-	-	-	1,885,764
Derivative financial assets	1,627	-	-	1,627	-	-	-	1,627
Loans and advances to customers	35,653	1,045,700	1,420,040	2,501,393	20,119,123	2,923,971	23,043,094	25,544,487
Investments available for sale	-	-	-	-	-	2,142,147	2,142,147	2,142,147
Investments held to maturity	-	-	-	-	487,199	-	487,199	487,199
Securities pledged under repurchase agreements	1,453,378	-	-	1,453,378	-	-	-	1,453,378
Other assets	110,822	-	-	110,822	-	-	-	110,822
	9,957,362	1,045,700	1,420,040	12,423,102	20,606,322	5,825,836	26,432,158	38,855,260
LIABILITIES								
Amounts due to the CBA	1,047,273	-	-	1,047,273	-	3,600,000	3,600,000	4,647,273
Derivative financial instruments	642	-	-	642	-	-	-	642
Amounts due to financial institutions	12,259	731,430	27,004	770,693	-	-	-	770,693
Amounts due to customers	5,612,951	1,228,495	4,428,788	11,270,234	141,191	-	141,191	11,411,425
Debt securities issued	-	-	992,206	992,206	3,857,700	-	3,857,700	4,849,906
	6,673,125	1,959,925	5,447,998	14,081,048	3,998,891	3,600,000	7,598,891	21,679,939
Net position	3,284,237	(914,225)	(4,027,958)	(1,657,946)	16,607,431	2,225,836	18,833,267	17,175,321
Accumulated gap	3,284,237	2,370,012	(1,657,946)		14,949,485	17,175,321		

35 Risk management

The Bank's activities expose it to a variety of financial risks and those activities involve the analysis, evaluation, acceptance and management of some degree of risk or combination of risks.

Risk is managed through a process of ongoing identification, measurement and monitoring, subject to risk limits and other controls. This process of risk management is critical to the Bank's continuing profitability. The Bank is exposed to credit risk, liquidity risk and market risk, the latter being subdivided into trading and non-trading risks. It is also subject to operating risks.

The independent risk control process does not include business risks such as changes in the environment, technology and industry. They are monitored through the Bank's strategic planning process.

Risk management structure

The Board of the Bank and the Management Board are ultimately responsible for identifying and controlling risks; however, there are separate independent bodies responsible for managing and monitoring risks.

Board of the Bank

The Board of the Bank is responsible for the overall risk management approach and for approving the risk strategies and principles.

Management Board

The Management Board is responsible for implementation, realization and control of processes, which are connected with risk management.

Risk Controlling Unit

The Risk Controlling Unit is responsible for monitoring compliance with risk principles, policies and limits across the Bank. This unit also ensures the complete capture of the risks in risk measurement and reporting systems.

Internal audit

Risk management processes throughout the Bank are audited annually by the internal audit function, which examines both the adequacy of the procedures and the Bank's compliance with the procedures. Internal Audit discusses the results of all assessments with management, and reports its findings and recommendations to the Board of the Bank and the Management Board.

Risk measurement and reporting systems

The Bank's risks are measured using a method which reflects both the expected loss likely to arise in normal circumstances and unexpected losses, which are an estimate of the ultimate actual loss based on statistical models. The models make use of probabilities derived from historical experience, adjusted to reflect the economic environment. The Bank also runs worst case scenarios that would arise in the event that extreme events which are unlikely to occur do, in fact, occur.

Monitoring and controlling risks is primarily performed based on limits established by the Bank. These limits reflect the business strategy and market environment of the Bank as well as the level of risk that the Bank is willing to accept, with additional emphasis on selected industries. In addition the Bank monitors and measures the overall risk bearing capacity in relation to the aggregate risk exposure across all risks types and activities.

Information compiled from all the businesses is examined and processed in order to analyse, control and identify early risks. This information is presented and explained to the Board of the Bank and the Management Board. The report includes aggregate credit exposure, hold limit exceptions, liquidity ratios and risk profile changes. On a monthly basis detailed reporting of industry, customer and geographic risks takes place by maturity. The Management receives a comprehensive risk report once a quarter which is designed to provide all the necessary information to assess and conclude on the risks of the Bank.

A daily briefing is given to the members of the Management Board, which includes Bank normative, current balance of the Bank, daily change in income and expenses and changes in off-balance sheet articles.

Excessive risk concentration

Concentrations arise when a number of counterparties are engaged in similar business activities, or activities in the same geographic region, or have similar economic features that would cause their ability to meet contractual obligations to be similarly affected by changes in economic, political or other conditions. Concentrations indicate the relative sensitivity of the Bank's performance to developments affecting a particular industry or geographical location.

In order to avoid excessive concentrations of risks, the Bank's policies and procedures include specific guidelines to focus on maintaining a diversified portfolio. Identified concentrations of credit risks are controlled and managed accordingly.

35.1 Credit risk

The Bank takes on exposure to credit risk, which is the risk that a counterparty will cause a financial loss for the Bank by failing to discharge an obligation. Credit risk is the most important risk for the Bank's business; management therefore carefully manages its exposure to credit risk. Credit exposures arise principally in lending activities that lead to loans and advances, and investment activities that bring debt securities and other bills into the Bank's asset portfolio. There is also credit risk in off-balance sheet financial instruments, such as loan commitments. The credit risk management and control are centralised in credit risk management team of Bank's Risk Management Department and reported to the Board of the Bank and Management Board.

The carrying amounts of the Bank's financial assets best represent the maximum exposure to credit risk related to them, without taking account of any collateral held or other credit enhancements.

35.1.1 Risk concentrations

Geographical sectors

The following table breaks down the Bank's main credit exposure at their carrying amounts, as categorized by geographical region as of 31 December.

In thousand Armenian drams	Armenia	Other non-OECD countries	OECD countries	Total
Cash and balances with CBA	**12,203,920**	**-**	**-**	**12,203,920**
Amounts due from other financial institutions	**3,281,860**	**212,933**	**1,140,395**	**4,635,188**
Derivative financial assets	**-**	**965**	**-**	**965**
Loans and advances to customers	**28,415,713**	**238,728**	**-**	**28,654,441**
Investments available for sale	**592,086**	**-**	**-**	**592,086**
Investments held to maturity	**203,433**	**-**	**-**	**203,433**
Securities pledged under repurchase agreements	**5,333,454**	**-**	**-**	**5,333,454**
Other assets	**85,323**	**-**	**-**	**85,323**
As at 31 December 2012	**50,115,789**	**452,626**	**1,140,395**	**51,708,810**
As at 31 December 2011	38,391,362	146,397	317,501	38,855,260

Assets have been classified based on the country in which the counterparty is located.

Industry sectors

The following table breaks down the Bank's main credit exposure at their carrying amounts, as categorized by the industry sectors of the counterparties as of 31 December.

In thousand Armenian drams	Financial institutions	Manufacturing	Agriculture	Construction	Trading	Consumer sector	Mortgage	Other	Total
Cash and balances with CBA	**12,203,920**	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**12,203,920**
Amounts due from other financial institutions	**4,635,188**	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**4,635,188**
Derivative financial assets	**965**	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**965**
Loans and advances to customers	**-**	**7,449,694**	**5,652,502**	**6,690,106**	**2,852,313**	**466,275**	**1,700,307**	**3,843,244**	**28,654,441**
Investments available for sale	**592,086**	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**592,086**
Investments held to maturity	**203,433**	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**203,433**
Securities pledged under repurchase agreements	**5,333,454**	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**5,333,454**
Other assets	**85,323**	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**85,323**
As at 31 December 2012	**23,054,369**	**7,449,694**	**5,652,502**	**6,690,106**	**2,852,313**	**466,275**	**1,700,307**	**3,843,244**	**51,708,810**
As at 31 December 2011	13,199,951	6,539,482	5,109,362	6,436,353	1,907,258	86,733	1,101,410	4,474,711	38,855,260

35.1.2 Risk limit control and mitigation policies

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, when considered necessary. Limits on the level of credit risk by product, industry sector and by country are approved quarterly by the Board of the Bank.

The exposure to any one borrower including banks and financial organizations is further restricted by sub-limits covering on- and off-balance sheet exposures, and daily delivery risk limits in relation to trading items such as forward foreign exchange contracts. Actual exposures against limits are monitored daily.

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

Some other specific control and mitigation measures are outlined below.

Collateral

The Bank employs a range of policies and practices to mitigate credit risk. It is common practice to take collateral for extended funs. The Bank implements guidelines on the acceptability of specific classes of collateral or credit risk mitigation. The principal collateral types for loans and advances are:

- Mortgages over residential properties;
- Charges over business assets such as premises, other fixed assets, inventory;
- Charges over financial instruments such as debt securities and equities.

Longer-term finance and lending to corporate entities are generally secured; revolving individual credit facilities are generally unsecured. In addition, in order to minimise the credit loss the Bank will seek additional collateral from the counterparty as soon as impairment indicators are noticed for the relevant individual loans and advances.

Collateral held as security for financial assets other than loans and advances is determined by the nature of the instrument. Debt securities, treasury and other eligible bills are generally unsecured.

The analysis of the loan portfolio by collateral is represented as follows:

In thousand Armenian drams	**2012**	2011
Loans collateralized by real estate	**20,583,715**	21,334,068
Loans collateralized by vehicles	**1,503,534**	1,476,611
Loans collateralized by guarantees of enterprises	**151,539**	1,183
Loans collateralized by inventories	**4,670,518**	1,893,202
Loans collateralized by shares of other companies	**576,595**	159,459
Loans collateralized by gold and precious metals	**835,786**	472,204
Loans collateralized by cash	**205,903**	299,519
Other collateral	**446,523**	166,436
Total loans and advances to customers (gross)	**28,974,113**	25,802,682

The amounts presented in the table above are carrying values of the loans, and do not necessarily represent the fair value of the collaterals. Estimates of market values of collaterals are based on valuation of the collateral at the date when loans were provided. Generally they are not updated unless loans are assessed as individually impaired.

Credit-related commitments

The primary purpose of these instruments is to ensure that funds are available to a customer as required. Guarantees and standby letters of credit 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 authorising a third party to draw drafts on the Bank up to a stipulated amount under specific terms and conditions – are collateralised by the underlying shipments of goods to which they relate and therefore carry less risk than a direct loan.

Commitments to extend credit represent unused portions of authorisations to extend credit in the form of loans. In this case, the possible amount of loss, that the Bank may bear, equals to the unused portions of loans.

However, the likely amount of loss is less than the total unused commitments, as most commitments to extend credit are contingent upon customers maintaining specific credit standards. The Bank monitors the term to maturity of credit commitments because longer-term commitments generally have a greater degree of credit risk than shorter-term commitments.

35.1.3 Impairment and provisioning policies

The main considerations for the loan impairment assessment include whether any payments of principal or interest are overdue or there are any known difficulties in the cash flows of counterparties, credit rating downgrades, or infringement of the original terms of the contract. The Bank addresses impairment assessment into areas: individually assessed allowances and collectively assessed allowances.

Individually assessed allowances

The Bank determines the allowances appropriate for each individually significant loan or advance on an individual basis. Items considered when determining allowance amounts include the sustainability of the counterparty's business plan, its ability to improve performance once a financial difficulty has arisen, projected receipts and the expected dividend payout should bankruptcy ensue, the availability of other financial support and the realizable value of collateral, and the timing of the expected cash flows. The impairment losses are evaluated at each reporting date, unless unforeseen circumstances require more careful attention.

Collectively assessed allowances

Allowances are assessed collectively for losses on loans and advances that are not significant (including credit cards, residential mortgages and unsecured consumer loans) and for individually significant loans and advances where there is not yet objective evidence of individual impairment. Allowances are evaluated on each reporting date with each portfolio receiving a separate review.

The collective assessment takes account of impairment that is likely to be present in the portfolio even though there is not yet objective evidence of the impairment in an individual assessment. Impairment losses are estimated by taking into consideration of the following information: historical losses on the portfolio, current economic conditions, the approximate delay between the time a loss is likely to have been incurred and the time it will be identified as requiring an individually assessed impairment allowance, and expected receipts and recoveries once impaired.

Financial guarantees and letters of credit are assessed and provision made in a similar manner as for loans.

Loans and advances neither past due or impaired

The table below shows the credit quality by class of asset for loans and advances neither past due or impaired, based on the historical counterparty default rates.

In thousand Armenian drams	**2012**	2011
Loans and advances to customers		
Industry	**0.33%**	0.67%
Construction	**1.39%**	0.40%
Trade	**0.33%**	0.67%
Consumer	**0.40%**	0.67%
Agriculture	**0.33%**	0.67%
Mortgage	**0.33%**	0.70%
Other	**0.33%**	0.70%

As of 31 December 2012 and 2011 the Bank has not had any losses on other financial assets bearing credit risk.

Past due but not impaired loans

Past due loans and advances include those that are only past due by a few days. The majority of the past due loans are not considered to be impaired.

Analysis of past due loans by age and by class is provided below.

In thousand Armenian drams					**2012**
	Less than 30 days	**31 to 60 days**	**61 to 90 days**	**More than 91 days**	**Total**
Loans and advances to customers					
Industry	**-**	**-**	**-**	**6,455**	**6,455**
Mortgage	**203**	**-**	**-**		**203**
Consumer	**6,182**	**-**	**-**	**11,471**	**17,653**
Total	**6,385**	**-**	**-**	**17,926**	**24,311**

In thousand Armenian drams					2011
	Less than 30 days	31 to 60 days	61 to 90 days	More than 91 days	Total
Loans and advances to customers					
Consumer	1,931	6,799	-	3,300	12,030
Total	1,931	6,799	-	3,300	12,030

Loans and advances individually impaired

Individually impaired loans extended to customers, before deducting any individually assessed impairment allowance, amount to AMD 167,289 thousand (2011: nil) (Note 18).

35.2 Market risk

Market risk is the risk that the fair value or future cash flows of financial instruments will fluctuate due to changes in market variables such as interest rates and foreign exchange rates. The Bank classifies exposures to market risk into either trading or non-trading portfolios. The market risk for the trading portfolio is managed and monitored based on a VaR methodology which reflects the interdependency between risk variables. Non-trading positions are managed and monitored using other sensitivity analyses. Except for the concentrations within foreign currency, the Bank has no significant concentration of market risk.

35.2.1 Market risk – Non-trading

Interest rate risk

Interest rate risk arises from the possibility that changes in interest rates will affect future cash flows or the fair values of financial instruments. The Board of the Bank has established limits on the interest rate gaps for stipulated periods. Positions are monitored on a daily basis.

The following table demonstrates the sensitivity to a reasonable possible change in interest rates, with all other variables held constant, of the Bank's income statement.

The sensitivity of the income statement is the effect of the assumed changes in interest rates on the net interest income for one year, based on the floating rate non-trading financial assets and financial liabilities held at 31 December 2012. The sensitivity of equity is calculated by revaluating fixed rate available-for-sale financial assets at 31 December 2012 for the effects of the assumed changes in interest rates. The sensitivity of equity is analysed by maturity of the asset or swap. The total sensitivity of equity is based on the assumption that there are parallel shifts in the yield curve, while the analysis by maturity displays the sensitivity to non-parallel changes.

In thousand Armenian drams **2012**

Currency	**Change in basis points**	**Sensitivity of net interest income**	**Sensitivity of equity**				
			Up to 6 months	**6 months to 1 year**	**1 year to 5 years**	**More than 5 years**	**Total**
AMD	**1%**	**-**	**-**	**-**	**(143,533)**	**(31,175)**	**(174,708)**
AMD	**-1%**	**-**	**-**	**-**	**149,815**	**33,513**	**183,328**

In thousand Armenian drams 2011

Currency	Change in basis points	Sensitivity of net interest income	Sensitivity of equity				
			Up to 6 months	6 months to 1 year	1 year to 5 years	More than 5 years	Total
AMD	+1%	(117,511)	-	-	(71,969)	(45,542)	(117,511)
AMD	-1%	123,273	-	-	74,724	48,549	123,273

Currency risk

Currency risk is the risk that the value of a financial instrument will fluctuate due to changes in foreign exchange rates. The Board of the Bank has set limits on positions by currency. Positions are monitored on a daily basis

.

The tables below indicate the currencies to which the Bank had significant exposure at 31 December 2012 on its non-trading monetary assets and liabilities and its forecast cash flows. The analysis calculated the effect of a reasonably possible movement of the currency rate against the Armenian dram, with all other variables held constant on the income statement (due to the fair value of currency sensitive non-trading monetary assets and liabilities). A negative amount in the table reflects a potential net reduction in income statement or equity, while a positive amount reflects a net potential increase.

In thousand Armenian drams

	2012			2011	
Currency	**Change in currency rate in %**	**Effect on profit before tax**	**Effect on equity**	Change in currency rate in %	Effect on profit before tax
USD	**+5**	**21,622**	**+5**	+5%	6,398
EUR	**+5**	**200**	**+5**	+5%	124
RUB	**+1**	**21**	**+1**	+1	6
USD	**(5)**	**(21,622)**	**(5)**	-5%	(6,398)
EUR	**(5)**	**(200)**	**(5)**	-5%	(124)
RUB	**(1)**	**(21)**	**(1)**	-1	(50)

The Bank's exposure to foreign currency exchange risk is as follow:

In thousand Armenian drams	Armenian Dram	Freely convertible currencies	Non-freely convertible currencies	Total
ASSETS				
Cash and balances with the CBA	**4,255,069**	**6,702,880**	**1,245,971**	**12,203,920**
Amounts due from other financial institutions	**3,207,175**	**1,293,414**	**134,599**	**4,635,188**
Loans and advances to customers	**15,646,812**	**13,007,629**	**-**	**28,654,441**
Investments available for sale	**592,086**	**-**	**-**	**592,086**
Investments held to maturity	**203,433**	**-**	**-**	**203,433**
Securities pledged under repurchase agreements	**5,333,454**	**-**	**-**	**5,333,454**
Other assets	**50,381**	**32,802**	**2,140**	**85,323**
	29,288,410	**21,036,725**	**1,382,710**	**51,707,845**
LIABILITIES				
Amounts due to the CBA	**8,830,551**	**-**	**-**	**8,830,551**
Amounts due to financial institutions	**240,448**	**-**	**-**	**240,448**
Amounts due to customers	**3,679,320**	**16,764,920**	**101,582**	**20,545,822**
Debt securities issued	**-**	**5,081,903**	**-**	**5,081,903**
	12,750,319	**21,846,823**	**101,582**	**34,698,724**
Total effect of derivative financial instruments on assets	**-**	**1,279,349**	**-**	**1,279,349**
Total effect of derivative financial instruments on liabilities	**-**	**-**	**(1,278,979)**	**(1,278,979)**
Total effect of net derivative financial instruments	**-**	**1,279,349**	**(1,278,979)**	**370**
Net position as at 31 December 2012	**16,538,091**	**469,251**	**2,149**	**17,009,491**
Commitments and contingent liabilities as at 31 December 2012	**885,806**	**261,619**	**-**	**1,147,425**
Total financial assets	24,085,491	14,211,614	558,155	38,855,260
Total financial liabilities	7,066,392	14,577,612	35,935	21,679,939
Net position as at 31 December 2011	17,019,099	(365,998)	522,220	17,175,321
Commitments and contingent liabilities as at 31 December 2011	879,810	214,294	-	1,094,104

Freely convertible currencies represent mainly US dollar amounts, but also include currencies from other OECD countries. Non-freely convertible amounts relate to currencies of CIS countries, excluding Republic of Armenia.

35.3 Liquidity risk

Liquidity risk is the risk that the Bank will be unable to meet its payment obligations when they fall due under normal and stress circumstances. To limit this risk, management has arranged diversified funding sources in addition to its core deposit base, manages assets with liquidity in mind, and monitors future cash flows and liquidity on a daily bases. This incorporates an assessment of expected cash flows and the availability of high grade collateral which could be used to secure additional funding if required.

The Bank maintains a portfolio of highly marketable and diverse assets that can be easily liquidated in the event of an unforeseen interruption of cash flow. The Bank also has committed lines of credit that it can access to meet liquidity needs. In addition, the Bank maintains an obligatory minimum reserve deposits with the Central Bank of Armenia equal to 8% of certain obligations of the Bank denominated in Armenian drams and 12% on certain obligations of the Bank denominated in foreign currency. See note 14. The liquidity position is assessed and managed under a variety of scenarios, giving due consideration to stress factors relating to both the market in general and specifically to the Bank.

The liquidity management of the Bank requires considering the level of liquid assets necessary to settle obligations as they fall due; maintaining access to a range of funding sources; maintaining funding contingency plans and monitoring balance sheet liquidity ratios against regulatory requirements. The Bank calculates liquidity ratios in accordance with the requirement of the Central Bank of Armenia.

	Not audited	
As at 31 December, these ratios were as follows:	**2012**	2011
N21- Total liquidity ratio (Highly liquid assets/ Total assets)	**28.72%**	27.14%
H22- Current liquidity ratio (Highly liquid assets /liabilities on demand)	**172.61%**	197.23%

Analysis of financial liabilities by remaining contractual maturities.

The table below summarises the maturity profile of the Bank's financial liabilities at 31 December 2012 based on contractual undiscounted repayment obligations. See note 34 for the expected maturities of these liabilities. Repayments which are subject to notice are treated as if notice were to be given immediately. However, the Bank expects that many customers will not request repayment on the earliest date the Bank could be required to pay and the table does not reflect the expected cash flows indicated by the Bank's deposit retention history.

In thousand Armenian drams					**2012**
	Demand and less than 1 month	**From 1 to 3 months**	**From 3 to 12 months**	**From 1 to 5 years**	**Total**
NON-DERIVATIVE FINANCIAL LIABILITIES					
Amounts due to the CBA	**5,248,495**	**-**	**-**	**4,315,000**	**9,563,495**
Amounts due to financial institutions	**19,580**	**55,014**	**172,096**	**-**	**246,690**
Amounts due to customers	**8,802,802**	**1,601,323**	**6,802,347**	**5,320,637**	**22,527,109**
Debt securities issued	**-**	**-**	**1,289,965**	**5,470,831**	**6,760,796**
Total undiscounted non-derivative financial liabilities	**14,070,877**	**1,656,337**	**8,264,408**	**15,106,468**	**39,098,090**
DERIVATIVE FINANCIAL LIABILITIES					
Foreign exchange spot transactions					
Inflow	**1,279,349**	-	-	-	**1,279,349**
Outflow	**1,278,979**	-	-	-	**1,278,979**
Commitments and contingent liabilities	**793,746**	**125,302**	**95,211**	**141,558**	**1,155,817**

In thousand Armenian drams	Demand and less than 1 month	From 1 to 3 months	From 3 to 12 months	From 1 to 5 years	More than 5 years	2011 Total
NON-DERIVATIVE FINANCIAL LIABILITIES						
Amounts due to the CBA	1,059,227	-	-	-	5,040,000	6,099,227
Amounts due to financial institutions	12,259	1,245,355	28,190	-	-	1,285,804
Amounts due to customers	5,807,235	938,237	4,624,431	144,172	1,844	11,515,919
Debt securities issued	-	-	935,920	5,734,043	-	6,669,963
Total undiscounted non-derivative financial liabilities	6,878,721	2,183,592	5,588,541	5,878,215	5,041,844	25,570,913
Derivative financial liabilities						
Foreign exchange spot transactions						
Inflow	520,512	-	-	-	-	520,512
Outflow	519,507	-	-	-	-	519,507
Commitments and contingent liabilities	946,198	11,109	210,075	114,328	-	1,281,710

35.4 Operational risk

Operational risk is the risk of direct or indirect loss arising from a wide variety of causes associated with the Bank's involvement with financial instruments, including processes, personnel, technology and infrastructure, and from external factors other than credit, market and liquidity risks such as those arising from legal and regulatory requirements and generally accepted standards of corporate behaviour.

The Bank's objective is to manage operational risk so as to balance the avoidance of financial losses and damage to the Bank's reputation with overall cost effectiveness.

The primary responsibility for the development and implementation of controls to address operational risk is assigned to the Risk Management department, Board of the Bank and Management Board. This responsibility is supported by the development of overall standards for the management of operational risk in the following areas:

- requirements for appropriate segregation of duties, including the independent authorisation of transactions;
- requirements for the reconciliation and monitoring of transactions;
- compliance with regulatory and other legal requirements, including the minimal requirements of the Central Bank of Armenia on internal control system;
- documentation of controls and procedures;
- requirements for the periodic assessment of operational risks faced, and the adequacy of controls and procedures to address the risks identified;
- requirements for the reporting of operational losses and proposed remedial action;
- development of contingency plans;
- training and professional development;
- ethical and business standards; and
- risk mitigation.

Compliance with Bank standards is supported by a programme of periodic reviews undertaken by Internal Audit. The results of Internal Audit reviews are discussed with the management of the Bank to which they relate, with summaries submitted to the Board of the Bank.

36 Capital adequacy

The Bank maintains an actively managed capital base to cover risks inherent in the business. The adequacy of the Bank's capital is monitored using, among other measures, the rules and ratios established in 1988 by the Basel Committee on Banking Supervision ("BIS rules/ratios") and adopted by the Central Bank of Armenia in supervising the Bank.

The primary objectives of the Bank's capital management are to ensure that the Bank complies with externally imposed capital requirements and that the Bank maintains strong credit ratings and healthy capital ratios in order to support its business and to maximise shareholders' value.

The Bank manages its capital structure and makes adjustments to it in the light of changes in economic conditions and the risk characteristics of its activities. In order to maintain or adjust the capital structure, the Bank may adjust the amount of dividend payment to shareholders, return capital to shareholders or issue capital securities. No changes were made in the objectives, polices and processes from the previous years.

The minimum ratio between total capital and risk weighted assets required by the Central Bank of Armenia is 12%.

Regulatory capital consists of Tier 1 capital, which comprises charter capital, retained earnings including current year profit, and general reserve. Regulatory capital is calculated in accordance with the requirements of the Central Bank of Armenia and accounting standards of the Republic of Armenia. The other component of regulatory capital is Tier 2 capital, which includes revaluation reserves and subordinated debt.

The risk-weighted assets are measured by means of a hierarchy of risk weights classified according to the nature of and reflecting an estimate of credit, market and operating risks.

As of 31 December 2012 and 2011 the amount of regulatory capital, risk waited assets and capital adequacy ratio calculated in accordance with the requirements of Central Bank of Armenia are provided below.

	Not audited	
In thousand Armenian drams	**2012**	2011
Tier 1 capital	**20,095,605**	18,453,768
Tier 2 capital	**2,184,803**	2,960,320
Total regulatory capital	**22,280,408**	21,414,088
Risk-weighted assets	**49,152,785**	40,274,756
Capital adequacy ratio	**45.33%**	53.17%

The Bank has complied with all externally imposed capital requirements through the period.

The Central Bank of Armenia has set the minimal required total capital at AMD 5,000,000 thousand from January 1 2009.