

**OPEN JOINT STOCK BANK
“UKRGASBANK”**

Independent Auditors’ Report

Financial Statements
31 December 2003

OPEN JOINT STOCK BANK “UKRGASBANK”

TABLE OF CONTENTS

	Page
INDEPENDENT AUDITORS’ REPORT	1
FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2003:	
Profit and loss account	2
Balance sheet	3
Statement of changes in shareholders’ equity	4
Statement of cash flows	5
Notes to financial statements	6 - 31

INDEPENDENT AUDITORS' REPORT

To the Shareholders and the Board of Directors of
Open Joint Stock Bank UkrGasbank:

We have audited the accompanying balance sheet of Open Joint Stock Bank UkrGasbank (the "Bank") as at 31 December 2003 and the related profit and loss account, and statements of changes in shareholders' equity and cash flows for the year then ended. These financial statements are the responsibility of the Bank's management. Our responsibility is to express an opinion on these financial statements based on our audit.

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

As discussed in Note 2 to the financial statements, the Bank did not adopt International Accounting Standard ("IAS") 29 "Financial Reporting in Hyperinflationary Economies", which practice is not in accordance with International Financial Reporting Standards. Should the Bank properly apply IAS 29 the effect would be to increase the share capital by UAH 50,342 thousand, share premium by UAH 790 thousand, and fixed assets by UAH 4,330 thousand. Retained earnings would be decreased to the net accumulated deficit by UAH 46,802 thousand.

In our opinion, except for the effects on the financial statements of the matter referred to in the preceding paragraph, the financial statements present fairly, in all material respects, the financial position of the Bank as at 31 December 2003 and the results of its operations and its cash flows for the year then ended in accordance with International Financial Reporting Standards.

Deloitte & Touche

26 March 2004

OPEN JOINT STOCK BANK UKRGASBANK

PROFIT AND LOSS ACCOUNT FOR THE YEAR ENDED 31 DECEMBER 2003 (in Ukrainian Hryvnias and in thousands)

	Notes	2003	2002
Interest income	4,26	83,673	60,077
Interest expense	4,26	(49,324)	(33,068)
NET INTEREST INCOME BEFORE PROVISION FOR LOAN LOSSES		34,349	27,009
Provision for loan losses	5	(4,145)	(8,027)
NET INTEREST INCOME AFTER PROVISION FOR LOAN LOSSES		30,204	18,982
Fee and commission income	6	25,574	23,799
Fee and commission expense	6	(3,518)	(1,652)
Net gain on foreign exchange operations	7	6,690	4,610
Net gain on securities available-for-sale	8	5,547	2,127
Other income	9	1,151	4,759
NET NON-INTEREST INCOME		35,444	33,643
OPERATING INCOME		65,648	52,625
OPERATING EXPENSES	10	(60,807)	(49,030)
PROFIT BEFORE OTHER PROVISIONS AND INCOME TAXES		4,841	3,595
(Provision)/recovery of provision for impairment of securities available-for-sale	5	(1,013)	38
Provision for losses on other transactions	5	(780)	(2)
PROFIT BEFORE INCOME TAXES		3,048	3,631
Income tax expense	11	(982)	(626)
NET PROFIT		2,066	3,005



On behalf of the Board

Gennadiy Polishchuk, Chairman of the Board

Tetiana Cheremoshentseva, Acting Chief Accountant

The notes on pages 6 to 31 form an integral part of these financial statements. Independent Auditors' Report is on page 1.

OPEN JOINT STOCK BANK UKRGASBANK

BALANCE SHEET

AS AT 31 DECEMBER 2003

(in Ukrainian Hryvnias and in thousands)

	Notes	2003	2002
ASSETS			
Cash and balances with the National Bank of Ukraine	12	115,413	31,989
Loans and advances to banks, less allowance for loan losses	13	150,243	55,668
Securities available-for-sale, less allowance for impairment	14,26	10,185	3,947
Loans and advances to customers, less allowance for loan losses	15,26	728,510	285,083
Fixed assets, less accumulated depreciation	16	61,385	41,894
Goodwill, less accumulated amortisation	17	502	836
Other assets, less allowance for losses	18	4,957	3,195
TOTAL ASSETS		1,071,195	422,612
LIABILITIES AND SHAREHOLDERS' EQUITY			
LIABILITIES:			
Deposits from banks	19	67,470	40,901
Loans from the National Bank of Ukraine	20	19,340	-
Customer accounts	21,26	876,939	303,013
Deferred income tax liability	11	982	-
Other liabilities	22	2,931	2,115
Total liabilities		967,662	346,029
FINANCIAL COMMITMENTS AND CONTINGENCIES	24	-	-
SHAREHOLDERS' EQUITY:			
Share capital	25	86,922	60,833
Share premium		2,025	2,025
Retained earnings		14,586	13,725
Total shareholders' equity		103,533	76,583
TOTAL LIABILITIES AND SHAREHOLDERS' EQUITY		1,071,195	422,612



On behalf of the Board

Gennadiy Polshchuk, Chairman of the Board

Tetiana Cheremoshentseva, Acting Chief Accountant

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OPEN JOINT STOCK BANK UKRGASBANK

STATEMENT OF CHANGES IN SHAREHOLDERS' EQUITY FOR THE YEAR ENDED 31 DECEMBER 2003 (in Ukrainian Hryvnias and in thousands)

	<u>Share Capital</u>	<u>Share Premium</u>	<u>Retained Earnings</u>	<u>Total</u>
Shareholders' equity as at 31 December 2001	36,564	2,025	11,671	50,260
Share capital increase	24,271	-	-	24,271
Treasury shares repurchased, net	(2)	-	-	(2)
Dividends declared	-	-	(951)	(951)
Net income	-	-	3,005	3,005
Shareholders' equity as at 31 December 2002	60,833	2,025	13,725	76,583
Share capital increase	25,432	-	-	25,432
Treasury shares sold, net	657	-	-	657
Dividends declared	-	-	(1,205)	(1,205)
Net income	-	-	2,066	2,066
Shareholders' equity as at 31 December 2003	86,922	2,025	14,586	103,533



On behalf of the Board

Gennadiy Polishchuk, Chairman of the Board

Tetiana Cheremoshentseva, Acting Chief Accountant

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OPEN JOINT STOCK BANK UKRGASBANK

STATEMENT OF CASH FLOWS FOR THE YEAR ENDED 31 DECEMBER 2003 (in Ukrainian Hryvnias and in thousands)

	Notes	2003	2002
CASH FLOWS FROM OPERATING ACTIVITIES:			
Profit before income taxes		3,048	3,631
Adjustments for:			
Provision for loan losses		4,145	8,027
Provision for losses on other transactions		780	2
Dividend income		(160)	(2,020)
Provision for/(recovery of) impairment of securities available-for-sale		1,013	(38)
Depreciation and amortisation expense		5,615	5,135
Write off of assets against provision		-	-
Loss from fixed assets disposal		718	34
Change in net interest and other accruals		(8,588)	(9,858)
Operating profit before changes in operating assets and liabilities		6,571	4,913
Changes in operating assets and liabilities			
(Increase)/decrease in operating assets:			
Reserve deposit with the National Bank of Ukraine		(25,228)	(13,507)
Loans and advances to banks		(57,890)	(35,436)
Loans and advances to customers		(435,309)	(42,920)
Other assets		(1,547)	9,302
Increase/(decrease) in operating liabilities:			
Loans and advances from banks		26,603	(14,489)
Loans from the National Bank of Ukraine		19,340	-
Customer accounts		570,144	103,256
Other liabilities		(115)	656
Net cash provided by operating activities before income tax		102,569	11,775
Income tax paid		-	(628)
Net cash provided by operating activities		102,569	11,147
CASH FLOW FROM INVESTING ACTIVITIES			
Net cash inflow from acquisition of subsidiary (Note 23)		-	21,661
Purchase of fixed assets		(26,766)	(31,798)
Cash proceeds from disposal of fixed assets		1,276	305
Purchase of securities, net		(7,091)	(545)
Net cash used in investing activities		(32,581)	(10,377)
CASH FLOW FROM FINANCING ACTIVITIES			
Share capital issued		25,432	-
Treasury shares resold/(repurchased)		657	(2)
Dividends paid		(849)	(951)
Net cash provided by/(used in) financing activities		25,240	(953)
NET INCREASE/(DECREASE) IN CASH AND CASH EQUIVALENTS		95,228	(183)
CASH AND CASH EQUIVALENTS, BEGINNING OF YEAR	12	15,319	15,502
CASH AND CASH EQUIVALENTS, END OF YEAR	12	<u>110,547</u>	<u>15,319</u>
Supplementary information:			
Interest received		71,337	48,894
Interest paid		45,576	31,743



On behalf of the Board

Gennadiy Polishchuk, Chairman of the Board

Tetiana Cheremoshentseva, Acting Chief Accountant

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OPEN JOINT STOCK BANK UKRGASBANK

NOTES TO FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2003 (in Ukrainian Hryvnias and in thousands)

1. ORGANIZATION

Open Joint Stock Bank UkrGasbank (the “Bank” or “UkrGasbank”) was legally established as a closed joint stock company on 22 August 1995 under National Bank of Ukraine (“NBU”) license #183, from the former closed joint stock bank “Hadjibej”, which later was renamed in “Intergazbank”. On 27 May 1997 the Bank changed its name from Intergazbank to UkrGasbank. Subsequently, on 10 October 1997, UkrGasbank was re-registered with the NBU as an open joint stock company. The Bank’s primary business consists of banking and financial services to commercial and private customers primarily located in Ukraine. In 1999, the Bank acquired two other Ukrainian banks – Service Bank located in Uzhgorod region and Ukrnaftogasbank which had a network of branches in different regions of Ukraine. Acquired banks lost their legal status and became branches of the Bank. Effective dates of acquisition are 14 January and 24 December 1999, respectively. In 2002 UkrGasbank acquired another Ukrainian Bank – Narodniy Bank with effective date of acquisition of 30 June 2002. In November 2002 the Bank acquired branch in Kharkiv from JSB “Energobank”. In 2003 the Bank acquired branch of OJS Bank Zahidbudgasbank in Kamenets-Podilskiy. Effective date of acquisition is 8 January 2003. Currently the Bank has 18 branches in different regions of Ukraine.

The Bank’s main office is located at 42/4 Pushkinska St. in Kyiv. It had an average of 1,073 employees during 2003 (2002 – an average of 830 employees).

As at 31 December 2003, the following shareholders owned the outstanding shares:

Shareholder	%
“New Gas Technology” LLC	15.3
“Investenergo” LLC	9.9
National JSC “Naftogas Ukraine”	9.9
“National Pension Fund “Ukraine” LLC	9.1
“New era” LLC	7.1
“Inter Invest Consulting” LLC	6.4
“USG Zhyttya” LLC	5.0
Other (less than 5%)	37.3
Total	100.0

These financial statements were authorized for issue by the Board of Directors on 26 March 2004.

2. BASIS OF PRESENTATION

Accounting basis – These financial statements of the Bank have been prepared in accordance with International Financial Reporting Standards (“IFRS”). These financial statements are presented in thousands of Ukrainian Hryvnias (“UAH”), unless otherwise indicated. These financial statements are prepared on accrual basis under the historical cost convention modified for the measurement at fair value of available-for-sale investment securities, financial assets and financial liabilities held for trading.

The Bank maintains its accounting records in accordance with Ukrainian law. These financial statements have been prepared from the Ukrainian statutory accounting records and have been adjusted to conform to IFRS.

Shareholders' equity as at 31 December 2003 and 31 December 2002 and profit for the years then ended are reconciled between Statutory Accounting Legislation and IFRS as follows:

	2003		2002	
	Equity	Profit/(loss)	Equity	Profit/(loss)
Ukrainian Accounting Legislation (unaudited)	106,263	3,307	78,072	1,268
Effect of goodwill	(2,645)	672	(3,317)	150
Deferred taxation	1,771	2,072	(301)	(301)
Fair value adjustments, net	(682)	352	(1,034)	(1,034)
Provisions for losses	(3,204)	(4,423)	1,219	1,219
Provision for impairment	(424)	(999)	575	575
Depreciation	1,957	1,085	872	872
Other, net	497	-	497	256
International Financial Reporting Standards	103,533	2,066	76,583	3,005

Hyperinflationary accounting – In accordance with International Accounting Standard 29 “Financial Reporting in Hyperinflationary Economies” (“IAS 29”) the economy of the Ukraine was considered to be hyperinflationary during 2000 and prior years. Starting from 1 January 2001, the Ukrainian economy is no longer considered to be hyperinflationary.

These financial statements are required to be adjusted to reflect the effects of the diminution of the purchasing power of the Ukrainian Hryvnia. Should the Bank properly apply IAS 29 the effect would be to increase share capital by UAH 50,342 thousand, share premium by UAH 790 thousand, and fixed assets by UAH 4,330 thousand as at 31 December 2003. Retained earnings would be decreased to the net accumulated deficit by UAH 46,802 thousand at the same date.

Use of estimates – The preparation of financial statements in conformity with IFRS requires management to make estimates and assumptions that affect the reported amount of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. Estimates that are particularly susceptible to change relate to the provisions for losses on loans and impairment and the fair value of financial instruments.

Measurement currency – The measurement currency of these financial statements is the Ukrainian Hryvnia (“UAH”). Accordingly, all currencies other than the UAH are treated as foreign currencies.

3. SIGNIFICANT ACCOUNTING POLICIES

Recognition and measurement of financial instruments – The Bank recognizes financial assets and liabilities on its balance sheet when, and only when, it becomes a party to the contractual provisions of the instrument. Regular way purchase and sale of the financial assets and liabilities are recognized using settlement date accounting.

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

Cash and cash equivalents – Cash and cash equivalents include cash, unrestricted balances on correspondent accounts with the National Bank of Ukraine (the “NBU”), advances to banks in countries included in the Organization for Economic Co-operation and Development (“OECD”), except for margin deposits for operations with plastic cards, which may be converted to cash within a short period of time. For purposes of determining cash flows, the minimum reserve deposit required by the National Bank of Ukraine is not included as a cash equivalent due to restrictions on its availability (Note 12).

Loans and advances to banks – 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 cost. Amounts due from credit institutions are carried net of any allowance for losses.

Originated loans – Loans originated by the Bank are financial assets that are created by the Bank by providing money directly to a borrower or by participating in loan facility, other than those that are originated with the intent to be sold immediately or in the short term, which are classified as trading investments.

Loans granted by the Bank are initially recognized in accordance with the policy stated above. The difference between nominal amount of consideration given and the amortized cost of loans issued at other than market terms is recognized in the period the loan is issued as initial recognition adjustment discounting using market rates at inception and included in profit and loss account. Loans to customers with fixed maturities are subsequently measured at amortized cost using the effective interest method. Those that do not have fixed maturities are carried at cost. Loans and advances to customers are carried net of any allowance for loan losses.

Write off of loans – Loans are written off against allowance for loan losses in case of uncollectibility of loans and advances, including through repossession of collateral. Loans are written off with the respective decision of the Board of Directors.

Non-accrual loans – Loans are placed on non-accrual status when interest or principal are recognized as doubtful. Interest income is not recognized in financial statements if recovery is doubtful. Subsequent payments by borrowers are applied to delinquent interest and principal thereon.

Allowance for losses – The Bank establishes an allowance for losses of financial assets when it is probable that the Bank will not be able to collect the principal and interest according to the contractual terms of financial assets, which are carried at cost or amortized cost. The allowance for losses is defined as the difference between carrying amounts and the present value of expected future cash flows, including amounts recoverable from guarantees and collateral, discounted at the original effective interest rate of the financial asset. For financial assets that do not have fixed maturities, expected future cash flows are discounted using periods during which the Bank expects to realize the loan.

The determination of the allowance for loan losses is based on an analysis of the loan portfolio and reflects the amount which, in the judgment of management, is adequate to provide for losses inherent in the loan portfolio. Specific provisions are made as a result of a detailed appraisal of risk assets. In addition, provisions are carried to cover potential risks, which although not specifically identified, are present in the loan portfolio judging by the previous experience.

The change in the allowance for loan losses is charged to profit and the total of the allowance for loan losses is deducted in arriving at loans and advances to customers and banks. Management's evaluation of the allowance is based on the Bank's past loss experience, known and inherent risks in the portfolio, adverse situations that may affect the borrower's ability to repay, the estimated value of any underlying collateral and current economic conditions.

It should be understood that estimates of loan losses involve an exercise of judgment. While it is possible that in particular periods the Bank may sustain losses, which are substantial relative to the allowance for loan losses, it is the judgment of management that the allowance for loan losses is adequate to absorb losses inherent in the loan portfolio.

Securities available-for-sale – Securities available-for-sale represent debt and equity investments that are intended to be held for an indefinite period of time. Such securities are initially recorded at cost which approximates the fair value of the consideration given. Subsequently the securities are

measured at fair value, with such re-measurement included in the profit and loss account, plus accrued coupon income. The Bank uses quoted market prices to determine fair value for the Bank's securities available-for-sale. If such quotes do not exist, management estimation is used. Non-marketable securities that do not have fixed maturities are stated at cost, less allowance for impairment unless there are other appropriate and workable methods of reasonably estimating their fair value. The financial result of sales of securities available-for-sale that are valued at cost and no fair value exist for them is calculated using FIFO method.

Fixed and intangible assets – Fixed and intangible assets are carried at historical cost less accumulated depreciation and any accumulated impairment loss. Depreciation on assets under construction and those not placed in service commences from the date the assets are ready for their intended use. Depreciation of fixed and intangible assets is designed to write off assets over their useful economic lives and is calculated on a straight-line basis at the following annual prescribed rates:

Buildings and improvements	1%
Furniture, vehicles and equipment	20%-25%
Other	25%

The carrying amounts of fixed and intangible assets are reviewed at each balance sheet date to assess whether they are recorded in excess of their recoverable amounts, and where carrying values exceed this estimated recoverable amount, assets are written down to their recoverable amount. Impairment is recognized in the respective period and is included in other administrative and operating expenses. After the recognition of an impairment loss the depreciation charge for fixed assets is adjusted in future periods to allocate the assets' revised carrying value, less its residual value (if any), on a systematic basis over its remaining useful life.

Leasehold improvements are amortized over the life of the related leased asset. Expenses related to repairs and renewals are charged when incurred and included in other administrative and operating expenses unless they qualify for capitalization.

Impairment loss – If the recoverable amount of an asset is less than its carrying amount, the carrying amount of the asset is reduced to its recoverable value. The difference being an impairment loss is recognized as an expense in the profit and loss account for the year in which it arises.

Goodwill – The excess, as at the date of the exchange transaction, of the Bank's interest in the fair value of the net identifiable assets acquired over the cost of an acquisition is recorded as goodwill and recognized as an asset in the balance sheet. Goodwill is carried at cost less accumulated amortization and accumulated impairment losses. Goodwill is amortized on a straight-line basis over its useful life, which has been estimated as being 3 years.

Operating leases – Leases of assets under which the risks and rewards of ownership are effectively retained with the lessor are classified as operating leases.

Bank as lessee – Lease payments under operating lease are recognized as expenses on a straight-line basis over the lease term and included into operating expenses.

Bank as lessor – 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 recognized in profit and loss account on a straight-line basis over the lease term as other operating income. Initial direct costs incurred specifically to earn revenues from an operating lease are recognized as an expense in the profit and loss account in the period in which they are incurred.

Taxation – Taxes on income are computed in accordance with the laws of Ukraine. Deferred taxes, if any, are provided on items recognized in different periods for financial reporting purposes and income tax purposes, using the balance sheet liability method at the tax rates that are expected to apply to the period when the asset is realized or the liability is settled. Deferred tax liabilities, if any,

which result from temporary differences, are provided for in full. Deferred tax assets are recorded to the extent that there is a reasonable expectation that these assets will be realized.

Deferred income tax assets and liabilities are offset when:

- the Bank has a legally enforceable right to set off the recognized amounts of current tax assets and current tax liabilities;
- the Bank has an intention to settle on a net basis, or to realize the asset and settle the liability simultaneously;
- the deferred tax assets and the deferred tax liabilities relate to income taxes levied by the same taxation authority in each future period in which significant amounts of deferred tax liabilities and assets are expected to be settled or recovered.

Ukraine also has various other taxes, which are assessed on the Bank's activities. These taxes are included as a component of operating expenses in the profit and loss account.

Deposits from banks and customers – Customers and bank deposits are initially recognized at cost, which amounts to the issue proceeds less transaction costs incurred. Subsequently amounts due are stated at amortized cost and any difference between net proceeds and the redemption value is recognized in the profit and loss account over the period of the borrowings using the effective interest method.

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

Share capital and share premium – Share capital is recognized at historical nominal cost. Treasury stock is recorded at cost. Gains and losses on sales of treasury stock are credited or charged to share premium.

Dividends on ordinary shares are recognized in shareholders' equity as a reduction in the period in which they are declared. Dividends that are declared after the balance sheet date are treated as a subsequent event under IAS 10 "Events After the Balance Sheet Date" and disclosed accordingly.

Retirement and other benefit obligations – The Bank has pension arrangements from the State pension system of Ukraine and supplementary pensions from the "National Pension Fund "Ukraine" LLC, which requires current contributions by 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.

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

Recognition of income and expense – Interest income and expense are recognized on an accrual basis. The recognition of interest income is suspended when loans are recognized as doubtful to recover. Commissions and other income are credited to income when the related transactions are completed. Loan origination fees are expensed in the period in which they incurred. Non-interest expenses are recognized on an accrual basis.

Foreign currency translation – Monetary assets and liabilities denominated in foreign currencies are translated into Ukrainian Hryvnias at the appropriate spot rates of exchange ruling at the balance sheet date. Foreign currency transactions are accounted for at the exchange rates prevailing at the date of transaction. Profits and losses arising from these translations are included in net gain on foreign exchange operations.

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

	31 December 2003	31 December 2002
UAH/USD	5.331500	5.332400
UAH/EUR	6.662242	5.532898
UAH/RUR	0.18101	0.16777

Offset of financial assets and liabilities – Financial assets and liabilities are offset and reported net on the balance sheet when the Bank has a legally enforceable right to set off the recognized amounts and the Bank intends either to settle on a net basis or to realize the asset and settle the liability simultaneously.

Fiduciary activities – The Bank provides depository services to its customers that include transactions with securities on their depo accounts. Assets accepted and liabilities incurred under the trustee activities are not included in the Bank's financial statements. The Bank accepts the operational risk on these activities, but the Bank's customers bear the credit and market risks associated with such operations.

Reclassifications – Certain reclassifications have been made to the financial statement as at 31 December 2002 to conform to the presentation as at 31 December 2003.

4. NET INTEREST INCOME

Net interest income comprises:

	2003	2002
Interest income		
Interest on loans and advances to customers	79,249	57,685
Interest on loans and advances to banks	4,083	2,386
Interest on securities available-for-sale	338	3
Other interest income	3	3
	<u>83,673</u>	<u>60,077</u>
Interest expense		
Interest on customer accounts	40,717	25,294
Interest on deposits from banks	8,607	7,774
	<u>49,324</u>	<u>33,068</u>
Net interest income before provision for loan losses	<u><u>34,349</u></u>	<u><u>27,009</u></u>

5. ALLOWANCE FOR LOSSES AND IMPAIRMENT, AND PROVISIONS

The movements in allowance for losses on loans and advances to banks and customers were as follows:

	Loans and advances to banks	Loans and advances to customers	Total
31 December 2001	320	19,662	19,982
- provision	61	7,966	8,027
- provision increase due to bank acquisition (Note 23)	-	911	911
- loan write-offs	-	(1,420)	(1,420)
	<u>381</u>	<u>27,119</u>	<u>27,500</u>
31 December 2002			
- provision	437	3,708	4,145
- loan write-offs	-	(1,408)	(1,408)
	<u>818</u>	<u>29,419</u>	<u>30,237</u>
31 December 2003	818	29,419	30,237

The provisions for loans and advances to banks and customers are deducted from the related assets.

The movements in allowances for other losses were as follows:

	Other assets	Guarantees and other commitments	Securities available-for- sale	Total
31 December 2001	32	347	554	933
- provision/(recovery)	110	(108)	(38)	(36)
31 December 2002	142	239	516	897
- provision	205	575	1,013	1,793
- write-offs	-	-	(634)	(634)
31 December 2003	347	814	895	2,056

Allowances for other assets and securities available-for-sale are deducted from the related assets. Provisions for guarantees and commitments are recorded in other liabilities.

6. FEE AND COMMISSION INCOME AND EXPENSE

Fee and commission income and expense comprise:

	2003	2002
Fee and commission income:		
Settlements	18,081	12,751
Foreign exchange operations	5,301	4,734
Loan operations	1,118	40
Operations with securities	330	3,123
Other operations	744	3,151
Total fee and commission income	25,574	23,799
Fee and commission expense:		
Settlements	2,046	1,080
Foreign exchange operations	1,408	487
Other operations	64	85
Total fee and commission expense	3,518	1,652

7. NET GAIN ON FOREIGN EXCHANGE OPERATIONS

Net gain on foreign exchange operations comprises:

	2003	2002
Dealing, net	5,506	3,482
Translation differences, net	1,184	1,128
Total net gain on foreign exchange operations	6,690	4,610

8. NET GAIN ON SECURITIES AVAILABLE FOR SALE

	2003	2002
Gain on sale of securities	5,077	-
Dividend income	186	2,020
Other gains on securities	284	107
Total net gain on securities	5,547	2,127

Dividend income for 2002 represents amount of dividends declared and capitalized on the Bank's investment into Ukrainian Interbank Currency Exchange.

9. OTHER INCOME

	2003	2002
Lease income	509	139
Penalties	102	250
Recovery of loans previously written off	2	3,147
Other income	538	1,223
	<hr/>	<hr/>
Total other income	1,151	4,759
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10. OPERATING EXPENSES

	2003	2002
Staff costs	19,679	13,560
Lease expenses	8,131	5,714
Communication	5,885	3,557
Depreciation	5,281	4,421
Repairs and maintenance	4,033	2,586
Financial risks insurance expense	3,522	9,073
General bank expenses	2,432	1,719
Security expenses	2,046	1,603
Charity	1,799	552
Taxes other than income tax	1,704	932
Advertising	1,265	1,655
Professional services fees	628	437
Amortization of goodwill	334	714
Business trip expenses	323	334
Penalties paid	37	31
Other	3,708	2,142
	<hr/>	<hr/>
Total operating expenses	60,807	49,030
	<hr/> <hr/>	<hr/> <hr/>

11. INCOME TAX EXPENSE

The Bank provides for taxes based on the statutory tax accounts maintained and prepared in accordance with the Ukrainian statutory tax regulations, which may differ from International Financial Reporting Standards. During the years ended 31 December 2003 and 2002, the tax rate for corporations' profits in Ukraine was 30%. According to changes in the Corporate Income Tax Law that came into effect from 1 January 2004, the corporate income tax rate is reduced to 25%. Therefore, the new tax rate was applied to all temporary differences, which are expected to reverse starting from 2004.

The Bank is subject to certain permanent tax differences due to non-tax deductibility of exchange losses and other expenses and tax-free treatment under local tax regulations.

Deferred taxes reflect the net tax effects of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for tax purposes. Temporary differences as at 31 December 2003 and 2002 relate mostly to different methods of income and expense recognition as well as to recorded values of certain assets.

Temporary differences as at 31 December 2003 and 2002 comprise:

	2003	2002
Deferred tax assets:		
Loans to banks and customers	2,417	2,095
Other assets	87	-
Accrued interest	48	1,085
Total deferred tax assets	2,552	3,180
Deferred tax liabilities:		
Fixed assets	570	22
Securities available-for-sale	315	-
Accrued interest	2,780	3,633
Other liabilities	-	241
Total deferred tax liabilities	3,665	3,896
Net deferred tax liability	(1,113)	(716)
Loss carry forward at the statutory tax rate (25%/30%)	131	1,114
Less: valuation allowance	-	(398)
Net deferred income tax liability	(982)	-

Relationships between tax expenses and accounting profit for the years ended 31 December 2003 and 2002 are explained as follows:

	2003	2002
Profit before income taxes	3,048	3,631
Statutory tax rate	30%	30%
Theoretical tax at the statutory tax rate	914	1,089
Tax effect of permanent differences		
Non-deductible expenses	1,185	1,103
Tax exempt income	(737)	(906)
Loss carry forward	(178)	-
Effect of changes in income tax rate	196	82
Change in valuation allowance	(398)	(742)
Income tax expense	982	626
Current income tax expense	-	626
Deferred income tax expense	982	-
Income tax expense	982	626

12. CASH AND BALANCES WITH THE NATIONAL BANK OF UKRAINE

	2003	2002
Cash on hand	42,762	17,636
Balance with the National Bank of Ukraine	72,651	14,353
Total cash and balances with the National Bank of Ukraine	115,413	31,989

The balances with the National Bank of Ukraine (“NBU”) as at 31 December 2003 and 2002 include UAH 47,930 thousand and UAH 22,702 thousand, respectively, which represent the minimum reserve deposits required by the NBU. The Bank is required to maintain the reserve balance at the NBU at all times.

Cash and cash equivalents for the purposes of the statements of cash flows include the following:

	2003	2002
Cash on hand	42,762	17,636
Balances with the NBU	72,651	14,353
	<u>115,413</u>	<u>31,989</u>
Advances to OECD banks (Note 13)	43,064	6,032
	<u>158,477</u>	<u>38,021</u>
Less minimum reserve deposit with the NBU	<u>(47,930)</u>	<u>(22,702)</u>
Total cash and cash equivalents	<u>110,547</u>	<u>15,319</u>

13. LOANS AND ADVANCES TO BANKS, LESS ALLOWANCE FOR LOAN LOSSES

	2003	2002
Advances to OECD banks	43,064	6,032
Advances to non-OECD banks	21,672	6,141
Loans to banks	86,229	43,870
Accrued interest income	96	6
	<u>151,061</u>	<u>56,049</u>
Less allowance for loan losses	<u>(818)</u>	<u>(381)</u>
Loans and advances to banks, less allowance for loan losses	<u>150,243</u>	<u>55,668</u>

Movements in allowances for loan losses for the years ended 31 December 2003 and 2002 are disclosed in Note 5.

As at 31 December 2003 and 2002, the loans to banks include fixed amounts of UAH 3,615 thousand and UAH 7,712 thousand, respectively, placed with OECD Banks as a guarantee deposit on operations with plastic cards.

As at 31 December 2003 and 2002 the Bank had two and one loans totalling UAH 44,984 thousand and UAH 15,997 thousand, respectively, which individually exceeded 10% of the Bank's equity.

As at 31 December 2003 and 2002 the Bank had loans and advances to banks totalling UAH 46,680 thousand and UAH 10,903 thousand, respectively, which represent significant geographical concentration in OECD region forming 31% and 19% of the loans and advances to banks, respectively.

During 2003, the Bank simultaneously placed with and received short-term funds from Ukrainian banks in different currencies. As at 31 December 2003 and 2002, the Bank placed equivalent of UAH 20,682 thousand and UAH 11,021 thousand, respectively as deposits with Ukrainian banks, and received deposits in the same currencies from the same banks (Note 19).

14. SECURITIES AVAILABLE-FOR-SALE, LESS ALLOWANCE FOR IMPAIRMENT

	2003	2002
Securities available-for-sale	11,080	4,463
Less allowance for impairment	<u>(895)</u>	<u>(516)</u>
Total securities available-for-sale, less allowance for impairment	<u>10,185</u>	<u>3,947</u>

Movements in allowances for impairment for the years ended 31 December 2003 and 2002 are disclosed in Note 5.

Securities available-for-sale comprise:

	Interest to nominal/ ownership	2003	Interest to nominal/ ownership	2002
Debt securities available-for-sale				
DP "PG Trade"	18%	2,365	-	-
Equity securities available-for-sale				
CJSC "Trest Kyvmiskbud - 1"	9.32%	5,306	-	-
CJSC "Ukrainian Interbank Currency Exchange"	5.00%	1,800	6.12%	2,203
OJSC "Chernigivgas"	15.17%	432	-	-
OJSC "UkrCARD"	18.57%	272	-	-
OJSC Insurance Company "Beregynya"	8.40%	261	8.19%	100
OJSC "Insurance company Skide"	-	-	13%	700
Other securities available-for-sale		528		1,227
Investments in associated companies		116		233
		11,080		4,463
Less allowance for impairment		(895)		(516)
Total securities available-for-sale, less allowance for impairment		10,185		3,947

Corporate bonds included in debt securities available-for-sale bear annual interest of 18% and mature on 25 May 2004.

Investments in associated companies comprise:

	Ownership	2003	2002
LLC "Zakarpatgasservice"	33%	78	78
CJSC "Izmayil steam-gas electric power station"	25%	38	-
OJSC "SKBT Element"	27%	-	155
Total investments in associated companies		116	233

There are no appropriate or workable methods of reasonably estimating fair value of these investments, therefore these investments are stated at cost.

15. LOANS AND ADVANCES TO CUSTOMERS, LESS ALLOWANCE FOR LOAN LOSSES

Loans and advances to customers comprise:

	2003	2002
Originated loans	727,170	293,269
Accrued interest income	30,759	18,933
	757,929	312,202
Less allowance for loan losses	(29,419)	(27,119)
Total loans and advances to customers, less allowance for loan losses	728,510	285,083

The Bank's loan portfolio is secured as follows:

	2003	2002
Loans collateralized by real estate	250,396	74,645
Loans collateralized by securities	146,917	17,629
Loans collateralized by equipment and other movable assets	123,535	30,349
Loans collateralized by inventories	89,963	51,910
Loans collateralized by accounts receivable	40,604	62,430
Loans collateralized by cash deposits	22,516	16,950
Loans collateralized by other assets	12,054	11,725
Unsecured loans	41,185	27,631
Accrued interest income	30,759	18,933
	<u>757,929</u>	<u>312,202</u>
Less allowance for loan losses	<u>(29,419)</u>	<u>(27,119)</u>
Loans and advances to customers, less allowance for loan losses	<u>728,510</u>	<u>285,083</u>

Movements in allowances for loan losses for the years ended 31 December 2003 and 2002 are disclosed in Note 5.

As at 31 December 2003 and 2002 the Bank had eight and six loans totalling UAH 137,847 thousand and UAH 53,889 thousand, respectively, which individually exceeded 10% of the Bank's equity.

As at 31 December 2003 and 2002 included in loans and advance to customers are non-accrual loans amounted to UAH 18,796 thousand and UAH 34,345 thousand, respectively, on which interest was not accrued.

Loans and advances to customers are made principally within Ukraine and comprise:

Analysis by industry	2003	2002
Agriculture	197,849	46,985
Manufacturing companies	181,186	127,432
Trading and catering companies	177,787	83,033
Consumer loans	83,621	25,890
Construction	41,625	5,394
Transport and communication	34,047	4,139
Other	11,055	396
Accrued interest income	30,759	18,933
	<u>757,929</u>	<u>312,202</u>
Less allowance for loan losses	<u>(29,419)</u>	<u>(27,119)</u>
Loans and advances to customers, less allowance for loan losses	<u>728,510</u>	<u>285,083</u>

As at 31 December 2003 the loans to customers in the amount of UAH 34,300 thousand were pledged as collateral under the loan agreement with the National Bank of Ukraine (Note 20).

16. FIXED ASSETS, LESS ACCUMULATED DEPRECIATION

	Land	Buildings and improvements	Furniture, vehicles and equipment	Other	Total
At cost					
31 December 2002	-	27,241	20,065	3,098	50,404
Additions	2,068	2,862	10,831	11,005	26,766
Transfers	-	95	(98)	3	-
Disposals	-	(1,104)	(1,288)	(101)	(2,493)
31 December 2003	2,068	29,094	29,510	14,005	74,677
Accumulated depreciation					
31 December 2002	-	366	7,591	553	8,510
Depreciation expense	-	88	4,820	373	5,281
Disposals	-	(91)	(325)	(83)	(499)
31 December 2003	-	363	12,086	843	13,292
Net book value					
31 December 2003	<u>2,068</u>	<u>28,731</u>	<u>17,424</u>	<u>13,162</u>	<u>61,385</u>
Net book value					
31 December 2002	<u>-</u>	<u>26,875</u>	<u>12,474</u>	<u>2,545</u>	<u>41,894</u>

17. GOODWILL, LESS ACCUMULATED AMORTISATION

Cost	
31 December 2002	<u>1,003</u>
31 December 2003	<u>1,003</u>
Accumulated amortisation	
31 December 2002	(167)
Charge for the year	<u>(334)</u>
31 December 2003	<u>(501)</u>
Carrying amount	
31 December 2003	<u>502</u>
31 December 2002	<u>836</u>

18. OTHER ASSETS, LESS ALLOWANCE FOR LOSSES

	2003	2002
Prepayments and other accounts receivable	2,331	2,056
Prepayments for purchase of securities	2,105	751
Other income accrued	472	52
Stationery and other materials	396	478
	<u>5,304</u>	<u>3,337</u>
Less allowance for losses	<u>(347)</u>	<u>(142)</u>
Other assets, less allowance for losses	<u>4,957</u>	<u>3,195</u>

Movements in allowances for losses for the years ended 31 December 2003 and 2002 are disclosed in Note 5.

19. DEPOSITS FROM BANKS

Deposits from banks comprise:

	2003	2002
Demand deposits	22,274	6,596
Time deposits	45,195	34,270
Accrued interest expense	1	35
Total deposits from banks	<u>67,470</u>	<u>40,901</u>

As at 31 December 2003 included into deposits from banks is UAH 16,550 thousand with a single Ukrainian bank.

During the year ended 31 December 2003, the Bank increased its borrowings from the banks entering into mutual placements agreements with Ukrainian banks (Note 13).

20. LOANS FROM THE NATIONAL BANK OF UKRAINE

In 2003 the Bank received three short-term loans from the National Bank of Ukraine totalling UAH 19,340 thousand, which mature in March – June 2004. The average interest rate is 8.7% per annum. The loans were collateralized by loans to customers in the amount of UAH 34,300 thousand (Note 15).

21. CUSTOMER ACCOUNTS

	2003	2002
Repayable on demand	272,741	132,628
Time deposits	597,867	167,836
Accrued interest expense	6,331	2,549
Total customer accounts	<u>876,939</u>	<u>303,013</u>

Amounts owed to customers include accounts with the following types of customers:

	2003	2002
Private enterprises	491,624	155,105
Individuals	376,696	145,342
State authorities	2,288	17
Accrued interest expense	6,331	2,549
Total customer accounts	<u>876,939</u>	<u>303,013</u>

22. OTHER LIABILITIES

	2003	2002
Accounts payable to shareholders	1,018	662
Provision for guarantees and other commitments	814	239
Accounts payable for securities	432	2
Accounts payable to Guarantee fund of individuals	285	125
Tax payable	66	383
Other payables and accruals	316	704
Total other liabilities	<u>2,931</u>	<u>2,115</u>

Movement in allowance for guarantees and other commitments is presented in Note 5.

23. ACQUISITIONS

On 29 June 2002 the Bank acquired 100% of the outstanding share capital of Narodniy Bank. The consideration was in the form of shares of Ukrgasbank in total amount of 28,000,000 shares with the nominal value of 1 UAH per share. The Bank recognised this acquisition at fair value of UAH 0.96 per own share and accounted for this acquisition by use of purchase method of accounting. As a result of this transaction the Bank recognized goodwill (Note 17). After acquisition Narodniy Bank lost its legal status and became a branch of the Bank.

Fair value of assets and liabilities acquired:

Cash and balances with the National Bank of Ukraine	684
Loans and advances to Ukrgasbank	20,977
Securities	115
Loans and advances to customers, less allowance for loan losses	10,113
Fixed assets	2,189
Other assets	1,238
Customer accounts	(11,941)
Other liabilities	(107)
Net assets	<u>23,268</u>
Goodwill (Note 17)	<u>1,003</u>
Total consideration (shares at fair value)	<u><u>24,271</u></u>
Net cash inflow arising on acquisition:	
Cash and cash equivalents acquired	<u><u>21,661</u></u>

24. FINANCIAL COMMITMENTS AND CONTINGENCIES

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 balance sheet and are disclosed below.

The Bank's maximum exposure to credit loss under contingent liabilities and commitments to extend credit, in the event of non-performance by the other party where all counterclaims, collateral or security prove valueless, is represented by the contractual amounts of those instruments.

The Bank uses the same credit control and management policies in undertaking off-balance sheet commitments as it does for on-balance operations.

The risk-weighted amount is obtained by applying credit conversion factors and counterparty risk weightings according to the principles employed by the Basle Committee on Banking Supervision.

As at 31 December 2003 and 2002, the nominal or contract amounts and the risk weighted credit equivalents of instruments with off-balance sheet risks were:

	31 December 2003		31 December 2002	
	Nominal amount	Risk weighted amount	Nominal Amount	Risk weighted amount
Contingent liabilities and credit commitments				
Guarantees and other direct substitutes and claims	10,633	10,633	10,617	10,617
Commitments on credits and unused credit lines	95,406	70,759	49,065	49,065
Total	106,039	81,392	59,682	59,682

The Bank has made a provision of UAH 814 thousand and UAH 239 thousand against commitments under guarantees issued as at 31 December 2003 and 2002, included in other liabilities.

Capital commitments – The Bank had no material commitments for capital expenditures outstanding as at 31 December 2003 and 2002.

Operating leases – The Bank’s future minimum rental payments under non-cancelable operating leases of buildings in effect as at 31 December 2003 and 2002 are presented in the table below.

	2003	2002
Not later than 1 year	3,448	4,249
Later than 1 year but not later than 5 years	11,180	17,448
Later than 5 years	3,461	3,282
Total operating lease payments	18,089	24,979

Legal proceedings – From time to time and in the normal course of business, claims against the Bank are received from customers and counterparties. Management is of the opinion that no material unaccrued losses will be incurred and accordingly no provision has been made in these financial statements.

Taxes – The government of the Ukraine continues to reform the business and commercial infrastructure in its transition to a market economy. As a result laws and regulations affecting businesses continue to change rapidly. These changes are characterized by different interpretations and arbitrary application by the authorities. In particular taxes are subject to review and investigation by a number of authorities enabled by law to impose fines and penalties. While the Bank believes it has provided adequately for all tax liabilities based on its understanding of the tax legislation, the above facts may create tax risk of additional taxes, penalties and interest. Tax years remain open to review by tax authorities for three years.

Pensions and retirement plans – Employees receive pension benefits from Ukraine in accordance with the laws and regulations of the country. In March 2003 the Bank arranged supplementary pensions for employees with the “National pension fund “Ukraine” LLC. Pension contributions consist of 5% from the total payroll. The Bank paid UAH 350 thousand during 2003 to this pension fund.

Operating environment – The Bank's principal business activities are within Ukraine. Laws and regulations affecting business environment in Ukraine are subject to rapid changes and the Bank's assets and operations could be at risk due to negative changes in the political and business environment.

25. SHARE CAPITAL

At 31 December 2003 and 2002, the Bank's share capital comprised of preferred and ordinary shares, each having a nominal value of UAH 1. All ordinary shares are ranked equally and carry one vote.

Preferred shares of the Bank carry fixed right to receive annual dividends, subject to approval at the Shareholders' meeting, regardless of the amount of the Bank's profit/loss for the period. Owners of preferred shares have primary right to assets distribution in case of the Bank's liquidation.

Share premium represents the excess of contributions received over the nominal value of shares issued.

During the years ended 31 December 2003 and 2002 the Bank issued 25,432 thousand ordinary shares and sold 657 thousand treasury ordinary shares.

	2003	2002
Number of authorized and issued preferred shares	477	477
Number of authorized and issued ordinary shares	89,523	64,090
Total nominal value	90,000	64,567
Number of authorized, issued and fully paid preferred shares	477	477
Number of authorized, issued and fully paid ordinary shares	62,174	36,085
Number of authorized, issued and fully paid ordinary shares exchanged for Narodniy Bank shares at fair value (Note 23)	24,271	24,271
Total carrying value	86,922	60,833

In 2003 the Meeting of shareholders of the Bank made a decision to pay dividends for 2002 in the total amount of UAH 1,205 thousand.

In 2002 the Meeting of shareholders of the Bank made a decision to pay dividends for 2001 in the total amount of UAH 951 thousand.

26. TRANSACTIONS WITH RELATED PARTIES

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

- (a) enterprises that directly, or indirectly through one or more intermediaries, control, or are controlled by, or are under common control with, the reporting enterprise. (This includes holding companies, subsidiaries and fellow subsidiaries);
- (b) associates – enterprises in which the Bank has significant influence and which is neither a subsidiary nor a joint venture of the investor;
- (c) individuals owning, directly or indirectly, an interest in the voting power of the Bank that gives them significant influence over the Bank;

- (d) key management personnel, that is, those persons having authority and responsibility for planning, directing and controlling the activities of the Bank, including directors and officers of the Bank and close members of the families of such individuals; and
- (e) enterprises in which a substantial interest in the voting power is owned, directly or indirectly, by any person described in (c) or (d) or over which such a person is able to exercise significant influence. This includes enterprises owned by directors or major shareholders of the Bank and enterprises that have a member of key management in common with the Bank.

In considering each possible related party relationship, attention is directed to the substance of the relationship, and not merely the legal form.

The Bank had the following transactions outstanding with related parties:

	2003		2002	
	Related party transactions	Total category as per financial statements caption	Related party transactions	Total category as per financial statements caption
Loans to customers	12,887	757,929	4,480	312,202
Allowance for loan losses	(600)	(29,419)	(90)	(27,119)
Securities available-for-sale	5,306	11,080	155	4,463
Allowance for impairment losses	(63)	(895)	-	(516)
Customer accounts	7,535	876,939	3,237	303,013

During the years ended 31 December 2003 and 2002 the Bank originated loans and advances to customers - related parties amounting to UAH 23,100 thousand and UAH 5,150 thousand, respectively, and received loans and advances repaid of UAH 14,693 thousand and UAH 6,159 thousand, respectively. The Bank has interest income accrued in respect of loans and advances granted to related parties totalling UAH 1,746 thousand and UAH 189 thousand, respectively, as at 31 December 2003 and 2002.

As at 31 December 2002 the Bank had an investment of UAH 155 thousand with an indirect related party that leases premises to the Bank's branch in Odessa at a lower than market price.

During the years ended 31 December 2003 and 2002 the Bank received advances from customers-related parties of UAH 80,542 thousand and UAH 155,616 thousand, respectively, and repaid deposits and advances totalling UAH 76,244 thousand and UAH 158,775 thousand, respectively. The Bank has interest expense accrued in respect of deposits and advances received from related parties, totalling UAH 81 thousand and UAH 32 thousand as at 31 December 2003 and 2002, respectively.

Included in the profit and loss account for the years ended 31 December 2003 and 2002 are the following amounts which arose due to transactions with related parties:

	2003		2002	
	Related party transactions	Total category as per financial statements caption	Related party transactions	Total category as per financial statements caption
Interest income	1,690	83,673	209	60,077
Interest expense	880	49,324	488	33,068

Majority of the transactions with related parties entered by the Bank during the years ended 31 December 2003 and 2002 and outstanding as at 31 December 2003 and 2002 were made in the normal course of business and under arm-length conditions.

27. FAIR VALUE OF FINANCIAL INSTRUMENTS

Estimated fair value disclosures of financial instruments are made in accordance with the requirements of IAS 32 “Financial Instruments: Disclosure and Presentation” and IAS 39 “Financial Instruments: Recognition and Measurement”. Fair value is defined as the amount at which the instrument could be exchanged in a current transaction between knowledgeable willing parties in an arm’s length transaction, other than in forced or liquidation sale. As no readily available market exists for a large part of the Bank’s financial instruments, judgment is necessary in arriving at fair value, based on current economic conditions and specific risks attributable to the instrument. The estimates presented herein are not necessarily indicative of the amounts the Bank could realize in a market exchange from the sale of its full holdings of a particular instrument.

As at 31 December 2003 and 2002 the following methods and assumptions were used by the Bank to estimate the fair value of each class of financial instruments for which it is practicable to estimate such value:

Cash and balances with the National Bank of Ukraine – For these short-term instruments the carrying amount is a reasonable estimate of fair value.

Loans and advances to banks – As at 31 December 2003 and 2002, the carrying amount of short-term deposits and advances given is a reasonable estimate of their fair value.

Loans and advances to customers – The fair value of the loan portfolio is based on the credit and interest rate characteristics of the individual loans within each sector of the portfolio. The estimation of the provision for loan losses includes consideration of risk premiums applicable to various types of loans based on factors such as the current situation of the economic sector in which each borrower operates, the economic situation of each borrower and guarantees obtained. Accordingly, the provision for loan losses is considered a reasonable estimate of the discount required to reflect the impact of credit risk.

Securities available-for-sale – As at 31 December 2003 and 2002 securities available-for-sale are non-marketable and are stated at cost, less allowance for impairment unless there are other appropriate and workable methods of reasonably estimating their fair value.

Deposits from banks – As at 31 December 2003 and 2002 the carrying amount of short-term deposits and deposits repayable on demand is a reasonable estimate of their fair value.

Loans from the National Bank of Ukraine – As at 31 December 2003 the carrying amount of short-term loans from the National Bank of Ukraine is a reasonable estimate of their fair value.

Customer accounts – As at 31 December 2003 and 2002 the carrying amount of deposits and current accounts of the Bank’s customers is a reasonable estimate of their fair value.

28. REGULATORY MATTERS

Quantitative measures established by regulation to ensure capital adequacy require the Bank to maintain minimum amounts and ratios (as set forth in the table below) of total and tier 1 capital to risk weighted assets.

The capital is calculated as the amount of restricted and free components of the shareholders’ capital and the Bank’s provisions for the principal risks on condition that the general provision for losses does not exceed 1.25% of the risk weighted assets.

The ratio was calculated according to the principles employed by the Basle Committee by applying the following risk estimates to the assets and off-balance sheet commitments net of allowances for losses:

Estimate	Description of position
0%	Cash and balances with the National Bank of Ukraine
0%	State debt securities in Hryvnias
20%	Loans and advances to banks for up to 1 year
100%	Loans and advances to customers
100%	Other assets
0%	Standby letters of credit secured by customer funds
50%	Other standby letters of credit and other transaction related contingent obligations and commitments on unused loans with the initial maturity of over 1 year
100%	Guarantees issued and similar commitments

The Bank's actual capital amounts and ratios are presented in the following table:

Capital amounts and ratios	Actual Amount in UAH thousand	For Capital Adequacy purposes Amount in UAH thousand	Ratio For Capital Adequacy purposes	Minimum Required Ratio
As at 31 December 2003				
Total capital	103,533	166,206	18%	8 %
Tier 1 capital	103,533	103,032	11%	4 %
As at 31 December 2002				
Total capital	76,583	80,820	20%	8 %
Tier 1 capital	76,583	75,470	19%	4 %

29. RISK MANAGEMENT POLICIES

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

The Bank manages the following risks:

Liquidity risk

Liquidity risk refers to the availability of sufficient funds to meet deposit withdrawals and other financial commitments associated with financial instruments as they actually fall due.

The Interbank Settlements Department controls these types of risks by means of maturity analysis, determining the Bank's strategy for the next financial period. Assets and Liabilities Committee approves the Bank's liquidity methodology. Current liquidity is managed by the Treasury Department, which trades on the currency markets for current liquidity support and cash flow optimization.

The following table presents an analysis of interest rate risk and liquidity risk on balance sheet. Interest bearing assets and liabilities generally have relatively short maturities and interest rates are reprised only at maturity.

2003

	Up to 1 month	1 to 3 months	3 month to 1 year	1 year to 5 years	Over 5 years	Overdue	Maturity undefined (including allowance for losses and impairment)	Total
ASSETS								
Interest bearing assets:								
Loans and advances to banks, less allowance for loan losses	84,228	500	1,500	-	-	-	(818)	85,410
Securities available-for-sale, less allowance for impairment	-	-	2,365	-	-	-	(71)	2,294
Loans and advances to customers, less allowance for loan losses	195,892	55,902	325,366	131,214	-	18,796	(23,247)	703,923
Total interest bearing assets	280,120	56,402	329,231	131,214	-	18,796	(24,136)	791,627
Cash and balances with the National Bank of Ukraine	67,483	-	-	-	-	-	47,930	115,413
Advances to banks	64,737	-	-	-	-	-	-	64,737
Securities available-for-sale, less allowance for impairment	-	-	-	8,715	-	-	(824)	7,891
Interests accrued on interest earning assets	26,297	-	-	-	-	4,558	(6,172)	24,683
Fixed and intangible assets, less accumulated depreciation	-	-	-	30,586	30,799	-	-	61,385
Goodwill, less accumulated amortization	-	-	-	502	-	-	-	502
Other assets, less allowance for losses	5,304	-	-	-	-	-	(347)	4,957
TOTAL ASSETS	443,941	56,402	329,231	171,017	30,799	23,354	16,451	1,071,195
LIABILITIES								
Interest bearing liabilities:								
Deposits from banks	34,423	2,775	7,997	-	-	-	-	45,195
Loans from the National Bank of Ukraine	-	5,460	13,880	-	-	-	-	19,340
Customer accounts	115,052	123,361	356,007	10,064	-	-	-	604,484
Total interest bearing liabilities	149,475	131,596	377,884	10,064	-	-	-	669,019
Deposits from banks	22,274	-	-	-	-	-	-	22,274
Customer accounts	266,124	-	-	-	-	-	-	266,124
Interest accrued on interest bearing liabilities	6,332	-	-	-	-	-	-	6,332
Deferred tax liability	-	-	982	-	-	-	-	982
Other liabilities	2,117	-	-	-	-	-	814	2,931
TOTAL LIABILITIES	446,322	131,596	378,866	10,064	-	-	814	967,662
Liquidity gap	(2,381)	(75,194)	(49,635)	160,953	30,799			
Interest sensitivity gap	130,645	(75,194)	(48,653)	121,150	-			
Cumulative interest sensitivity gap	130,645	55,451	6,798	127,948	127,948			
Cumulative interest sensitivity gap as a percentage of total assets	12%	5%	1%	12%	12%			

	Up to 1 month	1 to 3 months	3 months to 1 year	1 year to 5 years	Over 5 years	Overdue	Maturity undefined (including allowance for losses and impairment)	2002 Total
ASSETS								
Interest bearing assets:								
Loans and advances to banks, less allowance for loan losses	39,529	-	4,341	-	-	-	(381)	43,489
Securities available-for-sale	84	-	-	-	-	-	-	84
Loans and advances to customers, less allowance for loan losses	26,124	28,720	167,861	37,630	-	32,934	(19,983)	273,286
Total interest bearing assets	65,737	28,720	172,202	37,630	-	32,934	(20,364)	316,859
Cash and balances with the National Bank of Ukraine	9,287	-	-	-	-	-	22,702	31,989
Advances to banks	12,173	-	-	-	-	-	-	12,173
Securities available-for-sale	-	-	-	4,379	-	-	(516)	3,863
Interest accrued on interest earning assets	12,118	-	-	-	-	6,821	(7,136)	11,803
Fixed assets, less accumulated depreciation	-	-	-	15,019	26,875	-	-	41,894
Goodwill, less accumulated amortization	-	-	-	836	-	-	-	836
Other assets, less allowance for losses	2,732	-	-	605	-	-	(142)	3,195
TOTAL ASSETS	102,047	28,720	172,202	58,469	26,875	39,755	(5,456)	422,612
LIABILITIES								
Interest bearing liabilities:								
Deposits from banks	21,419	12,851	-	-	-	-	-	34,270
Customer accounts	66,456	5,112	84,341	11,927	-	-	-	167,836
Total interest bearing liabilities	87,875	17,963	84,341	11,927	-	-	-	202,106
Deposits from banks	6,596	-	-	-	-	-	-	6,596
Customers accounts	132,628	-	-	-	-	-	-	132,628
Interest accrued on interest bearing liabilities	2,584	-	-	-	-	-	-	2,584
Other liabilities	1,876	-	-	-	-	-	239	2,115
TOTAL LIABILITIES	231,559	17,963	84,341	11,927	-	-	239	346,029
Liquidity gap	(129,512)	10,757	87,861	46,542	26,875			
Interest Rate Sensitivity Gap	(22,138)	10,757	87,861	25,703	-			
Cumulative Interest Rate Sensitivity Gap	(22, 138)	(11,381)	76,480	102,183	102,183			
Cumulative Interest Rate Sensitivity Gap as a Percentage of Total Assets	(5%)	(3%)	18%	24%	24%			

The majority of the Bank's interest earning assets and interest bearing liabilities are at fixed rates of interest.

The maturity of the loan portfolio as presented above shows the remaining period from the balance sheet date to the contractual maturity. Long-term loans are generally not available in Ukraine, however many short-term loans are granted with the expectation of renewing the loans at maturity. Accordingly, the effective maturity of the loan portfolio may be longer than indicated by the analysis based on the contractual terms.

Interest rate risk

Interest rate risk arises from the possibility that changes in interest rates will affect the value of the financial instruments. The following table presents an analysis of interest rate risk and thus the potential of the Bank for gain or loss. Effective interest rates are presented by categories of financial assets and liabilities to determine interest rate exposure and effectiveness of the interest rate policy used by the Bank.

The Risk and Loan Analysis Department and Assets and Liabilities Committee consider the liabilities' costs and the assets' profitability, maturity correspondence of assets and liabilities. The Assets and Liabilities Committee establishes the interest margin policy of the Bank. The Bank's Finance and Budgeting Department monitors the current financial position of the Bank, and estimates the Bank's sensitivity to changes in interest rates and its influence on the Bank's profitability.

	UAH	USD	EUR	2003 Non-convertible currencies	UAH	USD	EUR	2002 Non-convertible currencies
ASSETS								
Loans and advances to banks	14%	2%	5%	4%	5%	2%	4%	10%
Loans and advances to customers	21%	15%	15%	22%	27%	16%	18%	20%
Available-for-sale securities	18%	-	-	-	-	-	-	-
LIABILITIES								
Deposits from banks	11%	7%	6%	3%	10%	5%	5%	-
Loans from the National Bank of Ukraine	8.7%	-	-	-	-	-	-	-
Customer accounts	12%	9%	11%	-	13%	9%	5%	-

The majority of the Bank's loan contracts and other financial assets and liabilities that bear interest are fixed interest rate. The Bank monitors its interest rate margin and consequently does not consider itself exposed to significant interest rate risk or consequential cash flow risk.

Currency risk

Currency risk is defined as the risk that the value of a financial instrument will fluctuate due to changes in foreign exchange rates. The Bank is exposed to effects of fluctuation in the prevailing foreign currency exchange rates on its financial position and cash flows. The Interbank Settlements Department constantly evaluates the risk of losses from significant currency rates fluctuations. The Bank has set limits for open currency position in order to minimize the currency risk. The Interbank Settlements Department performs monitoring of the Bank's open currency position on daily basis with the aim to meet the requirements of the National Bank of Ukraine. The Treasury Department trades on the interbank currency markets. The Bank's exposure to foreign currency exchange rate risk is presented in the table below:

2003

	UAH	USD (1 USD = UAH 5.3315)	EUR (1 EUR = UAH 6.6622)	Other currency	Allowance for losses and impairment	Total
ASSETS						
Cash and balances with the National Bank of Ukraine	99,606	13,281	2,395	131	-	115,413
Loans and advances to banks, less allowance for loan losses	92,564	49,048	7,219	2,230	(818)	150,243
Securities available-for-sale, less allowance for impairment	11,080	-	-	-	(895)	10,185
Loans and advances to customers, less allowance for loan losses	568,759	175,172	13,858	140	(29,419)	728,510
Fixed assets, less accumulated depreciation	61,385	-	-	-	-	61,385
Goodwill, less accumulated amortization	502	-	-	-	-	502
Other assets, less allowance for losses	5,304	-	-	-	(347)	4,957
TOTAL ASSETS	839,200	237,501	23,472	2,501	(31,479)	1,071,195
LIABILITIES						
Deposits from banks	48,142	19,328	-	-	-	67,470
Loans from the National Bank of Ukraine	19,340	-	-	-	-	19,340
Customer accounts	667,901	185,003	22,808	1,227	-	876,939
Deferred tax liability	982	-	-	-	-	982
Other liabilities	2,015	60	40	2	814	2,931
TOTAL LIABILITIES	738,380	204,391	22,848	1,229	814	967,662
OPEN BALANCE SHEET POSITION						
	100,820	33,110	624	1,272		

2002

	UAH	USD (1 USD = UAH 5.3324)	EUR (1 EUR = UAH 5.5329)	Other currency	Allowance for losses and impairment	Total
ASSETS						
Cash and balances with the National Bank of Ukraine	25,935	5,318	680	56	-	31,989
Loans and advances to banks, less allowance for loan losses	36,203	18,670	779	397	(381)	55,668
Securities available-for-sale, less allowance for impairment	4,463	-	-	-	(516)	3,947
Loans and advances to customers, less allowance for loan losses	189,950	108,683	13,549	20	(27,119)	285,083
Fixed assets, less accumulated depreciation	41,894	-	-	-	-	41,894
Goodwill, less accumulated amortization	836	-	-	-	-	836
Other assets, less allowance for losses	2,442	895	-	-	(142)	3,195
TOTAL ASSETS	301,723	133,566	15,008	473	(28,158)	422,612
LIABILITIES						
Deposits from banks	4,419	36,482	-	-	-	40,901
Customer accounts	222,450	57,499	22,939	125	-	303,013
Other liabilities	1,395	481	-	-	239	2,115
TOTAL LIABILITIES	228,264	94,462	22,939	125	239	346,029
OPEN BALANCE SHEET POSITION						
	73,459	39,104	(7,931)	348		

The Bank's principal cash flows (revenues, operating expenses) are largely generated in Ukrainian Hryvnias. As a result, future movements in the exchange rate between the Ukrainian Hryvnias and US dollar/Euro may affect the carrying value of the Bank's monetary assets and liabilities. Such changes may also affect the Bank's ability to invest in non-monetary assets as measured in US dollars in these financial statements.

Credit risk

The Bank is exposed to credit risk which is the risk that one party to a financial instrument will fail to discharge an obligation and cause the other party to incur a financial loss.

Risk management is performed by the Credit Committee, the Risk and Loan Analysis Department and the Loan Department of the Bank. Based upon information prepared by the Risk and Loan Analysis Department and the Loan Department, the Credit Committee approves borrower's limits, makes decisions on disbursing, and considers the possibility of loans prolongation. The Risk and Loan Analysis Department performs the analysis of loan portfolio, evaluates loans in order to provide for loan losses on a monthly basis and prepares all necessary documentation for approval of all above mentioned decisions by the Credit Committee of the Bank.

Where appropriate, and in the case of most loans, the Bank obtains collateral and corporate and personal guaranties but some portion is personal lending, where no such facilities can be obtained. Such risks are monitored on a continuous basis and subject to annual or more frequent reviews.

Commitments to extend credit represent unused portions of credit in the form of loans, guarantees or letters of credit. The credit risk on off-balance sheet financial instruments is defined as a probability of losses due to inability of the counterparty to comply with the contractual terms and conditions. With respect to credit risk on commitments to extend credit, the Bank is potentially exposed to loss in an amount equal to the total unused commitments. However, the likely amount of loss is less than the total unused commitments since most commitments to extend credit are contingent upon customers maintaining specific credit standards. The Bank applies the same credit policy to the contingent liabilities as it does to the balance sheet financial instruments, i.e. the one based on the procedures for approving the grant of loans, using limits to mitigate the risk, and current monitoring. 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.

Geographical concentration

The geographical concentration of assets and liabilities is set out below:

	2003				
	Ukraine	Other CIS countries	OECD countries	Allowance for losses and impairment	Total
Cash and balances with the National Bank of Ukraine	115,413	-	-	-	115,413
Loans and advances to banks, less allowance for loan losses	102,963	1,418	46,680	(818)	150,243
Securities available-for-sale, less allowance for impairment	11,080	-	-	(895)	10,185
Loans and advances to customers, less allowance for loan losses	757,929	-	-	(29,419)	728,510
Fixed assets, less accumulated depreciation	61,385	-	-	-	61,385
Goodwill, less accumulated amortization	502	-	-	-	502
Other assets, less allowance for losses	5,304	-	-	(347)	4,957
TOTAL ASSETS	1,054,576	1,418	46,680	(31,479)	1,071,195
LIABILITIES					
Deposits from banks	67,465	-	5	-	67,470
Loans from the National Bank of Ukraine	19,340	-	-	-	19,340
Customer accounts	876,939	-	-	-	876,939
Deferred tax liability	982	-	-	-	982
Other liabilities	2,117	-	-	814	2,931
TOTAL LIABILITIES	966,843	-	5	814	967,662
NET BALANCE SHEET POSITION	87,733	1,418	46,675		
					2002
	Ukraine	Other CIS countries	OECD countries	Allowance for losses and impairment	Total
Cash and balances with the National Bank of Ukraine	31,989	-	-	-	31,989
Loans and advances to banks, less allowance for loan losses	44,750	396	10,903	(381)	55,668
Securities available-for-sale, less allowance for impairment losses	3,947	-	-	-	3,947
Loans and advances to customers, less allowance for loan losses	312,202	-	-	(27,119)	285,083
Fixed assets, less accumulated depreciation	41,894	-	-	-	41,894
Goodwill, less accumulated amortization	836	-	-	-	836
Other assets, less allowance for losses	3,337	-	-	(142)	3,195
TOTAL ASSETS	438,955	396	10,903	(27,642)	422,612
LIABILITIES					
Deposits from banks	40,901	-	-	-	40,901
Customer accounts	303,013	-	-	-	303,013
Other liabilities	1,876	-	-	239	2,115
TOTAL LIABILITIES	345,790	-	-	239	346,029
NET BALANCE SHEET POSITION	93,165	396	10,903		