

BANK PIVDENNYI

Financial Statements and Auditors' Report

31 December 2005

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AUDITORS' REPORT

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AUDITORS' REPORT

To the Shareholders and Board of Directors of Bank Pivdennyi:

- 1 We have audited the accompanying balance sheet of Bank Pivdennyi (the "Bank") as at 31 December 2005, and the related statements of income, cash flows and changes in equity for the year then ended. These financial statements set out on pages 1 to 42 are the responsibility of the Bank's Management. Our responsibility is to express an opinion on these financial statements based on our audit.
- 2 We conducted our audit in accordance with International Standards on Auditing. Those Standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by Management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.
- 3 In our opinion, the accompanying financial statements present fairly, in all material respects, the financial position of the Bank as of 31 December 2005 and the results of its operations and its cash flows for the year then ended in accordance with International Financial Reporting Standards.

PricewaterhouseCoopers

Kyiv, Ukraine
28 April 2006

Auditor L. Pakhucha
Audit certificate # 0000025 issued by the National Bank of Ukraine



Bank Pivdennyi
Balance Sheet

	Note	31 December 2005	31 December 2004
<i>In thousands of Ukrainian hryvnias</i>			
ASSETS			
Cash and cash equivalents and mandatory reserve balances	7	263,781	191,714
Trading securities	8	8,346	-
Other securities at fair value through profit or loss	9	10,215	18,740
Due from other banks	10	38,934	82,409
Loans and advances to customers	11	1,642,667	1,196,139
Investment securities available for sale	12	62,542	6,476
Guarantee deposits with the National Bank of Ukraine		-	29,738
Deferred income tax asset	22	-	2,562
Intangible assets	13	1,807	788
Premises and equipment	13	165,603	52,898
Other assets		4,603	4,303
TOTAL ASSETS		2,198,498	1,585,767
LIABILITIES			
Due to the National Bank of Ukraine		-	41,333
Due to other banks	14	300,194	291,312
Customer accounts	15	1,600,063	1,061,343
Debt securities in issue		27,170	23,571
Subordinated debt	16	7,747	-
Current income tax liability		548	355
Deferred income tax liability	22	6,390	-
Other liabilities	17	5,052	8,454
TOTAL LIABILITIES		1,947,164	1,426,368
EQUITY			
Share capital	18	208,896	148,898
Revaluation reserve for premises		26,348	-
Retained earnings		16,090	10,501
TOTAL EQUITY		251,334	159,399
TOTAL LIABILITIES AND EQUITY		2,198,498	1,585,767

Approved for issue and signed on behalf of the Board of Directors on 28 April 2006.

Vadim V. Morokhovskiy
Chairman of the Board



Ludmila V. Kovalenok
Chief Accountant

Bank Pivdennyi
Income Statement

<i>In thousands of Ukrainian hryvnias</i>	Note	2005	2004
Interest income	19	237,783	198,286
Interest expense	19	(137,331)	(111,716)
Net interest income		100,452	86,570
Provision for loan impairment	10, 11	(20,735)	(16,925)
Net interest income after provision for loan impairment		79,717	69,645
Gains less losses from trading securities		4,598	-
Gains less losses from other securities at fair value through profit or loss		232	4,435
Gains less losses from trading in foreign currencies		19,503	11,021
Foreign exchange translation (losses less gains)/gains less losses		(4,920)	42
Fee and commission income	20	50,873	38,867
Fee and commission expense	20	(5,634)	(4,035)
Losses on initial recognition of assets at rates below market	11	(3,059)	(7,653)
Gains on initial recognition of liabilities at rates below market	15	-	3,051
Recovery of/(provision) for impairment of investment securities available for sale	12	347	(3,172)
Recovery of/(provision) for losses on credit related commitments	24	674	(1,434)
Other operating income		752	419
Operating income		143,083	111,186
Administrative and other operating expenses	21	(105,443)	(77,689)
Profit before tax		37,640	33,497
Income tax expense	22	(8,959)	(10,495)
Profit for the year		28,681	23,002

Bank Pivdennyi
Statement of Changes in Equity

	Note	Share capital	Revaluation reserve for premises	Retained earnings	Total
<i>In thousands of Ukrainian hryvnias</i>					
Balance at 31 December 2003		108,898	-	9,920	118,818
Profit for the year		-	-	23,002	23,002
Total recognised income for 2004		-	-	23,002	23,002
Share issue		26,000	-	-	26,000
Dividends capitalised		14,000	-	(14,000)	-
Distributed profit	18	-	-	(11,228)	(11,228)
Income tax recorded in equity		-	-	2,807	2,807
Balance at 31 December 2004		148,898	-	10,501	159,399
Premises and equipment:					
- Revaluation	13	-	35,131	-	35,131
Income tax recorded in equity		-	(8,783)	-	(8,783)
Net income recognised directly in equity		-	26,348	-	26,348
Profit for the year		-	-	28,681	28,681
Total recognised income for 2005		-	26,348	28,681	55,029
Share issue		43,500	-	-	43,500
Dividends capitalised		16,498	-	(16,498)	-
Distributed profit	18	-	-	(8,792)	(8,792)
Income tax recorded in equity		-	-	2,198	2,198
Balance at 31 December 2005		208,896	26,348	16,090	251,334

Bank Pivdennyi
Statement of Cash Flows

<i>In thousands of Ukrainian hryvnias</i>	Note	2005	2004
Cash flows from operating activities			
Interest received		236,952	197,299
Interest paid		(132,625)	(99,341)
Income received from trading in trading securities		2,785	-
Income received from trading in foreign currencies		19,503	11,021
Fees and commissions received		50,873	38,867
Fees and commissions paid		(5,634)	(4,035)
Other operating income received		751	419
Staff costs paid		(46,842)	(31,724)
Administrative and other operating expenses paid		(45,079)	(37,417)
Income tax paid		(6,399)	(9,117)
Cash flows from operating activities before changes in operating assets and liabilities		74,285	65,972
Changes in operating assets and liabilities			
Net increase in mandatory cash balances with the National Bank of Ukraine		(53,056)	(10,337)
Net increase in trading securities		(6,533)	-
Net decrease/(increase) in other securities at fair value through profit or loss		8,525	(10,874)
Net decrease/(increase) in due from other banks		42,281	(57,537)
Net increase in loans and advances to customers		(466,945)	(269,728)
Net decrease/(increase) in guarantee deposits with the National Bank of Ukraine		29,738	(29,738)
Net increase in other assets		(982)	(1,275)
Net (decrease)/increase in due to the National Bank of Ukraine		(41,219)	24,933
Net increase in due to other banks		13,085	183,265
Net increase in customer accounts		521,013	160,928
Net increase in debt securities in issue		3,910	6,875
Net decrease in other liabilities		(2,728)	(1,371)
Net cash from operating activities		121,374	61,113
Cash flows from investing activities			
Acquisition of investment securities available for sale	12	(92,793)	(530)
Proceeds from disposal of investment securities available for sale	12	37,074	15,100
Acquisition of premises and equipment	13	(87,527)	(19,262)
Proceeds from disposal of premises and equipment		166	228
Acquisition of intangible assets	13	(1,260)	(822)
Net cash used in investing activities		(144,340)	(5,286)
Cash flows from financing activities			
Issue of ordinary shares		43,500	26,000
Net increase/(decrease) in subordinated debt		7,747	(11,196)
Capital distributions to shareholders other than dividends		(8,792)	(11,228)
Net cash from financing activities		42,455	3,576
Effect of exchange rate changes on cash and cash equivalents		(478)	720
Net increase in cash and cash equivalents		19,011	60,123
Cash and cash equivalents at the beginning of the year		120,513	60,390
Cash and cash equivalents at the end of the year	7	139,524	120,513

1 Introduction

Bank Pivdennyi (the "Bank") was founded in 1993 as a closed-type joint stock entity. The Bank is registered in Ukraine to carry out banking and foreign exchange activities and operates under a banking license issued by the National Bank of Ukraine ("NBU"). The Bank's principal business activity is commercial and retail banking operations within Ukraine. As at 31 December 2005 major shareholders of the Bank are six Ukrainian companies and eleven individuals which collectively own over 61% and over 37% of the outstanding shares, respectively (31 December 2004: six Ukrainian companies and eleven individuals owned over 61% and 37% of the outstanding shares, respectively). The ultimate beneficial owners of the Bank as at 31 December 2005 were 2 individuals: Mr Rodin Y.O. and Mr Bekker M.I.

The Bank has 14 (2004: 13) branches within Ukraine.

Registered address and place of business. The Bank's registered address is:

2, Sabanskyi lane
65014 Odesa,
Ukraine

Presentation currency. These financial statements are presented in thousands of Ukrainian hryvnias ("UAH thousands").

2 Operating Environment of the Bank

Whilst there have been improvements in economic trends in the country, Ukraine continues to display certain characteristics of an emerging market. These characteristics include, but are not limited to, the existence of a currency that is not freely convertible outside of Ukraine, restrictive currency controls, and inflation of 10.3% for 2005 (2004: 12.3%). The tax, currency and customs legislation within Ukraine is subject to varying interpretations and changes, which can occur frequently.

The future economic direction of Ukraine is largely dependent upon the effectiveness of economic, financial and monetary measures undertaken by the Government, together with tax, legal, regulatory, and political developments.

The banking sector in Ukraine is particularly sensitive to adverse fluctuations in confidence and economic conditions. Furthermore, the need for further developments in the anti-money laundering legislation, bankruptcy laws, formalised procedures for the registration and enforcement of collateral, and other legal and fiscal impediments contribute to the difficulties experienced by banks currently operating in Ukraine.

In addition, economic conditions continue to limit the volume of activity in the financial markets. Market quotations in generally illiquid markets may not be reflective of the values for financial instruments, which would be determined in an efficient, active market involving many willing buyers and willing sellers.

3 Basis of Preparation and Significant Accounting Policies

Basis of Preparation. These financial statements have been prepared in accordance with International Financial Reporting Standards ("IFRS") under the historical cost convention, as modified by the revaluation of premises, available-for-sale financial assets, and financial instruments categorised as at fair value through profit or loss. The principal accounting policies applied in the preparation of these financial statements are set out below. These policies have been consistently applied to all the periods presented, unless otherwise stated (refer to Note 5, Adoption of New or Revised Standards and Interpretations).

Key measurement terms. Depending on their classification financial instruments are carried at cost, fair value, or amortised cost as described below.

Cost is the amount of cash or cash equivalents paid or the fair value of the other consideration given to acquire an asset at the time of its acquisition and includes *transaction costs*. *Transaction costs* are incremental costs that are directly attributable to the acquisition, issue or disposal of a financial instrument. An incremental cost is one that would not have been incurred if the transaction had not taken place. Transaction costs include fees and commissions paid to agents (including employees acting as selling agents), advisors, brokers and dealers, levies by regulatory agencies and securities exchanges, and transfer taxes and duties. Transaction costs do not include debt premiums or discounts, financing costs or internal administrative or holding costs.

3 Basis of Preparation and Significant Accounting Policies (Continued)

Fair value is the amount for which an asset could be exchanged, or a liability settled, between knowledgeable, willing parties in an arm's length transaction. Fair value is the current bid price for financial assets and current asking price for financial liabilities which are quoted in an active market. For assets and liabilities with offsetting market risks, the Bank may use mid-market prices as a basis for establishing fair values for the offsetting risk positions and apply the bid or asking price to the net open position as appropriate. A financial instrument is regarded as quoted in an active market if quoted prices are readily and regularly available from an exchange or other institution and those prices represent actual and regularly occurring market transactions on an arm's length basis.

In other than active markets, the most recent arms length transactions are the basis of current fair values. Recent transaction prices are appropriately adjusted if they do not reflect current fair values, for example because the transaction was a distress sale. Fair value is not the amount that an entity would receive or pay in a forced transaction, involuntary liquidation or distress sale.

Valuation techniques such as discounted cash flows models and consideration of financial data of the investees are used to fair value certain financial instruments for which external market pricing information is not available. Valuation techniques may require assumptions not supported by observable market data. Disclosures are made in these financial statements if changing any such assumptions to a reasonably possible alternative would result in significantly different profit, income, total assets or total liabilities.

Amortised cost is the amount at which the financial instrument was recognised at initial recognition less any principal repayments, plus accrued interest, and for financial assets less any write-down for incurred impairment losses. Accrued interest includes amortisation of transaction costs deferred at initial recognition and of any premium or discount to maturity amount using the effective interest method. Accrued interest income and accrued interest expense, including both accrued coupon and amortised discount, are not presented separately and are included in the carrying values of related balance sheet items.

The effective interest method is a method of allocating interest income or interest expense over the relevant period so as to achieve a constant periodic rate of interest (effective interest rate) on the carrying amount. The effective interest rate is the rate that exactly discounts estimated future cash payments or receipts (excluding future credit losses) through the expected life of the financial instrument or a shorter period, if appropriate, to the net carrying amount of the financial instrument. The effective interest rate discounts cash flows of variable interest instruments to the next interest repricing date except for the premium or discount which reflects the credit spread over the floating rate specified in the instrument, or other variables that are not reset to market rates. Such premiums or discounts are amortised over the whole expected life of the instrument. The present value calculation includes all fees and points paid or received between parties to the contract that are an integral part of the effective interest rate (refer to income and expense recognition policy).

Initial recognition of financial instruments. Trading securities and other securities at fair value through profit or loss are initially recorded at fair value. All other financial instruments are initially recorded at fair value plus transaction costs. Fair value at initial recognition is best evidenced by the transaction price. A gain or loss on initial recognition is only recorded if there is a difference between fair value and transaction price which can be evidenced by other observable current market transactions in the same instrument or by a valuation technique whose inputs include only data from observable markets.

All purchases and sales of financial instruments that require delivery within the time frame established by regulation or market convention ("regular way" purchases and sales) are recorded at trade date, which is the date that the Bank commits to deliver a financial instrument. All other purchases and sales are recognised on the settlement date with the change in value between the commitment date and settlement date not recognised for assets carried at cost or amortised cost; recognised in profit or loss for trading securities and other securities at fair value through profit or loss; and recognised in equity for assets classified as available for sale.

Cash and cash equivalents. Cash and cash equivalents are items which can be converted into cash at short notice and which are subject to an insignificant risk of changes in value. All short term interbank placements, beyond overnight placements, are included in due from other banks. Amounts, which relate to funds that are of a restricted nature, are excluded from cash and cash equivalents. Cash and cash equivalents are carried at amortised cost.

Mandatory reserve balances. Mandatory reserve balances are carried at amortised cost and represent non-interest bearing mandatory reserve assets which are not available to finance the Bank's day to day operations and hence are not considered as part of cash and cash equivalents for the purposes of the cash flow statement.

3 Basis of Preparation and Significant Accounting Policies (Continued)

Trading securities. Trading securities are securities, which are either acquired for generating a profit from short-term fluctuations in price or trader's margin, or are securities included in a portfolio in which a pattern of short-term trading exists. The Bank classifies securities into trading securities if it has an intention to sell them within a short period after purchase, i.e. within 3 months. Trading securities are not reclassified out of this category even when the Bank's intentions subsequently change.

Trading securities are carried at fair value. Interest earned on trading securities calculated using the effective interest method is presented in the income statement as interest income. Dividends are included in dividend income within other operating income when the Bank's right to receive the dividend payment is established. All other elements of the changes in the fair value and gains or losses on derecognition are recorded in profit or loss as gains less losses from trading securities in the period in which they arise.

Other securities at fair value through profit or loss. Other securities at fair value through profit or loss are securities designated irrevocably, at initial recognition, into this category. Recognition and measurement of this category of financial assets is consistent with the above policy for trading securities.

Due from other banks. Amounts due from other banks are recorded when the Bank advances money to counterparty banks with no intention of trading the resulting unquoted non-derivative receivable due on fixed or determinable dates. Amounts due from other banks are carried at amortised cost.

Loans and advances to customers. Loans and advances to customers are recorded when the Bank advances money to purchase or originate an unquoted non-derivative receivable from a customer due on fixed or determinable dates and has no intention of trading the receivable. Loans and advances to customers are carried at amortised cost.

Impairment of financial assets carried at amortised cost. Impairment losses are recognised in profit or loss when incurred as a result of one or more events ("loss events") that occurred after the initial recognition of the financial asset and which have an impact on the amount or timing of the estimated future cash flows of the financial asset or group of financial assets that can be reliably estimated. If the Bank determines that no objective evidence exists that impairment was incurred for an individually assessed financial asset, whether significant or not, it includes the asset in a group of financial assets with similar credit risk characteristics and collectively assesses them for impairment.

For the purposes of a collective evaluation of impairment, financial assets are grouped on the basis of similar credit risk characteristics. Those characteristics are relevant to the estimation of future cash flows for groups of such assets by being indicative of the debtors' ability to pay all amounts due according to the contractual terms of the assets being evaluated.

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 and the experience of management in respect of the extent to which amounts will become overdue as a result of past loss events and the success of recovery of overdue amounts. Past experience is adjusted on the basis of current observable data to reflect the effects of current conditions that did not affect past periods and to remove the effects of past conditions that do not exist currently.

Impairment losses are recognised through an allowance account to write down the asset's carrying amount to the present value of expected cash flows (which exclude future credit losses that have not been incurred) discounted at the effective interest rate of the asset. 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 foreclosure is probable.

If, in a subsequent period, the amount of the impairment loss decreases and the decrease can be related objectively to an event occurring after the impairment was recognised (such as an improvement in the debtor's credit rating), the previously recognised impairment loss is reversed by adjusting the allowance account through profit or loss.

Uncollectable assets are written off against the related impairment loss provision after all the necessary procedures to recover the asset have been completed and the amount of the loss has been determined.

Investment securities available for sale. This classification includes investment securities which the Bank intends to hold for an indefinite period of time and which may be sold in response to needs for liquidity or changes in interest rates, exchange rates or equity prices. The Bank classifies investments as available for sale at the time of purchase and reassesses that classification at each subsequent balance sheet date.

Investment securities available for sale are carried at fair value. Interest income on available for sale debt securities is calculated using the effective interest method and recognised in profit or loss. Dividends on available-for-sale equity instruments are recognised in profit or loss when the Bank's right to receive payment is established. All other elements of changes in the fair value are deferred in equity until the investment is derecognised or impaired, at which time the cumulative gain or loss is removed from equity to profit or loss.

3 Basis of Preparation and Significant Accounting Policies (Continued)

Impairment losses are recognised in profit or loss when incurred as a result of one or more events (“loss events”) that occurred after the initial recognition of investment securities available for sale. A significant or prolonged decline in the fair value of an equity security below its cost is an indicator that it is impaired. The cumulative impairment loss – measured as the difference between the acquisition cost and the current fair value, less any impairment loss on that asset previously recognised in profit or loss – is removed from equity and recognised in profit or loss. Impairment losses on equity instruments are not reversed through profit or loss. If, in a subsequent period, the fair value of a debt instrument classified as available for sale increases and the increase can be objectively related to an event occurring after the impairment loss was recognised in profit or loss, the impairment loss is reversed through current period’s profit or loss.

Sale and repurchase agreements. Sale and repurchase agreements (“repo agreements”) are treated as secured financing transactions. Securities purchased under agreements to resell (“reverse repo agreements”) are recorded as due from other banks or loans and advances to customers, as appropriate. The difference between the sale and repurchase price is treated as interest income and accrued over the life of repo agreements using the effective interest method.

Derecognition of financial assets. The Bank derecognises financial assets when (i) the assets are redeemed or the rights to cash flows from the assets otherwise expired or (ii) the Bank has transferred substantially all the risks and rewards of ownership of the assets or (iii) the Bank has neither transferred nor retained substantially all risks and rewards of ownership but has not retained control. Control is retained if the counterparty does not have the practical ability to sell the asset in its entirety to an unrelated third party without needing to impose additional restrictions on the sale.

Premises and equipment. Premises and equipment are stated at cost, restated to the equivalent purchasing power of the Ukrainian hryvnia at 31 December 2000 for assets acquired prior to 1 January 2001, or revalued amounts, as described below, less accumulated depreciation and provision for impairment, where required.

Premises of the Bank are subject to revaluation on a regular basis. The frequency of revaluation depends upon the movements in the fair values of the premises being revalued. The revaluation reserve for premises included in equity is transferred directly to retained earnings when the surplus is realised, ie on the retirement or disposal of the asset.

Premises have been revalued to market value at 31 December 2005. The revaluation was performed based on the reports of independent appraiser, who hold a recognised and relevant professional qualification and who have recent experience in valuation of assets of similar location and category. The basis used for the appraisal was market value.

Construction in progress is carried at cost, restated to the equivalent purchasing power of the Ukrainian hryvnia at 31 December 2000 for assets acquired prior to 1 January 2001, less provision for impairment where required. Upon completion, assets are transferred to premises at their carrying amount. Construction in progress is not depreciated until the asset is available for use.

Costs of minor repairs and maintenance are expensed when incurred. Cost of replacing major parts or components of premises and equipment items are capitalised and the replaced part is retired.

If impaired, premises and equipment are written down to the higher of their value in use and fair value less costs to sell. The decrease in carrying amount is charged to profit or loss to the extent it exceeds the previous revaluation surplus in equity. An impairment loss recognised for an asset in prior years is reversed if there has been a change in the estimates used to determine the asset’s value in use or fair value less costs to sell.

Gains and losses on disposals determined by comparing proceeds with carrying amount are recognised in profit or loss.

Depreciation. Depreciation of premises and equipment is calculated using the straight-line method to allocate their cost or revalued amounts to their residual values over their estimated useful lives on the following basis (in years):

Premises	20;
Furniture and equipment	5;
Motor vehicles	5;
Computers	4;and
Other	1-7.

The residual value of an asset is the estimated amount that the Bank would currently obtain from disposal of the asset less the estimated costs of disposal, if the asset were already of the age and in the condition expected at the end of its useful life. The residual value of an asset is nil if the Bank expects to use the asset until the end of its physical life. The assets’ residual values and useful lives are reviewed, and adjusted if appropriate, at each balance sheet date.

3 Basis of Preparation and Significant Accounting Policies (Continued)

Intangible assets. All of the Bank's intangible assets have definite useful life and primarily include capitalised computer software.

Acquired computer software licenses are capitalised on the basis of the costs incurred to acquire and bring to use the specific software. Development costs that are directly associated with identifiable and unique software controlled by the Bank are recorded as intangible assets if inflow of incremental economic benefits exceeding costs is probable. Capitalised costs include staff costs of the software development team and an appropriate portion of relevant overheads. All other costs associated with computer software, eg its maintenance, are expensed when incurred. Capitalised computer software is amortised on a straight line basis over expected useful lives of 2 to 10 years.

Operating leases. Where the Bank is a lessee in a lease which does not transfer substantially all the risks and rewards incidental to ownership from the lessor to the Bank, the total lease payments, including those on expected termination, are charged to profit or loss on a straight-line basis over the period of the lease.

Due to other banks. Amounts due to other banks are recorded when money or other assets are advanced to the Bank by counterparty banks. The non-derivative liability is carried at amortised cost. If the Bank purchases its own debt, it is removed from the balance sheet and the difference between the carrying amount of the liability and the consideration paid is included in gains or losses arising from retirement of debt.

Customer accounts. Customer accounts are non-derivative liabilities to individuals, state or corporate customers and are carried at amortised cost.

Debt securities in issue. Debt securities in issue include certificates of deposits issued by the Bank. Debt securities are stated at amortised cost. If the Bank purchases its own debt securities in issue, they are removed from the balance sheet and the difference between the carrying amount of the liability and the consideration paid is included in gains arising from retirement of debt.

Subordinated debt. Subordinated debt represents long-term borrowing agreements that, in case of the Bank's default, would be secondary to the Bank's primary debt obligations. Subordinated debt is carried at amortised cost.

Income taxes. Income taxes have been provided for in the financial statements in accordance with Ukrainian legislation enacted or substantively enacted by the balance sheet date. The income tax charge comprises current tax and deferred tax and is recognised in the income statement except if it is recognised directly in equity because it relates to transactions that are also recognised, in the same or a different period, directly in equity.

Current tax is the amount expected to be paid to or recovered from the taxation authorities in respect of taxable profits or losses for the current and prior periods. Taxable profits or losses are based on estimates if financial statements are authorised prior to filing relevant tax returns. Taxes, other than on income, are recorded within administrative and other operating expenses.

Deferred income tax is provided using the balance sheet liability method for tax loss carry forwards and temporary differences arising between the tax bases of assets and liabilities and their carrying amounts for financial reporting purposes. In accordance with the initial recognition exemption, deferred taxes are not recorded for temporary differences on initial recognition of an asset or a liability in a transaction other than a business combination if the transaction, when initially recorded, affects neither accounting nor taxable profit. Deferred tax balances are measured at tax rates enacted or substantively enacted at the balance sheet date which are expected to apply to the period when the temporary differences will reverse or the tax loss carry forwards will be utilised. Deferred tax assets for deductible temporary differences and tax loss carry forwards are recorded only to the extent that it is probable that future taxable profit will be available against which the deductions can be utilised.

Provisions for liabilities and charges. Provisions for liabilities and charges are non-financial liabilities of uncertain timing or amount. They are accrued when the Bank has a present legal or constructive obligation as a result of past events, it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation, and a reliable estimate of the amount of the obligation can be made.

Trade and other payables. Trade payables are accrued when the counterparty performed its obligations under the contract and are carried at amortised cost.

Credit related commitments. In the normal course of business, the Bank enters into credit related commitments, including irrevocable credit lines, letters of credit and guarantees. Specific provisions are recorded against other credit related commitments when losses are considered more likely than not.

3 Basis of Preparation and Significant Accounting Policies (Continued)

Dividends. Dividends are recorded in equity in the period in which they are declared. Dividends declared after the balance sheet date and before the financial statements are authorised for issue are disclosed in the subsequent events note. The statutory accounting reports of the Bank are the basis for profit distribution and other appropriations. Ukrainian legislation identifies the basis of distribution as the retained earnings.

Income and expense recognition. Interest income and expense are recorded in the income statement for all debt instruments on an accrual basis using the effective interest method. This method defers, as part of interest income or expense, all fees paid or received between the parties to the contract that are an integral part of the effective interest rate, transaction costs and all other premiums or discounts.

Fees integral to the effective interest rate include origination fees received or paid by the entity relating to the creation or acquisition of a financial asset or issuance of a financial liability, for example fees for evaluating creditworthiness, evaluating and recording guarantees or collateral, negotiating the terms of the instrument and for processing transaction documents. Commitment fees received by the Bank to originate loans at market interest rates are integral to the effective interest rate if it is probable that the Bank will enter into a specific lending arrangement and does not expect to sell the resulting loan shortly after origination. The Bank does not designate loan commitments as financial liabilities at fair value through profit or loss.

When loans and other debt instruments become doubtful of collection, they are written down to present value of expected cash inflows and interest income is thereafter recorded for the unwinding of the present value discount based on the asset's effective interest rate which was used to measure the impairment loss.

All other fees, commissions and other income and expense items are generally recorded on an accrual basis by reference to completion of the specific transaction assessed on the basis of the actual service provided as a proportion of the total services to be provided. Loan syndication fees are recognised as income when the syndication has been completed and the Bank retained no part of the loan package for itself or retained a part at the same effective interest rate for the other participants.

Custody service fees that are continuously provided over an extended period of time are recorded ratably over the period the service is provided.

Foreign currency translation. Functional currency of the Bank is the currency of the primary economic environment in which the Bank operates. The Bank's functional currency and presentation currency is the national currency of Ukraine, Ukrainian hryvnia ("UAH").

Monetary assets and liabilities are translated into functional currency at the official exchange rate of the NBU at the respective balance sheet dates. Foreign exchange gains and losses resulting from the settlement of the transactions and from the translation of monetary assets and liabilities into functional currency at year-end official exchange rates of the NBU are recognised in profit or loss. Translation at year-end rates does not apply to non-monetary items, including equity investments. Effects of exchange rate changes on the fair value of equity securities are recorded as part of the fair value gain or loss.

At 31 December 2005 the principal rates of exchange used for translating foreign currency balances were USD 1 = UAH 5.0500, EUR 1 = UAH 5.9716 (2004: USD 1 = UAH 5.3054, EUR 1 = UAH 7.2175). Exchange restrictions and controls exist relating to converting Ukrainian hryvnias into other currencies. At present, the Ukrainian hryvnia is not a freely convertible currency in most countries outside of Ukraine.

Fiduciary activities. Assets and liabilities held by the Bank in its own name, but on the account of third parties, are not reported on the balance sheet. The extent of such balances and transactions is indicated in Note 24. For the purposes of disclosure, fiduciary activities do not encompass safe custody functions. Commissions received from fiduciary activities are shown in fee and commission income.

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

Accounting for the effects of hyperinflation. Ukraine has previously experienced relatively high levels of inflation and was considered to be hyperinflationary as defined by IAS 29 "Financial Reporting in Hyperinflationary Economies" ("IAS 29"). IAS 29 requires that the financial statements prepared in the currency of a hyperinflationary economy be stated in terms of the measuring unit current at the balance sheet date. It states that reporting operating results and financial position in the local currency without restatement is not useful because money loses purchasing power at such a rate that the comparison of amounts from transactions and other events that have occurred at different times, even within the same accounting period, is misleading.

3 Basis of Preparation and Significant Accounting Policies (Continued)

The characteristics of the economic environment of Ukraine indicate that hyperinflation has ceased effective from 1 January 2001. Restatement procedures of IAS 29 are therefore only applied to assets acquired or revalued and liabilities incurred or assumed prior to that date. For these balances, the amounts expressed in the measuring unit current as at 31 December 2000 are the basis for the carrying amounts in these financial statements. The restatement was calculated by indexing the historical balances by changes in the general price index up to 31 December 2000.

Staff costs and related contributions. Wages, salaries, contributions to the Ukraine state pension and social insurance funds, paid annual leave and sick leave, bonuses, and non-monetary benefits are accrued in the year in which the associated services are rendered by the employees of the Bank.

Changes in presentation. Where necessary, corresponding figures have been adjusted to conform with changes in the presentation of the current year. The effect of reclassifications is as follows:

<i>In thousands of Ukrainian Hryvnias</i>	2005	2004
Increase in		
Other securities at fair value through profit or loss	-	18,740
Provision for impairment of investment securities available for sale	-	(3,172)
Decrease in		
Investment securities available for sale	-	(18,740)
Losses less gains from investment securities available for sale	-	3,172

Provision for impairment of investment securities available for sale previously disclosed within losses less gains arising from securities, is presented as a separate line item in the income statement of the Bank.

The Bank has not reclassified any financial asset to a category measured at amortised cost rather than fair value during 2005 (2004: none). These financial statements were approved for issue on 28 April 2006 and further changes require approval of the body that gave that authorisation.

4 Critical Accounting Estimates, and Judgements in Applying Accounting Policies

The Bank makes estimates and assumptions that affect the reported amounts of assets and liabilities within the next financial year. Estimates and judgements are continually evaluated and are based on management's experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances. Management also makes certain judgements, apart from those involving estimations, in the process of applying the accounting policies. Judgements that have the most significant effect on the amounts recognised in the financial statements and estimates that can cause a significant adjustment to the carrying amount of assets and liabilities within the next financial year include:

Impairment of available for-sale equity investments. The Bank determines 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 requires 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.

Impairment losses on loans and advances. The Bank regularly reviews its loan portfolios to assess impairment. In determining whether an impairment loss should be recorded in the income statement, the Bank makes judgements as to whether there is any observable data indicating that there is a measurable decrease in the estimated future cash flows from a portfolio of loans before the decrease can be identified with an individual loan in that portfolio. This evidence may include observable data indicating that there has been an adverse change in the payment status of borrowers in a group, or national or local economic conditions that correlate with defaults on assets in the group. Management uses estimates based on historical loss experience for assets with credit risk characteristics and objective evidence of impairment similar to those in the portfolio when scheduling its future cash flows. The methodology and assumptions used for estimating both the amount and timing of future cash flows are reviewed regularly to reduce any differences between loss estimates and actual loss experience. To the extent that the net present value of estimated cash flows differs by +/-5 percent, the provision would be estimated UAH 485 thousand higher or UAH 485 thousand lower (2004: UAH 361 thousand higher or UAH 361 thousand lower).

Tax legislation. Ukrainian tax, currency and customs legislation is subject to varying interpretations. Refer to Note 24.

Deferred income tax asset recognition. The net deferred tax asset represents income taxes recoverable through future deductions from taxable profits and is recorded on the balance sheet. Deferred income tax assets are recorded to the extent that realisation of the related tax benefit is probable. In determining future taxable profits and the amount of tax benefits that are probable in the future Management makes judgements and applies estimation based on last three years taxable profits and expectations of future income that are believed to be reasonable under the circumstances.

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.

5 Adoption of New or Revised Standards and Interpretations

Certain new IFRSs became effective for the Bank from 1 January 2005. Listed below are those new or amended standards or interpretations which are or in the future could be relevant to the Bank's operations and the nature of their impact on the Bank's accounting policies. All changes in accounting policies were applied retrospectively with adjustments made to the retained earnings at 1 January 2004, unless otherwise described below.

IAS 1 (revised 2003), Presentation of Financial Statements. Certain new disclosures and changes in presentation required by the revised standard were made in these financial statements.

IAS 16 (revised 2003) Property, Plant and Equipment. The residual value is now defined as the amount that the Bank estimates it would receive currently for the asset if the asset were already of the age and in the condition expected at the end of its useful life. The Bank's policy is now not to cease depreciating assets during temporary periods when the assets are idle. The Bank now derecognises the carrying amount of a component of premises and equipment which has been replaced and capitalises the cost of the replacement. The previous version of IAS 16 did not extend its derecognition principle to components; rather, its recognition principle for subsequent expenditures effectively precluded the cost of a replacement from being capitalised. All changes to accounting policies as a result of the revised IAS 16 were accounted for retrospectively and did not result in a significant effect on the carrying amount of the Bank's assets.

5 Adoption of New or Revised Standards and Interpretations (Continued)

IAS 17 (revised 2003) Leases. Initial direct costs incurred in negotiating a finance lease are now deferred as part of the net investment in the lease. Finance leases are now recognised at commencement based on values measured at inception. Commencement is when the lessee can start using the leased asset. Inception is the earlier of the date of the lease agreement and the date of commitment to the principal provisions of the lease. The revised IAS 17 is applied retrospectively to all leases in accordance with the transitional provisions of the standard.

IAS 24 (revised 2003) Related Party Disclosures. The definition of related parties was extended and additional disclosures required by the revised standard were made in these financial statements.

IAS 32 (revised 2003) Financial Instruments: Disclosure and Presentation. Additional disclosures required by the revised Standard were made in these financial statements.

IAS 39 (revised 2003) Financial Instruments: Recognition and Measurement. The definition of 'originated loans and receivables' was amended to become 'loans and receivables'. This category now comprises originated or purchased loans and receivables that are not quoted in an active market. The Bank amended its policies and may designate any financial instrument on initial recognition as one to be measured at fair value, with changes in fair value recognised in profit or loss. Subsequent reclassifications into or out of the 'at fair value through profit or loss' category are prohibited. The Bank no longer recognises gains and losses on available-for-sale financial assets in profit or loss but in equity.

The Bank amended its policies for derecognition of financial assets. Under the original IAS 39, several concepts governed derecognition. The revised IAS 39 retains the two main concepts of risks and rewards and control, but clarifies that the evaluation of the transfer of risks and rewards precedes the evaluation of the transfer of control. The Bank now applies the guidance added to IAS 39 on how to determine fair values using valuation techniques and how to evaluate impairment in a group of loans, receivables or held-to-maturity investments which cannot yet be identified with any individual asset in the group. In accordance with the standard's transitional provisions the revised accounting policies are applied retrospectively except for the clarified derecognition rules which are applied prospectively from 1 January 2004. The Bank has redesignated financial instruments into 'at fair value through profit or loss' from the 'available for sale' category at the date of initial application of the revised IAS 39. Previously all realised and unrealised gains and losses arising from changes in the fair value of investments available-for-sale were included in the statement of income in the period in which they arose.

Effect of Adoption of New or Revised Standards. The effect of adoption of the above new or revised standards and interpretations on the Bank's financial position at 31 December 2005 and 31 December 2004 and on the results of its operations for the years then ended was not significant.

6 New Accounting Pronouncements

Certain new standards and interpretations have been published that are mandatory for the Bank's accounting periods beginning on or after 1 January 2006 or later periods and which the Bank has not early adopted:

IFRIC 4, Determining whether an Arrangement contains a Lease (effective from 1 January 2006). IFRIC 4 requires that determining whether an arrangement is, or contains, a lease be based on the substance of the arrangement. It requires an assessment of whether (a) fulfilment of the arrangement is dependent on the use of a specific asset or assets (the asset); and (b) the arrangement conveys a right to use the asset.

IAS 39 (Amendment) – The Fair Value Option (effective from 1 January 2006). IAS 39 (as revised in 2003) permitted entities to designate irrevocably on initial recognition practically any financial instrument as one to be measured at fair value with gains and losses recognised in profit or loss ('fair value through profit or loss'). The amendment changes the definition of financial instruments 'at fair value through profit or loss' and restricts the ability to designate financial instruments as part of this category. The group of financial assets designated by the Bank as 'at fair value through profit or loss' is managed and its performance evaluated on a fair value basis.

IAS 39 (Amendment) - Cash Flow Hedge Accounting of Forecast Intragroup Transactions (effective from 1 January 2006). The amendment allows the foreign currency risk of a highly probable forecast intragroup transaction to qualify as a hedged item in the financial statements provided that the transaction is denominated in a currency other than the functional currency of the entity entering into that transaction and the foreign currency risk will affect profit or loss.

IAS 39 (Amendment) – Financial Guarantee Contracts (effective from 1 January 2006). Issued financial guarantees, other than those previously asserted by the entity to be insurance contracts, will have to be initially recognised at their fair value, and subsequently measured at the higher of (i) the unamortised balance of the related fees received and deferred and (ii) the expenditure required to settle the commitment at the balance sheet date. Different requirements apply for the subsequent measurement of issued financial guarantees that prevent derecognition of financial assets or result in continuing involvement accounting.

IFRS 7 Financial Instruments: Disclosures and a complementary Amendment to IAS 1 Presentation of Financial Statements - Capital Disclosures (effective from 1 January 2007). The IFRS introduces new disclosures to improve the information about financial instruments. It replaces IAS 30, Disclosures in the Financial Statements of Banks and Similar Financial Institutions, and some of the requirements in IAS 32, Financial Instruments: Disclosure and Presentation. The Amendment to IAS 1 introduces disclosures about level of an entity's capital and how it manages capital. The Bank is currently assessing what impact the new IFRS and the amendment to IAS 1 will have on disclosures in its financial statements.

IAS 19 (Amendment) - Employee Benefits (effective from 1 January 2006). The amendment to IAS 19 introduces an additional option to recognise actuarial gains and losses arising in post-employment defined benefit plans in full directly in retained earnings in equity. It also requires new disclosures about defined benefit plans and clarifies accounting for a contractual agreement between a multi-employer plan and participating employers.

Unless otherwise described above, the new standards and interpretations are not expected to significantly affect the Bank's financial statements.

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7 Cash and Cash Equivalents and Mandatory Reserve Balances

<i>In thousands of Ukrainian hryvnias</i>	2005	2004
Cash on hand	117,551	84,070
Cash balances with the NBU	127,765	102,179
Correspondent accounts and overnight placements with other banks		
- Ukraine	3,959	1,470
- Other countries	14,506	3,995
Total cash and cash equivalents and mandatory reserve balances	263,781	191,714

As at 31 December 2005 the mandatory reserve balance is calculated on the basis of a simple average over a monthly period (2004: monthly period) and should be maintained at the level of 6 to 8 per cent (2004: 6 to 7 percent) of certain obligations of the Bank. As such, the balance can vary from day-to-day. As at 31 December 2005 the Bank's mandatory reserve balance was UAH 124,257 thousand (31 December 2004: UAH 71,201 thousand). The Bank may satisfy its mandatory reserve requirement with its balance on correspondent account with the National Bank of Ukraine (2004: balance on correspondent account with the National Bank of Ukraine and up to 40% of UAH cash on hand). Mandatory reserve balance carries 0% interest rate.

As at 31 December 2005 in accordance with the NBU regulations the Bank was required to maintain the daily balance on correspondent account with the NBU at the level not less than 90% of the mandatory reserve balance for the preceding month (31 December 2004: not less than 60% of the mandatory reserve balance for the preceding month).

As the respective liquid assets are not available to finance the Bank's day-to-day operations, the mandatory reserve balance is excluded from cash and cash equivalents for the purposes of the cash flow statement. As at 31 December 2005 the Bank's cash and cash equivalents for the purposes of cash flow statement equalled UAH 139,524 thousand (31 December 2004: UAH 120,513 thousand).

Geographical, currency and interest rate analyses of cash and cash equivalents and mandatory reserve balances are disclosed in Note 23.

8 Trading Securities

<i>In thousands of Ukrainian hryvnias</i>	2005	2004
Corporate shares	8,346	-
Total trading securities	8,346	-

Corporate shares represent shares of Ukrainian enterprises, traded on Ukrainian over-the-counter market (PFTS).

Geographical, currency and interest rate analyses of trading securities are disclosed in Note 23.

9 Other Securities at Fair Value Through Profit or Loss

<i>In thousands of Ukrainian hryvnias</i>	2005	2004
Ukrainian Treasury Bonds (OVDP)	-	14,036
Municipal bonds	5,039	-
Corporate bonds	4,951	-
Corporate shares	225	4,704
Total other securities at fair value through profit or loss	10,215	18,740

Municipal bonds represent bonds of local authorities of Odessa city, traded on Ukrainian over-the-counter market (PFTS). The bonds mature in December 2007, have coupon rate of 12% and yield to maturity of 12%.

Corporate bonds represent bonds of Ukrainian enterprises, traded on Ukrainian over-the-counter market (PFTS). The bonds mature from December 2008 to October 2010, have coupon rates of 16.5% - 18%, and yield to maturity of 16.5% - 18%.

The Bank irrevocably designated the above securities that are not part of its trading book, as at fair value through profit or loss.

Geographical, currency and interest rate analyses of other securities at fair value through profit or loss are disclosed in Note 23.

10 Due from Other Banks

<i>In thousands of Ukrainian hryvnias</i>	2005	2004
Term placements with other banks	26,282	65,367
Guarantee deposits with other banks	12,652	17,998
Less: Provision for impairment of due from other banks	-	(956)
Total due from other banks	38,934	82,409

Guarantee deposits represent balances placed with other banks as cover for guarantees and import letters of credit. These are effectively restricted deposits, which are required to be maintained to complete the related trade financing activity.

As at 31 December 2005 term placements with other banks included UAH 25,250 thousand (31 December 2004: none), whereby the same counterparty has also placed the same amount of deposits with the Bank for the same term. The respective assets and liabilities have not been offset, as there is no legal right to offset. Refer to Note 14.

Movements in the provision for impairment of due from other banks are as follows:

<i>In thousands of Ukrainian hryvnias</i>	2005	2004
Provision for impairment of due from other banks at 1 January	956	231
(Recovery of)/provision for impairment of due from other banks during the year	(956)	725
Provision for impairment of due from other banks at 31 December	-	956

At 31 December 2005 the estimated fair value of due from other banks was UAH 38,934 thousand (2004: UAH 79,459 thousand). Refer to Note 25.

Geographical, currency, maturity and interest rate analyses of due from other banks are disclosed in Note 23.

11 Loans and Advances to Customers

<i>In thousands of Ukrainian hryvnias</i>	2005	2004
Current loans	1,748,196	1,282,063
Overdue loans	16,315	30,651
Reverse sale and repurchase agreements	-	1,219
Less: Provision for loan impairment	(121,844)	(117,794)
Total loans and advances to customers	1,642,667	1,196,139

During 2005 a loss on initial recognition of loans at rates below market in amount of UAH 3,059 thousand (2004: UAH 7,653 thousand) has been recorded in the income statement.

Movements in the provision for loan impairment are as follows:

<i>In thousands of Ukrainian hryvnias</i>	2005	2004
Provision for loan impairment at 1 January	117,794	101,947
Provision for loan impairment during the year	21,691	16,200
Loans and advances to customers written off during the year as uncollectible	(17,641)	(353)
Provision for loan impairment at 31 December	121,844	117,794

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

<i>In thousands of Ukrainian hryvnias</i>	2005		2004	
	Amount	%	Amount	%
Trade and commerce	944,898	54	834,992	64
Agriculture and food industry	217,907	12	138,900	10
Manufacturing	193,198	11	117,567	9
Transport and communication	154,295	9	38,201	3
Individuals	132,194	7	55,201	4
Other	122,019	7	129,072	10
Total loans and advances to customers (before impairment)	1,764,511	100	1,313,933	100

At 31 December 2005, the largest 10 borrowers of the Bank (2004: 10 borrowers) had aggregated loan amounts of UAH 357,409 thousand (2004: UAH 372,256 thousand) or 20% of the gross loan portfolio (2004: 28%).

At 31 December 2005 loans and advances to customers amounting to UAH 46,593 thousand were provided as collateral against term deposits of other banks totalling UAH 13,957 thousand. Refer to Notes 14 and 24.

At 31 December 2005 the estimated fair value of loans and advances to customers was UAH 1,646,019 thousand (2004: UAH 1,190,812 thousand). Refer to Note 25.

Geographical, currency, maturity and interest rate analyses of loans and advances to customers are disclosed in Note 23. The information on related party balances is disclosed in Note 26.

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12 Investment Securities Available for Sale

<i>In thousands of Ukrainian hryvnias</i>	2005	2004
Corporate bonds	60,842	4,056
Corporate shares	4,375	4,125
Promissory notes	150	1,467
Less: Provision for impairment of investment securities available for sale	(2,825)	(3,172)
Total investment securities available for sale	62,542	6,476

Corporate bonds represent bonds of Ukrainian enterprises. The bonds mature from January 2007 to November 2010, have coupon rates of 15% - 20.5%, and yield to maturity of 13.5% - 15%.

Corporate shares are shares of Ukrainian enterprises for which market quotations are not available. They are carried at cost, less provision for impairment.

The movements in investment securities available for sale are as follows:

<i>In thousands of Ukrainian hryvnias</i>	2005	2004
Carrying amount at 1 January	6,476	24,218
Recovery of/(provision) for impairment	347	(3,172)
Purchases	92,793	530
Disposals	(37,074)	(15,100)
Carrying amount at 31 December	62,542	6,476

Geographical, currency, maturity and interest rate analyses of investment securities available for sale are disclosed in Note 23. The information on related party debt investment securities available for sale is disclosed in Note 26.

BANK PIVDENNYI
NOTES TO THE FINANCIAL STATEMENTS – 31 DECEMBER 2005

13 Premises, Equipment and Intangible Assets

<i>In thousands of Ukrainian hryvnias</i>	Note	Premises	Furniture and equipment	Computers	Motor vehicles	Intangible assets	Other	Construction in progress	Total
Cost at 1 January 2004		33,609	8,407	11,049	4,467	780	2,848	-	61,160
Accumulated depreciation		(4,010)	(5,059)	(6,412)	(1,487)	(670)	(1,988)	-	(19,626)
Carrying amount at 1 January 2004		29,599	3,348	4,637	2,980	110	860	-	41,534
Additions		10,461	2,601	4,905	1,060	822	235	-	20,084
Disposals		-	(32)	(6)	(148)	-	-	-	(186)
Depreciation and amortisation charge	21	(2,015)	(1,432)	(2,665)	(919)	(144)	(571)	-	(7,746)
Carrying amount at 31 December 2004		38,045	4,485	6,871	2,973	788	524	-	53,686
Cost at 31 December 2004		44,070	10,923	15,833	5,054	1,572	2,809	-	80,261
Accumulated depreciation		(6,025)	(6,438)	(8,962)	(2,081)	(784)	(2,285)	-	(26,575)
Carrying amount at 31 December 2004		38,045	4,485	6,871	2,973	788	524	-	53,686
Additions		8,930	2,323	7,118	1,520	1,260	1,121	66,515	88,787
Revaluation		35,131	-	-	-	-	-	-	35,131
Disposals		-	-	(2)	(188)	-	-	-	(190)
Depreciation and amortisation charge	21	(2,205)	(2,001)	(3,056)	(1,152)	(241)	(1,349)	-	(10,004)
Carrying amount at 31 December 2005		79,901	4,807	10,931	3,153	1,807	296	66,515	167,410
Cost or valuation at 31 December 2005		79,901	13,235	22,674	6,240	2,832	3,928	66,515	195,325
Accumulated depreciation		-	(8,428)	(11,743)	(3,087)	(1,025)	(3,632)	-	(27,915)
Carrying amount at 31 December 2005		79,901	4,807	10,931	3,153	1,807	296	66,515	167,410

13 Premises, Equipment and Intangible Assets (Continued)

Construction in progress consists of construction and refurbishment of branch premises. Upon completion, assets are transferred to premises.

Premises were independently valued as at 31 December 2005. The valuation was carried out by an independent firm of valuers, Private Company "Analityk". The basis used for the appraisal was market value. Fair values were estimated using market prices. Included in the above carrying amount is UAH 35,131 thousand representing revaluation surplus relating to premises of the Bank. At 31 December 2005 the carrying amount of premises would have been UAH 44,770 thousand (2004: UAH 38,045 thousand) had the assets been carried at cost less depreciation.

14 Due to Other Banks

<i>In thousands of Ukrainian hryvnias</i>	2005	2004
Correspondent accounts and overnight placements of other banks	59,408	470
Term placements of other banks	240,786	290,842
Total due to other banks	300,194	291,312

Included in the total amount of due to other banks is a balance of UAH 160,882 thousand (31 December 2004: UAH 248,528 thousand) from a bank located in Latvia, which is a related party of the Bank. Refer to Note 26. As disclosed in Note 27, in January 2006 the Bank acquired 49% of the share capital of this bank.

As at 31 December 2005 correspondent accounts and overnight placements of other banks included UAH 25,250 thousand (31 December 2004: none), whereby the same counterparty had also received the same amount of overnight placement from the Bank. The respective assets and liabilities have not been offset, as there is no legal right to offset. Refer to Note 10.

As at 31 December 2005 term placements of other banks included deposits amounting to UAH 13,957 thousand collateralised by loans to customers totalling UAH 46,593 thousand. Refer to Notes 11 and 24.

At 31 December 2005 the estimated fair value of due to other banks was UAH 300,194 thousand (2004: UAH 291,128 thousand). Refer to Note 25.

Geographical, currency, maturity and interest rate analyses of due to other banks are disclosed in Note 23. The information on related party balances is disclosed in Note 26.

15 Customer Accounts

<i>In thousands of Ukrainian hryvnias</i>	2005	2004
Legal entities		
- Current/settlement accounts	421,289	315,272
- Term deposits	385,771	290,353
Individuals		
- Current/demand accounts	115,353	50,784
- Term deposits	677,650	404,934
Total customer accounts	1,600,063	1,061,343

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15 Customer Accounts (Continued)

Economic sector concentrations within customer accounts are as follows:

<i>In thousands of Ukrainian hryvnias</i>	2005		2004	
	Amount	%	Amount	%
Individuals	793,003	50	455,718	43
Trade and commerce	443,750	28	252,719	24
Transport and communications	116,758	7	93,798	9
Manufacturing	74,403	5	74,808	7
Finance and insurance	35,646	2	105,691	10
Other	136,503	8	78,609	7
Total customer accounts	1,600,063	100	1,061,343	100

During 2004 a gain on initial recognition of term deposits at rates below market in the amount of UAH 3,051 thousand has been recorded in the income statement.

At 31 December 2005, the largest 10 customers of the Bank (2004: 10 customers) had total aggregate balances of UAH 299,866 thousand (2004: UAH 154,133 thousand) or 19% (2004: 15%) of total customer accounts.

At 31 December 2005 included in customer accounts are deposits of UAH 5,054 thousand (2004: UAH 5,239 thousand) held as collateral for irrevocable commitments under import letters of credit and guarantees. Refer to Note 24.

At 31 December 2005 the estimated fair value of customer accounts was UAH 1,597,913 thousand (2004: UAH 1,057,894 thousand). Refer to Note 25.

Geographical, currency, maturity and interest rate analyses of customer accounts are disclosed in Note 23. The information on related party balances is disclosed in Note 26.

16 Subordinated Debt

Subordinated debt represents a long term borrowing agreement, which, in case of the Bank's default, would be secondary to the Bank's other obligations, including deposits and other debt instruments. In accordance with the Law of Ukraine on Banks and Banking Activities and the NBU regulations, subordinated debt cannot be withdrawn from the Bank for at least five years from the date of receipt.

Subordinated debt was attracted from an individual in USD and EUR in August 2005 and matures in 2010, with an interest rate of 10% per annum. As at 31 December 2005 fair value of the subordinated debt amounted to UAH 7,747 thousand.

Geographical, currency, maturity and interest rate analyses of subordinated debt are disclosed in Note 23.

17 Other Liabilities

<i>In thousands of Ukrainian hryvnias</i>	Note	2005	2004
Provision for losses on credit related commitments	24	2,908	3,582
Other taxes payable		799	1,035
Trade creditors		485	846
Provision for tax payments		-	1,590
Other		860	1,401
Total other liabilities		5,052	8,454

Geographical, currency and maturity analyses of other liabilities are disclosed in Note 23.

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18 Share Capital

	Number of outstanding shares	Nominal amount	Inflation adjusted amount
<i>In thousands of Ukrainian hryvnias</i>			
At 1 January 2004	100,002,200	100,002	108,898
New shares issued	40,000,000	40,000	40,000
At 31 December 2004	140,002,200	140,002	148,898
New shares issued	59,997,800	59,998	59,998
At 31 December 2005	200,000,000	200,000	208,896

At 31 December 2005, all of the Bank's outstanding shares were authorised, issued and fully paid in.

All ordinary shares have a nominal value of UAH 1 per share and rank equally. Each share carries one vote.

During the year ended 31 December 2005 the Bank has made distributions to certain shareholders in the amount of UAH 6,594 thousand net of tax effect of UAH 2,198 thousand (year ended 31 December 2004: UAH 8,421 thousand net of tax effect of UAH 2,807 thousand).

BANK PIVDENNYI
NOTES TO THE FINANCIAL STATEMENTS – 31 DECEMBER 2005

19 Interest Income and Expense

<i>In thousands of Ukrainian hryvnias</i>	2005	2004
Interest income		
Loans and advances to legal entities	217,408	182,666
Loans and advances to individuals	13,523	6,731
Due from other banks	3,985	2,629
Debt investment securities available for sale	2,021	2,588
Debt trading securities	551	-
Other debt securities at fair value through profit or loss	295	3,672
Total interest income	237,783	198,286
Interest expense		
Term deposits of individuals	68,299	49,815
Term deposits of legal entities	43,078	30,465
Placements of other banks	17,158	20,952
Current/settlement accounts	6,433	6,465
Debt securities in issue	1,732	2,834
Due to the National Bank of Ukraine	-	1,139
Subordinated debt	631	46
Total interest expense	137,331	111,716
Net interest income	100,452	86,570

Information on interest income and expenses from transactions with related parties is disclosed in Note 26.

20 Fee and Commission Income and Expense

<i>In thousands of Ukrainian hryvnias</i>	2005	2004
Fee and commission income		
- Cash and settlement transactions with customers	31,539	26,977
- Purchase and sale of foreign currency	12,526	10,087
- Guarantees issued	4,976	490
- Cash and settlement transactions with other banks	1,055	1,069
- Transactions with securities	294	244
- Other	483	-
Total fee and commission income	50,873	38,867
Fee and commission expense		
- Cash and settlement transactions with other banks	4,481	3,089
- Other	1,153	946
Total fee and commission expense	5,634	4,035
Net fee and commission income	45,239	34,832

21 Administrative and Other Operating Expenses

<i>In thousands of Ukrainian hryvnias</i>	Note	2005	2004
Staff costs		50,188	35,791
Depreciation and amortisation of premises, equipment and intangible assets	13	10,004	7,746
Taxes other than on income		7,308	6,292
Operating lease expense		6,442	5,135
Mail and telecommunications		5,017	4,390
Advertising and marketing services		4,865	2,059
Repairs and maintenance		3,941	4,090
Household expenses		3,930	2,041
Professional services		3,727	1,134
Security services		2,604	2,006
Insurance of credit risks		2,010	2,947
Other		5,407	4,058
Total administrative and other operating expenses		105,443	77,689

Included in staff costs are statutory social security and pension contributions of UAH 11,859 thousand (2004: UAH 7,567 thousand).

22 Income Taxes

Income tax expense comprises the following:

<i>In thousands of Ukrainian hryvnias</i>	2005	2004
Current tax charge	6,592	9,053
Deferred tax movement due to origination or reversal of temporary differences	8,952	(1,365)
Deferred tax movement recognised directly in equity	(8,783)	-
Tax effect of distribution recognised directly in equity	2,198	2,807
Income tax expense for the year	8,959	10,495

In 2005 and 2004 the Bank transferred funds to certain shareholders which are treated as distributed profit in these financial statements. The tax effect on the distributions is recognised directly in equity as required by IAS 12 "Income Taxes".

The income tax rate applicable to the Bank's income is 25% (2004: 25%).

A reconciliation between the expected and the actual taxation charge is provided below.

<i>In thousands of Ukrainian hryvnias</i>	2005	2004
IFRS profit before tax	37,640	33,497
Theoretical tax charge at statutory rate (2005: 25%; 2004: 25%)	9,410	8,374
Tax effect of items which are not deductible or assessable for taxation purposes:		
- Non-deductible expense	1,139	531
(Reversal of)/provision for tax payments	(1,590)	1,590
Income tax expense for the year	8,959	10,495

A deferred tax liability of UAH 8,783 thousand has been recorded directly in equity in respect of the revaluation of the Bank's premises. Refer to Note 13.

Differences between IFRS and Ukrainian statutory taxation regulations give rise to temporary differences between the carrying amount of assets and liabilities for financial reporting purposes and their tax bases. The tax effect of the movements in these temporary differences is detailed below and is recorded at the rate of 25% (2004: 25%).

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NOTES TO THE FINANCIAL STATEMENTS – 31 DECEMBER 2005

22 Income Taxes (Continued)

	31 December 2003	Recognised in the statement of income	31 December 2004	Recognised in the statement of income	Recognised in equity	31 December 2005
<i>In thousands of Ukrainian hryvnias</i>						
Tax effect of deductible temporary differences						
Loan impairment provision	2,342	(1,547)	795	2,067	-	2,862
Gain/(loss) on origination of assets/liabilities at rates above/below market	(153)	1,688	1,535	(1,205)	-	330
Accrued expenses	182	242	424	(306)	-	118
Gross deferred tax asset	2,371	383	2,754	556	-	3,310
Tax effect of taxable temporary differences						
Premises and equipment	317	628	945	332	(8,783)	(7,506)
Accrued income	220	91	311	(319)	-	(8)
Trading securities, other securities at fair value through profit or loss and investment securities available for sale	(1,711)	263	(1,448)	(738)	-	(2,186)
Gross deferred tax liability	(1,174)	982	(192)	(725)	(8,783)	(9,700)
Recognised deferred tax asset/(liability)	1,197	1,365	2,562	(169)	(8,783)	(6,390)

23 Financial Risk Management

The risk management function within the Bank is carried out in respect of financial risks (credit, market, geographical, currency, liquidity and interest rate), operational risks and legal risks. The primary objectives of the financial risk management function are to establish risk limits, and then ensure that exposure to risks stays within these limits. The operational and legal risk management functions are intended to ensure proper functioning of internal policies and procedures to minimise operational and legal risks.

Credit risk. The Bank takes on exposure to credit risk which is the risk that a counterparty will be unable to pay all amounts in full when due. The Bank structures the levels of credit risk it undertakes by placing limits on the amount of risk accepted in relation to one borrower, or groups of borrowers, and to geographical and industry segments. Such risks are monitored on a revolving basis and subject to an annual or more frequent review. Limits on the level of credit risk by product, borrower and industry sector are approved regularly by the Board of Directors.

The exposure to any one borrower including banks and brokers is further restricted by sub-limits covering on and off-balance sheet exposures. Actual exposures against limits are monitored daily.

Exposure to credit risk is managed through regular analysis of the ability of borrowers and potential borrowers to meet interest and principal repayment obligations and by changing these lending limits where appropriate. Exposure to credit risk is also managed, in part, by obtaining collateral and corporate and personal guarantees.

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

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

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

BANK PIVDENNYI
NOTES TO THE FINANCIAL STATEMENTS – 31 DECEMBER 2005

23 Financial Risk Management (Continued)

Geographical risk. The geographical concentration of the Bank's assets and liabilities at 31 December 2005 is set out below:

<i>In thousands of Ukrainian hryvnias</i>	Ukraine	OECD	Non-OECD	Total
Assets				
Cash and cash equivalents and mandatory reserve balances	249,275	11,801	2,705	263,781
Trading securities	8,346	-	-	8,346
Other securities at fair value through profit or loss	10,215	-	-	10,215
Due from other banks	35,316	227	3,391	38,934
Loans and advances to customers	1,642,667	-	-	1,642,667
Investment securities available for sale	62,542	-	-	62,542
Intangible assets	1,807	-	-	1,807
Premises and equipment	165,603	-	-	165,603
Other assets	4,603	-	-	4,603
Total assets	2,180,374	12,028	6,096	2,198,498
Liabilities				
Due to other banks	139,284	-	160,910	300,194
Customer accounts	1,515,885	24,784	59,394	1,600,063
Debt securities in issue	27,170	-	-	27,170
Subordinated debt	7,747	-	-	7,747
Current income tax liability	548	-	-	548
Deferred income tax liability	6,390	-	-	6,390
Other liabilities	5,052	-	-	5,052
Total liabilities	1,702,076	24,784	220,304	1,947,164
Net balance sheet position	478,298	(12,756)	(214,208)	251,334
Credit related commitments (Note 24)	99,479	-	-	99,479

OECD balances are mainly represented by the balances of counterparties located in USA and Germany. Non-OECD balances are mainly represented by the balances of counterparties located in Latvia.

Assets, liabilities and credit related commitments have been based on the country in which the counterparty is located. Balances with Ukrainian counterparties actually outstanding to/from off-shore companies of these Ukrainian counterparties are allocated to the caption "Ukraine". Cash on hand, and premises and equipment have been allocated based on the country in which they are physically held.

BANK PIVDENNYI
NOTES TO THE FINANCIAL STATEMENTS – 31 DECEMBER 2005

23 Financial Risk Management (Continued)

The geographical concentration of the Bank's assets and liabilities at 31 December 2004 is set out below:

<i>In thousands of Ukrainian hryvnias</i>	Ukraine	OECD	Non-OECD	Total
Assets				
Cash and cash equivalents and mandatory reserve balances	187,719	3,270	725	191,714
Other securities at fair value through profit or loss	18,740	-	-	18,740
Due from other banks	42,779	39,630	-	82,409
Loans and advances to customers	1,196,139	-	-	1,196,139
Investment securities available for sale	6,476	-	-	6,476
Guarantee deposits with the National Bank of Ukraine	29,738	-	-	29,738
Deferred income tax asset	2,562	-	-	2,562
Intangible assets	788	-	-	788
Premises and equipment	52,898	-	-	52,898
Other assets	4,303	-	-	4,303
Total assets	1,542,142	42,900	725	1,585,767
Liabilities				
Due to the National Bank of Ukraine	41,333	-	-	41,333
Due to other banks	41,542	806	248,964	291,312
Customer accounts	1,026,307	27,827	7,209	1,061,343
Debt securities in issue	21,639	-	1,932	23,571
Current income tax liability	355	-	-	355
Other liabilities	8,454	-	-	8,454
Total liabilities	1,139,630	28,633	258,105	1,426,368
Net balance sheet position	402,512	14,267	(257,380)	159,399
Credit related commitments (Note 24)	57,270	804	-	58,074

23 Financial Risk Management (Continued)

Currency risk. The Bank takes on exposure to effects of fluctuations in the prevailing foreign currency exchange rates on its financial position and cash flows. The Board of Directors sets limits on the level of exposure by currency and in total for both overnight and intra-day positions, which are monitored daily. The table below summarises the Bank's exposure to foreign currency exchange rate risk at 31 December 2005:

<i>In thousands of Ukrainian hryvnias</i>	UAH	USD	Euro	Other	Total
Assets					
Cash and cash equivalents and mandatory reserve balances	223,577	27,961	6,611	5,632	263,781
Trading securities	8,346	-	-	-	8,346
Other securities at fair value through profit or loss	10,215	-	-	-	10,215
Due from other banks	25,263	13,671	-	-	38,934
Loans and advances to customers	745,503	836,893	60,271	-	1,642,667
Investment securities available for sale	62,542	-	-	-	62,542
Intangible assets	1,807	-	-	-	1,807
Premises and equipment	165,603	-	-	-	165,603
Other assets	4,596	3	-	4	4,603
Total assets	1,247,452	878,528	66,882	5,636	2,198,498
Liabilities					
Due to other banks	55,348	217,646	27,200	-	300,194
Customer accounts	906,490	656,731	33,861	2,981	1,600,063
Debt securities in issue	27,104	66	-	-	27,170
Subordinated debt	-	4,585	3,162	-	7,747
Current income tax liability	548	-	-	-	548
Deferred income tax liability	6,390	-	-	-	6,390
Other liabilities	4,831	216	5	-	5,052
Total liabilities	1,000,711	879,244	64,228	2,981	1,947,164
Net balance sheet position	246,741	(716)	2,654	2,655	251,334
Credit related commitments (Note 24)	66,822	22,019	10,638	-	99,479

Balances in other currencies are mainly represented by balances denominated in Russian Roubles and British Pounds.

BANK PIVDENNYI
NOTES TO THE FINANCIAL STATEMENTS – 31 DECEMBER 2005

23 Financial Risk Management (Continued)

At 31 December 2004, the Bank had the following positions in currencies:

<i>In thousands of Ukrainian hryvnias</i>	UAH	USD	Euro	Other	Total
Assets					
Cash and cash equivalents and mandatory reserve balances	140,518	43,485	4,574	3,137	191,714
Other securities at fair value through profit or loss	18,740	-	-	-	18,740
Due from other banks	-	78,154	4,255	-	82,409
Loans and advances to customers	595,967	595,651	4,521	-	1,196,139
Investment securities available for sale	6,476	-	-	-	6,476
Guarantee deposits with the National Bank of Ukraine	-	21,799	7,939	-	29,738
Deferred income tax asset	2,562	-	-	-	2,562
Intangible assets	788	-	-	-	788
Premises and equipment	52,898	-	-	-	52,898
Other assets	4,274	29	-	-	4,303
Total assets	822,223	739,118	21,289	3,137	1,585,767
Liabilities					
Due to the National Bank of Ukraine	41,333	-	-	-	41,333
Due to other banks	37,661	249,529	4,122	-	291,312
Customer accounts	596,834	443,071	20,019	1,419	1,061,343
Debt securities in issue	21,639	1,932	-	-	23,571
Current income tax liability	355	-	-	-	355
Other liabilities	7,538	602	314	-	8,454
Total liabilities	705,360	695,134	24,455	1,419	1,426,368
Net balance sheet position	116,863	43,984	(3,166)	1,718	159,399
Credit related commitments (Note 24)	22,826	23,191	12,057	-	58,074

The Bank has extended loans and advances denominated in foreign currencies. Movements in foreign exchange rates affect the borrowers' repayment ability and incurrance of loan losses.

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

The table below shows assets and liabilities at 31 December 2005 by their remaining contractual maturity, unless there is evidence that any of the assets are impaired and will be settled after their contractual maturity dates, in which case the expected date of settlement of the assets is used. Some of the assets and liabilities, however, may be of a longer term nature; for example, loans are frequently renewed and accordingly short term loans can have a longer term duration.

Overdue liabilities, such as term deposits not withdrawn by the Bank's customers, are classified within the "demand and less than 1 month" column. Overdue assets are allocated based on their expected maturity. The entire portfolio of trading securities is classified within demand and less than one month based on management's assessment of portfolio's realisability and their view that it is a fairer portrayal of the Bank's liquidity position.

23 Financial Risk Management (Continued)

The liquidity position of the Bank at 31 December 2005 is set out below.

<i>In thousands of Ukrainian hryvnias</i>	Demand and less than 1 month	From 1 to 3 months	From 3 to 12 months	More than 1 year	No stated maturity	Total
Assets						
Cash and cash equivalents and mandatory reserve balances	263,781	-	-	-	-	263,781
Trading securities	8,346	-	-	-	-	8,346
Other securities at fair value through profit or loss	-	-	-	9,990	225	10,215
Due from other banks	26,971	11,963	-	-	-	38,934
Loans and advances to customers	370,870	135,922	406,272	729,603	-	1,642,667
Investment securities available for sale	-	-	-	60,992	1,550	62,542
Intangible assets	-	-	-	-	1,807	1,807
Premises and equipment	-	-	-	-	165,603	165,603
Other assets	2,284	271	2,048	-	-	4,603
Total assets	672,252	148,156	408,320	800,585	169,185	2,198,498
Liabilities						
Due to other banks	193,337	43,348	-	63,509	-	300,194
Customer accounts	627,722	140,240	538,151	293,950	-	1,600,063
Debt securities in issue	66	17,014	5,088	5,002	-	27,170
Subordinated debt	67	-	-	7,680	-	7,747
Current income tax liability	-	-	548	-	-	548
Deferred income tax liability	-	-	-	-	6,390	6,390
Other liabilities	2,692	-	2,360	-	-	5,052
Total liabilities	823,884	200,602	546,147	370,141	6,390	1,947,164
Net liquidity gap	(151,632)	(52,446)	(137,827)	430,444	162,795	251,334
Cumulative liquidity gap as at 31 December 2005	(151,632)	(204,078)	(341,905)	88,539	251,334	-

The Bank has a significant cumulative maturity mismatch of the assets and liabilities maturing within 12 months. This liquidity mismatch arises due to the fact that a significant source of finance for the Bank as at 31 December 2005 were customer accounts and interbank deposits being on demand and maturing in up to 12 months. Management believes that in spite of the substantial portion of customer accounts and interbank deposits being on demand and maturing in up to 12 months, diversification of these balances and the past experience of the Bank indicates that these deposits provide a long-term and stable source of finance for the Bank.

23 Financial Risk Management (Continued)

The liquidity position of the Bank at 31 December 2004 is set out below.

<i>In thousands of Ukrainian hryvnias</i>	Demand and less than 1 month	From 1 to 3 months	From 3 to 12 months	More than 1 year	No stated maturity	Total
Assets						
Cash and cash equivalents and mandatory reserve balances	191,714	-	-	-	-	191,714
Other securities at fair value through profit or loss	28	-	-	14,008	4,704	18,740
Due from other banks	76,429	-	1,923	4,057	-	82,409
Loans and advances to customers	193,035	181,448	407,172	414,484	-	1,196,139
Investment securities available for sale	-	-	4,465	710	1,301	6,476
Guarantee deposits with the National Bank of Ukraine	29,738	-	-	-	-	29,738
Deferred income tax asset	-	-	-	-	2,562	2,562
Intangible assets	-	-	-	-	788	788
Premises and equipment	-	-	-	-	52,898	52,898
Other assets	557	3,389	247	110	-	4,303
Total assets	491,501	184,837	413,807	433,369	62,253	1,585,767
Liabilities						
Due to the National Bank of Ukraine	41,333	-	-	-	-	41,333
Due to other banks	135,315	58,019	93,159	4,819	-	291,312
Customer accounts	406,028	104,939	439,432	110,944	-	1,061,343
Debt securities in issue	-	5,432	18,139	-	-	23,571
Current income tax liability	-	355	-	-	-	355
Other liabilities	2,214	3,838	479	333	1,590	8,454
Total liabilities	584,890	172,583	551,209	116,096	1,590	1,426,368
Net liquidity gap	(93,389)	12,254	(137,402)	317,273	60,663	159,399
Cumulative liquidity gap as at 31 December 2004	(93,389)	(81,135)	(218,537)	98,736	159,399	-

23 Financial Risk Management (Continued)

The matching and/or controlled mismatching of the maturities and interest rates of assets and liabilities is fundamental to the management of the Bank. It is unusual for banks ever to be completely matched since business transacted is often of an uncertain term and of different types. An unmatched position potentially enhances profitability, but can also increase the risk of losses. The maturities of assets and liabilities and the ability to replace, at an acceptable cost, interest-bearing liabilities as they mature, are important factors in assessing the liquidity of the Bank and its exposure to changes in interest and exchange rates.

Customer accounts are classified in the above analysis based on contractual maturities. However, in accordance with Ukrainian Civil Code, individuals have a right to withdraw their deposits prior to maturity if they forfeit their right to accrued interest.

Liquidity requirements to support calls under guarantees and standby letters of credit are considerably less than the amount of the commitment because the Bank does not generally expect the third party to draw funds under the agreement. The total outstanding contractual amount of commitments to extend credit does not necessarily represent future cash requirements, since many of these commitments will expire or terminate without being funded.

Interest rate risk. The Bank takes on exposure to the effects of fluctuations in the prevailing levels of market interest rates on its financial position and cash flows. Interest margins may increase as a result of such changes but may reduce or create losses in the event that unexpected movements arise. The table below summarises the Bank's exposure to interest rate risks at 31 December 2005. Included in the table are the Bank's assets and liabilities at carrying amounts, categorised by the earlier of contractual repricing or maturity dates.

<i>In thousands of Ukrainian hryvnias</i>	Demand and less than 1 month	From 1 to 3 months	From 3 to 12 months	More than 1 year	Non-interest bearing	Total
Assets						
Cash and cash equivalents and mandatory reserve balances	263,781	-	-	-	-	263,781
Trading securities	8,346	-	-	-	-	8,346
Other securities at fair value through profit or loss	-	-	-	9,990	225	10,215
Due from other banks	26,971	11,963	-	-	-	38,934
Loans and advances to customers	370,870	135,922	406,272	729,603	-	1,642,667
Investment securities available for sale	-	-	-	60,992	1,550	62,542
Intangible assets	-	-	-	-	1,807	1,807
Premises and equipment	-	-	-	-	165,603	165,603
Other assets	-	-	-	-	4,603	4,603
Total assets	669,968	147,885	406,272	800,585	173,788	2,198,498
Liabilities						
Due to other banks	193,337	43,348	-	63,509	-	300,194
Customer accounts	627,722	140,240	538,151	293,950	-	1,600,063
Debt securities in issue	66	17,014	5,088	5,002	-	27,170
Subordinated debt	67	-	-	7,680	-	7,747
Current income tax liability	-	-	-	-	548	548
Deferred income tax liability	-	-	-	-	6,390	6,390
Other liabilities	-	-	-	-	5,052	5,052
Total liabilities	821,192	200,602	543,239	370,141	11,990	1,947,164
Net sensitivity gap	(151,224)	(52,717)	(136,967)	430,444	161,798	251,334
Cumulative sensitivity gap at 31 December 2005	(151,224)	(203,941)	(340,908)	89,536	251,334	-

23 Financial Risk Management (Continued)

The following table summarises the Bank's exposure to interest rate risks at 31 December 2004 by showing assets and liabilities in categories based on the earlier of contractual repricing or maturity dates.

<i>In thousands of Ukrainian hryvnias</i>	Demand and less than 1 month	From 1 to 3 months	From 3 to 12 months	More than 1 year	Non-interest bearing	Total
Assets						
Cash and cash equivalents and mandatory reserve balances	191,714	-	-	-	-	191,714
Other securities at fair value through profit or loss	28	-	-	14,008	4,704	18,740
Due from other banks	76,429	-	1,923	4,057	-	82,409
Loans and advances to customers	193,035	181,448	407,172	414,484	-	1,196,139
Investment securities available for sale	-	-	4,465	710	1,301	6,476
Guarantee deposits with the National Bank of Ukraine	29,738	-	-	-	-	29,738
Deferred income tax asset	-	-	-	-	2,562	2,562
Intangible assets	-	-	-	-	788	788
Premises and equipment	-	-	-	-	52,898	52,898
Other assets	-	-	-	-	4,303	4,303
Total assets	490,944	181,448	413,560	433,259	66,556	1,585,767
Liabilities						
Due to the National Bank of Ukraine	41,333	-	-	-	-	41,333
Due to other banks	135,315	58,019	93,159	4,819	-	291,312
Customer accounts	406,028	104,939	439,432	110,944	-	1,061,343
Debt securities in issue	-	5,432	18,139	-	-	23,571
Current income tax liability	-	-	-	-	355	355
Other liabilities	-	-	-	-	8,454	8,454
Total liabilities	582,676	168,390	550,730	115,763	8,809	1,426,368
Net sensitivity gap	(91,732)	13,058	(137,170)	317,496	57,747	159,399
Cumulative sensitivity gap at 31 December 2004	(91,732)	(78,674)	(215,844)	101,652	159,399	-

The Bank is exposed to fair value interest rate risk as a result of assets and liabilities at fixed interest rates; these are primarily presented in the above table as being repriced in the long-term. In practice, interest rates that are contractually fixed on both assets and liabilities are usually renegotiated to reflect current market conditions.

The Board of Directors monitors on a daily basis and sets limits on the level of mismatch of interest rate repricing that may be undertaken. In the absence of any available hedging instruments, the Bank normally seeks to match its interest rate positions.

23 Financial Risk Management (Continued)

The table below summarises the effective interest rates by major currencies for major debt instruments. The analysis has been prepared based on period-end effective rates used for amortisation of the respective assets/liabilities.

<i>in %</i>	2005			2004		
	USD	UAH	Euro	USD	UAH	Euro
Assets						
Nostro balances with other banks	2	3	1	3	5	3
Other debt securities at fair value through profit or loss	-	15	-	-	10	-
Due from other banks	3	5	-	1	-	1
Loans and advances to customers	13	17	12	14	18	15
Debt investment securities available for sale	-	19	-	-	15	-
Liabilities						
Due to other banks	8	7	10	9	15	11
Customer accounts						
- current and settlement accounts	1	2	1	2	4	1
- term deposits	10	15	9	11	16	8
Debt securities in issue	3	15	-	12	19	-
Subordinated debt	10	-	10	-	-	-

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

24 Contingencies and Commitments

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

Tax legislation. Ukrainian tax, currency and customs legislation is subject to varying interpretations, and changes, which can occur frequently. Management’s interpretation of such legislation as applied to the transactions and activity of the Bank may be challenged by the relevant authorities. The tax authorities may be taking a more assertive position in their interpretation of the legislation and assessments, and it is possible that transactions and activities that have not been challenged in the past may be challenged. As a result, significant additional taxes, penalties and interest may be assessed. Fiscal periods remain open to review by the authorities in respect of taxes for three calendar years preceding the year of review. Under certain circumstances reviews may cover longer periods.

The tax consequence of transactions for Ukrainian taxation purposes is frequently determined by the form in which transactions are documented and the underlying accounting treatment prescribed by Ukrainian Accounting Rules. Accordingly, the Bank structures certain transactions so as to take advantage of such form driven determinations to reduce the overall effective tax rate of the Bank. The income statement as presented in these financial statements includes reclassifications to reflect the underlying economic substance of those transactions.

The Bank’s Management believes that its interpretation of the relevant legislation is appropriate and the Bank’s tax, currency legislation and customs positions will be sustained.

24 Contingencies and Commitments (Continued)

Capital expenditure commitments. At 31 December 2005 the Bank has contractual capital expenditure commitments in respect of construction of premises totalling UAH 67,425 thousand (2004: UAH 63,600 thousand).

Operating lease commitments. Where the Bank is the lessee, the future minimum lease payments under non-cancellable operating leases are as follows:

<i>In thousands of Ukrainian hryvnias</i>	2005	2004
Not later than 1 year	4,945	7,206
Later than 1 year and not later than 5 years	4,711	11,560
Later than 5 years	304	1,976
Total operating lease commitments	9,960	20,742

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, which represent irrevocable assurances that the Bank will make payments in the event that a customer cannot meet its obligations to third parties, carry the same credit risk as loans. Documentary and commercial letters of credit, which are written undertakings by the Bank on behalf of a customer 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 or cash deposits and therefore carry less risk than a direct borrowing.

Undrawn credit lines represent unused portions of authorisations to extend credit in the form of loans, guarantees or letters of credit. 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 monitors the term to maturity of credit related commitments because longer-term commitments generally have a greater degree of credit risk than shorter-term commitments. Outstanding credit related commitments are as follows:

<i>In thousands of Ukrainian hryvnias</i>	Note	2005	2004
Undrawn credit lines		11,066	6,024
Import letters of credit	15	3,752	3,237
Guarantees issued	15	87,569	52,395
Less: Provision for losses on credit related commitments		(2,908)	(3,582)
Total credit related commitments		99,479	58,074

The total outstanding contractual amount of undrawn credit lines, letters of credit and guarantees does not necessarily represent future cash requirements, as these financial instruments may expire or terminate without being funded.

24 Contingencies and Commitments (Continued)

Movements in the provision for losses on credit related commitments are as follows:

	Note	2005	2004
Provision for losses on credit related commitments as at 1 January		3,582	2,148
(Recovery of)/provision for losses on credit related commitments during the year		(674)	1,434
Provision for losses on credit related commitments as at 31 December	17	2,908	3,582

Fiduciary activities. These assets are not included in the Bank's balance sheet as they are not assets of the Bank. Nominal values disclosed below are normally different from the fair values of respective securities. The fiduciary assets fall into the following categories:

<i>In thousands of Ukrainian hryvnias</i>	2005 Nominal value	2004 Nominal value
Shares in companies held on behalf of the Banks's customers	637,832	499,601

Assets pledged and restricted. At 31 December 2005 the Bank has the following assets pledged as collateral:

<i>In thousands of Ukrainian hryvnias</i>	Notes	2005		2004	
		Asset pledged	Related liability	Asset pledged	Related liability
Currency swap agreements with the National Bank of Ukraine		-	-	29,738	29,502
Loans and advances to customers	11, 14	46,593	13,957	-	-
Other securities at fair value through profit or loss		-	-	14,036	11,800
Total		46,593	13,957	43,774	41,302

In addition, mandatory cash balances with the NBU in the amount of UAH 124,257 thousand (2004: UAH 71,201 thousand) represent mandatory reserve deposits which are not available to finance the Bank's day to day operations.

Guarantee deposits in the amount of UAH 12,652 thousand (2004: UAH 17,998 thousand) represent balances placed with other banks as cover for guarantees and import letters of credit. These are effectively restricted deposits, which are required to be maintained to complete the related trade financing activity.

25 Fair Value of Financial Instruments

Fair value is the amount at which a financial instrument could be exchanged in a current transaction between willing parties, other than in a forced sale or liquidation, and is best evidenced by an active quoted market price.

The estimated fair values of financial instruments have been determined by the Bank using available market information, where it exists, and appropriate valuation methodologies. However, judgement is necessarily required to interpret market data to determine the estimated fair value. Ukraine continues to display some characteristics of an emerging market and economic conditions continue to limit the volume of activity in the financial markets. Market quotations may be outdated or reflect distress sale transactions and therefore not represent fair values of financial instruments. Management has used all available market information in estimating the fair value of financial instruments.

Financial instruments carried at fair value. Trading securities, other securities at fair value through profit or loss and investment securities available for sale are carried on the balance sheet at their fair value. Cash and cash equivalents are carried at amortised cost which approximates current fair value.

25 Fair Value of Financial Instruments (Continued)

Fair values were determined based on quoted market prices except for certain investment securities available for sale for which there were no available external independent market price quotations. These securities have been fair valued by the Bank on the basis of results of recent sales of equity interests in the investees between unrelated third parties, consideration of other relevant information such as discounted cash flows and financial data of the investees and application of other valuation methodologies. Valuation techniques required certain assumptions that were not supported by observable market data. Changing any such used assumptions to a reasonably possible alternative would not result in a significantly different profit, income, total assets or total liabilities.

Loans and receivables carried at amortised cost. 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 12 % to 18 % per annum (2004: 13 % to 20 % per annum). Refer to Notes 10 and 11 for the estimated fair values of due from other banks and loans and advances to customers, respectively.

Liabilities carried at amortised cost. The fair value is based on quoted market prices, if available. The estimated fair value of fixed interest rate instruments with stated maturity, for which a quoted market price is not available, was estimated based on expected cash flows discounted at current interest rates for new instruments with similar credit risk and remaining maturity. The fair value of liabilities repayable on demand or after a notice period (“demandable liabilities”) is estimated as the amount payable on demand, discounted from the first date that the amount could be required to be paid. Refer to Notes 14, 15 and 16 for the estimated fair values of due to other banks, customer accounts and subordinated debt respectively.

26 Related Party Transactions

For the purposes of these financial statements, parties are considered to be related if one party has the ability to control the other party, is under common control, or can exercise significant influence over the other party in making financial or operational decisions. In considering each possible related party relationship, attention is directed to the substance of the relationship, not merely the legal form.

At 31 December 2005, the outstanding balances with related parties were as follows:

<i>In thousands of Ukrainian hryvnias</i>	Ultimate shareholders	Other signifi- cant share- holders	Entities under common control	Other related parties
Gross amount of loans and advances to customers (contractual interest rate: 8 - 16 %)	330	36	84,837	1,333
Impairment provisions for loans and advances to customers at 31 December	(6)	(2)	(9,456)	(188)
Investment securities available for sale				
- Debt securities (contractual interest rate: 15 %)	-	-	15,022	-
- Shares of JSC Kotovskoe ZPP (10 % holding)	-	-	1,533	-
Due to other banks (contractual interest rate: 8 - 12 %)	-	-	160,882	-
Customer accounts (contractual interest rate: 2 - 18 %)	287	16,840	3,279	957
Debt securities in issue (contractual interest rate: 15 %)	5,000	17,000	-	-

26 Related Party Transactions (Continued)

The income and expense items with related parties for the year 2005 were as follows:

<i>In thousands of Ukrainian hryvnias</i>	Ultimate shareholders	Other signifi- cant share- holders	Entities under common control	Other related parties
Interest income	16	362	9,892	2,644
Interest expense	1,423	1,227	19,147	2,624
Provision for loan impairment	(13)	(900)	5,365	171
Gains less losses from trading in foreign currencies	-	-	75	-
Fee and commission income	-	7	611	14
Losses on initial recognition of assets at rates below market	-	-	191	-
Administrative and other operating expenses	-	4,489	5,212	463

At 31 December 2005, other rights and obligations with related parties were as follows:

<i>In thousands of Ukrainian hryvnias</i>	Ultimate shareholders	Other signifi- cant share- holders	Entities under common control	Other related parties
Guarantees issued by the Bank at the year end	-	-	-	1,120

Aggregate amounts lent to and repaid by related parties during 2005 were:

<i>In thousands of Ukrainian hryvnias</i>	Ultimate shareholders	Other signifi- cant share- holders	Entities under common control	Other related parties
Amounts lent to related parties during the period	383	17,502	99,974	18,625
Amounts repaid by related parties during the period	325	30,497	87,730	17,410

26 Related Party Transactions (Continued)

At 31 December 2004, the outstanding balances with related parties were as follows:

<i>In thousands of Ukrainian hryvnias</i>	Ultimate shareholders	Other signifi- cant share- holders	Entities under common control	Other related parties
Gross amount of loans and advances to customers (contractual interest rate: 12 - 18%)	272	13,031	72,593	118
Impairment provisions for loans and advances to customers at 31 December	(19)	(902)	(4,091)	(17)
Investment securities available for sale				
- Debt securities (contractual interest rate: 15 %)	-	-	4,056	-
- Shares of JSC Kotovskoe ZPP (10 % holding)	-	-	1,153	-
Due to other banks (contractual interest rate: 9 - 11 %)	-	-	248,945	-
Customer accounts (contractual interest rate: 9 - 21 %)	2,829	61,820	39,853	469

The income and expense items with related parties for the year 2004 were as follows:

<i>In thousands of Ukrainian hryvnias</i>	Ultimate shareholders	Other signifi- cant share- holders	Entities under common control	Other related parties
Interest income	33	1,624	9,623	12
Interest expense	220	3,020	19,683	16
Provision for loan impairment	3	163	738	3
Gains less losses from trading securities	-	(2,076)	619	-
Fee and commission income	-	15	278	5
Losses on initial recognition of assets at rates below market	-	-	(36)	-
Gains/(losses) on initial recognition of liabilities at rates below/above market	-	800	(1,713)	-
Administrative and other operating expenses	-	5,150	256	-

Aggregate amounts lent to and repaid by related parties during 2004 were:

<i>In thousands of Ukrainian hryvnias</i>	Ultimate shareholders	Other signifi- cant share- holders	Entities under common control	Other related parties
Amounts lent to related parties during the period	282	24,325	46,166	88
Amounts repaid by related parties during the period	347	16,331	50,357	25

The Bank is ultimately controlled by Mr Rodin Y.O. and Mr Bekker M.I. (2004: Mr Rodin Y.O. and Mr Bekker M.I.).

In 2005, the remuneration of members of the Board of Directors comprised salaries, discretionary bonuses and other short-term benefits totalling to UAH 786 thousand (2004: UAH 696 thousand).

27 Subsequent Events

According to a decision of shareholders meeting of 8 February 2006, the Bank announced a new share issue with a nominal value of UAH 50,000 thousand. This share issue was fully paid up and registered by 31 March 2006.

After the balance sheet date, on January 2006, the Bank acquired 49% of the share capital of Regional Investment Bank, Latvia.