

CAPITRON BANK LLC

Audited Financial Statements

31 December 2003

CAPITRON BANK LLC

CORPORATE INFORMATION

REGISTERED OFFICE : Capitron Bank Building
Peace Avenue
Ulaanbaatar 21064

BOARD OF DIRECTORS : Joel Cachet
O. Enkhbayar
D. Oma
B. Saran
P. Byambasuren
Ts. Erdene
B. Altankhuyag

COMPANY SECRETARY : T. Aldarmaa

AUDITORS : Ernst & Young Mongolia Audit LLC
Certified Public Accountants

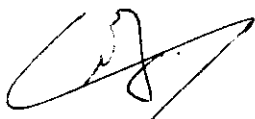
CAPITRON BANK LLC

**FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2003**

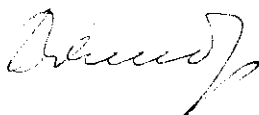
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STATEMENT BY DIRECTORS AND EXECUTIVE

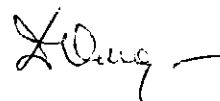
We, JOEL CACHET and P. BYAMBASUREN two of the directors of CAPITRON BANK LLC ("the Bank"), and D. OMA, being the officer primarily responsible for the financial management of the Bank, do hereby state that, in our opinion, the accompanying financial statements set out on pages 3 to 30 are drawn up in accordance with applicable International Financial Reporting Standards and Regulations issued by the Bank of Mongolia so as to give a true and fair view of the financial position of the Bank as at 31 December 2003 and of the results and the cash flows of the Bank for the year then ended.



JOEL CACHET



P. BYAMBASUREN



D. OMA

Ulaanbaatar
24 April 2004

REPORT OF THE AUDITORS

To the Board of Directors of Capitron Bank LLC

We have audited the accompanying financial statements of Capitron Bank LLC as at 31 December 2003 set out on pages 3 to 30. These financial statements are the responsibility of the Bank's directors. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with applicable 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 the directors, as well as evaluating the overall presentation of the financial statements. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the financial statements have been properly drawn up in accordance with applicable International Financial Reporting Standards and Regulations issued by Bank of Mongolia so as to give a true and fair view of the financial position of the Bank as of 31 December 2003 and of the results and the cash flows for the year then ended.

Without qualifying our opinion we draw attention to Note 15 to the financial statements. The Bank is in the midst of finalising the transfer of rights and ownership of certain assets to its name from a borrower. The Bank has represented that the rights and ownership of these assets have been reserved under its name and legal transfer of the title and ownership is in progress. The ultimate outcome of the matter cannot presently be determined and no provision for loan losses that may result had been made in the financial statements.

Erni + Young Mongol Audit Co.

Ulaanbaatar
24 April 2004

CAPITRON BANK LLC

INCOME STATEMENT FOR THE YEAR ENDED 31 DECEMBER 2003

	Note	2003 MNT '000	2002 MNT '000
Interest income	4	4,346,729	2,454,498
Interest expense	5	<u>(2,598,784)</u>	<u>(1,246,998)</u>
Net interest income		1,747,945	1,207,500
Non-interest income	6	<u>271,714</u>	<u>95,409</u>
Operating profit		2,019,659	1,302,909
Operating expenses	7	<u>(1,139,839)</u>	<u>(601,899)</u>
Profit before provisions		879,820	701,010
Provisions	8	<u>(884,095)</u>	<u>(163,110)</u>
(Loss)/profit before taxation		(4,275)	537,900
Taxation	9	<u>-</u>	<u>(235,559)</u>
(Loss)/profit after taxation		<u>(4,275)</u>	<u>302,341</u>

The accompanying notes form an integral part of the financial statements.

CAPITRON BANK LLC

BALANCE SHEET AS AT 31 DECEMBER 2003

	Note	2003 MNT '000	2002 MNT '000
ASSETS			
Cash and short term funds	12	1,771,658	528,102
Deposits and placements with other banks and financial institutions	13	4,563,056	2,699,699
Investment in securities	14	1,792,058	2,848,695
Loans and advances	15	17,201,620	11,944,160
Other assets	16	296,039	44,999
Tax recoverable	17	35,000	-
Property, plant and equipment	18	747,563	420,756
TOTAL ASSETS		<u>26,406,994</u>	<u>18,486,411</u>
LIABILITIES			
Deposits from customers	19	22,341,185	14,151,089
Deposits and placements of other banks and financial institutions	20	-	500,000
Other liabilities	21	69,876	29,378
TOTAL LIABILITIES		<u>22,411,061</u>	<u>14,680,467</u>
EQUITY			
Statutory fund	22	4,000,000	3,500,000
(Accumulated loss)/retained earnings		(4,275)	305,941
Social development fund	11	208	3
TOTAL EQUITY		<u>3,995,933</u>	<u>3,805,944</u>
TOTAL EQUITY AND LIABILITIES		<u>26,406,994</u>	<u>18,486,411</u>
OFF BALANCE SHEET ITEMS	26	<u>372,217</u>	<u>82,863</u>

The accompanying notes form an integral part of the financial statements.

CAPITRON BANK LLC

**STATEMENT OF CHANGES IN EQUITY
FOR THE YEAR ENDED 31 DECEMBER 2003**

	Note	Statutory <u>fund</u> MNT'000	Retained earnings/ (accumulated <u>loss</u>) MNT'000	<u>Total</u> MNT'000
At 1 January 2002		3,000,000	4,000	3,004,000
Profit for the year		-	302,341	302,341
Transfer to Social Development Fund		-	(400)	(400)
Issue of shares		500,000	-	500,000
At 31 December 2002		<u>3,500,000</u>	<u>305,941</u>	<u>3,805,941</u>
Loss for the year		-	(4,275)	(4,275)
Dividends	10	-	(285,941)	(285,941)
Transfer to Social Development Fund	11	-	(20,000)	(20,000)
Issue of shares		500,000	-	500,000
At 31 December 2003		<u>4,000,000</u>	<u>(4,275)</u>	<u>3,995,725</u>

The accompanying notes form an integral part of the financial statements.

CAPITRON BANK LLC

**CASH FLOW STATEMENT
FOR THE YEAR ENDED 31 DECEMBER 2003**

	2003	2002
	MNT '000	MNT '000
CASH FLOWS FROM OPERATING ACTIVITIES		
(Loss)/profit before taxation	(4,275)	537,900
<i>Adjustments for :-</i>		
Depreciation of property, plant and equipment	87,829	32,552
Provisions for other assets	2,583	-
Net provision on loan losses	881,512	163,110
Operating profit before working capital changes	<u>967,649</u>	<u>733,562</u>
<i>Increase in operating assets:-</i>		
Loans and advances	(6,138,972)	(9,646,847)
Other assets	(253,623)	(36,698)
<i>Increase/(decrease) in operating liabilities</i>		
Deposits from customers	8,190,096	13,377,739
Deposits and placements of other banks and financial institutions	(500,000)	500,000
Social Development Fund expenses	(19,795)	(397)
Other liabilities	40,498	28,453
Cash generated from operations	<u>2,285,853</u>	<u>4,955,812</u>
Income tax paid	(35,000)	(235,559)
Net cash flow from operating activities	<u>2,250,853</u>	<u>4,720,253</u>
CASH FLOW FROM INVESTING ACTIVITIES		
Net decrease / (increase) in investment securities	1,056,637	(2,848,695)
Proceeds on disposal of property , plant and equipment	-	512
Purchase of property, plant and equipment	(414,636)	(340,531)
Net cash flow from investing activities	<u>642,001</u>	<u>(3,188,714)</u>
CASH FLOWS FROM FINANCING ACTIVITIES		
Increase in statutory fund	500,000	500,000
Dividends paid	(285,941)	-
Net cash flow from financing activities	<u>214,059</u>	<u>500,000</u>
Net increase in cash and cash equivalents	3,106,913	2,031,539
Cash and cash equivalents brought forward	<u>3,227,801</u>	<u>1,196,262</u>
Cash and cash equivalents carried forward	<u>6,334,714</u>	<u>3,227,801</u>
Cash and cash equivalents comprises:		
Cash and short term funds	1,771,658	528,102
Deposits and placement with other banks and financial institutions	4,563,056	2,699,699
	<u>6,334,714</u>	<u>3,227,801</u>

The accompanying notes form an integral part of the financial statements.

CAPITRON BANK LLC

NOTES TO THE FINANCIAL STATEMENTS - 31 DECEMBER 2003

1. CORPORATE INFORMATION

The Bank is principally engaged in the business of provision of banking and financial services pursuant to License No. 22 issued by Bank of Mongolia. There have been no significant changes in the nature of these activities during the year.

The Bank is a public limited liability company, incorporated and domiciled in Mongolia. The registered address and the principal place of business of the Bank is Capitron Bank Building, Peace Avenue, Ulaanbaatar-210648, Mongolia.

These financial statements of the Bank for the year ended 31 December 2003 were authorised for issue by the Board of Directors in accordance with a resolution of the directors on 24 April 2004.

2. BASIS OF PREPARATION

These financial statements have been prepared in accordance with applicable International Financial Reporting Standards and Regulations issued by Bank of Mongolia.

The financial statements have been prepared under the historical cost convention. The reporting currency used in the financial statements is the Mongolian Togrog, which is denoted by the symbol MNT, shown rounded to the nearest thousand.

3. SIGNIFICANT ACCOUNTING POLICIES

(a) Interest Income and Expense

Interest income and expense are recognised in the income statement for all interest bearing instruments on an accrual basis using the effective yield method based on the actual purchase price. The recognition of interest income is suspended when loans are outstanding for more than ninety days, in accordance with the requirements of Bank of Mongolia. On commencement of suspension, previously accrued interest not received is clawed-back. Recognition of interest subsequent to suspension is on a cash basis. Interest recognition will resume on an accruals basis when the uncertainties surrounding the recoverability are removed and the loan is reclassified as performing.

(b) Fee and Commission Income

Fee and commission income are generally recognised on an accrual basis when the service has been provided. Types of fees and commission income derived by the Bank relate mainly to loan processing fees, guarantee fees, service charges for credit cards and money transfer commissions.

3. SIGNIFICANT ACCOUNTING POLICIES (CONTD.)

(c) Foreign Currencies

Transactions in foreign currencies are initially recorded in Togrog at rates of exchange ruling at the date of the transaction. At each balance sheet date, foreign currency monetary items are translated into Togrog at exchange rates ruling at that date, unless hedged by forward foreign exchange contracts, in which case the rates specified in such forward contracts are used. Non-monetary items initially denominated in foreign currencies, which are carried at historical cost are translated using the historical rate as of the date of acquisition and non-monetary items which are carried at fair value are translated using the exchange rate that existed when the values were determined. All exchange rate differences are taken to the income statement.

The principal exchange rates used for every unit of foreign currency ruling at the balance sheet date are as follows:

	2003	2002
United States Dollar	1,168.00	1,125.00
Great Britain Pound	2,073.40	1,804.00
European Euro	1,460.20	1,169.40
Japanese Yen	10.92	9.38
Swiss Francs	935.70	804.00
Chinese Yuan	141.20	135.80

(d) Loans and Advances and Provision for Loan Loss

Loans originated by the Bank by providing money directly to the borrower at draw down are categorised as loans and advances. Third party expenses, such as legal fees, incurred in securing a loan are treated as part of the cost of the transaction.

All loans and advances are recognised when cash is advanced to borrowers.

Provision for loan loss are made as considered necessary having regard to both specific and general factors. In determining the need for provisions, management considers, among other things, the financial position of the borrowers, the value of any collateral and guarantees received, industry performance, current economic conditions and past experiences. Provision made during the year are charged against the income statement.

The maturity of the loan portfolio is presented in Note 15 which shows the remaining period of loans from the balance sheet date to the contractual maturity. Long-term credits are generally not available in Mongolia except for programs set up by international financial institutions and under government financing arrangements. However, in the Mongolian marketplace, short-term credits are granted with the expectation of renewing the loans at maturity.

3. SIGNIFICANT ACCOUNTING POLICIES (CONTD.)

(e) Taxation

The Bank provides for income tax based on its income for financial reporting purposes, adjusted for items which are not assessable or deductible for income tax purpose, in accordance with the regulations of the Mongolian Government and is measured using the tax rates that have been enacted at the balance sheet date.

(f) Cash and Cash Equivalents

For the purposes of the cash flow statement, cash and cash equivalents consist of cash and short term funds, deposits and placements with other banks and financial institutions that are readily convertible to cash with insignificant risk of changes in value.

(g) Investment Securities

Investment securities are securities that are acquired and held for yield or capital growth and are usually held to maturity.

Corporate bonds and Bank of Mongolia Treasury Bills are stated at cost adjusted for amortisation of premiums or accretion of discounts, where applicable, to maturity dates.

Quoted investments are stated at the lower of cost and market value.

Unquoted investments are stated at cost and where applicable, adjusted for amortisation of premiums or accretion of discounts to maturity dates. Provision is made for diminution in value which is other than temporary.

On disposal of the investment securities, the differences between the net disposal proceeds and their carrying amounts are charged or credited to the income statement.

(h) Property, Plant and Equipment

Property, plant and equipment are stated at cost less accumulated depreciation and impairment losses. The policy for the recognition and measurement of impairment losses is in accordance with Note 3 (j).

The estimated useful lives used by the Bank are as follows :

	Rates
Buildings	40 years
Furniture, fixtures and vehicles	10 years
Computers	5 years

Assets under construction are not depreciated. Depreciation of these assets begins when the related assets are placed in service.

3. SIGNIFICANT ACCOUNTING POLICIES (CONTD.)

(h) Property, Plant and Equipment (Contd.)

Upon disposal of an item of property, plant or equipment, the difference between the net disposal proceeds and the net carrying amount is recognised in the income statement.

(i) Customer Deposits

Deposits from customers are stated at cost which is the fair value of the consideration to be paid in the future for deposits received.

(j) Impairment of Assets

The Bank reviews the carrying amounts of its assets to determine whether there is any indication that those assets have suffered an impairment loss. If any such indication exists, impairment is measured by comparing the carrying values of the assets with their recoverable amounts. Recoverable amount is the higher of net selling price and value in use, which is measured by reference to discounted future cash flows.

An impairment loss is charged to the income statement immediately, unless the asset is carried at revalued amount. Any impairment loss of a revalued asset is treated as a revaluation decrease to the extent of any available previously recognised revaluation surplus for the same asset. Reversal of impairment losses recognised in prior years is recorded when there is an indication that the impairment losses recognised for the asset no longer exist or have decreased.

(k) Employee Benefits

(i) Short term benefits

Wages, salaries and other salary related expenses are recognised as an expense in the year in which the associated services are rendered by employees of the Bank. Short term accumulating compensated absences such as paid annual leave are recognised when services rendered by employees that increase their entitlement to future compensated absences and short term non-accumulating compensated absences such as sick leave are recognised when absences occur.

(ii) Defined contribution plans

As required by the law, companies in Mongolia make contributions to the government pension scheme, Social Security and Health Fund. Such contributions are recognised as an expense in the income statement as incurred.

(l) Financial Instruments

Financial instruments are recognised in the balance sheet when the Bank has become a party to the contractual provisions of the instrument. The accounting policies on recognition and measurement of these items are disclosed in their respective accounting policies.

3. SIGNIFICANT ACCOUNTING POLICIES (CONTD.)

(l) Financial Instruments (Contd.)

Financial instruments are classified as liabilities or equity in accordance with the substance of the contractual arrangement. Interest, dividends and gains and losses relating to a financial instrument classified as a liability, are reported as expense or income. Distributions to holders of financial instruments classified as equity are charged directly to equity. Financial instruments are offset when the Bank has a legally enforceable right to offset and intends to settle either on a net basis or to realise the asset and settle the liability simultaneously.

(i) Equity Instruments

Statutory fund is classified as equity and dividends are recognised in equity in the period in which they are declared.

(ii) Derivative Financial Instruments

Derivative financial instruments are not recognised in the financial statements on inception.

Forward foreign exchange contracts

The underlying foreign currency assets or liabilities are translated at their respective hedged exchange rate and all gains and losses are recognised as income or expense in the income statement in the same period as the exchange differences on the underlying hedged items. Exchange gains or losses arising on contracts entered into as hedges of anticipated future transactions are deferred until the date of such transaction, at which time they are included in the measurement of such transaction.

4. INTEREST INCOME

	2003	2002
	MNT '000	MNT '000
Loans and advances	4,049,511	2,364,236
Deposits and placements with other		
banks and financial institutions	58,055	13,424
Bank of Mongolia treasury bills	181,262	71,438
Corporate bonds	57,901	5,400
	<u>4,346,729</u>	<u>2,454,498</u>

5. INTEREST EXPENSE

	2003 MNT '000	2002 MNT '000
Deposits from customers	2,567,284	1,169,928
Deposits and placements of other banks and financial institutions	31,500	77,070
	<u>2,598,784</u>	<u>1,246,998</u>

6. NON-INTEREST INCOME

	2003 MNT '000	2002 MNT '000
Fee income and commission income:		
Commission	188,949	74,936
Service charges and fees	11,081	2,089
Guarantee fees	2,593	1,991
	<u>202,623</u>	<u>79,016</u>
Other income:		
Realised foreign currency gain	39,487	18,410
Unrealised foreign currency gain/(loss)	20,773	(5,417)
Other operating income	8,831	3,400
	<u>69,091</u>	<u>16,393</u>
Total non-interest income	<u>271,714</u>	<u>95,409</u>

7. OPERATING EXPENSES

	2003 MNT '000	2002 MNT '000
Salaries and related expenses	270,102	120,760
Rental of premises	250,820	133,501
Depreciation of property, plant and equipment	87,829	32,552
Maintenance of property, plant and equipment	82,720	66,451
Membership and auditing fees	82,616	98,262
Advertising	69,566	48,830
Stationery	58,479	16,924
Business trips	46,438	21,060
Communications	45,195	17,012
Security and safety expense	35,652	15,251
Tender costs	28,032	-
Transportation and fuel supplies	24,708	15,264
Balance carried forward	<u>1,082,157</u>	<u>585,867</u>

7. OPERATING EXPENSES (CONTD.)

	2003	2002
	MNT '000	MNT '000
Balance brought forward	1,082,157	585,867
Finance charges	12,281	493
Loan and collection expense	10,972	1,707
Entertainment	7,142	4,249
Cash collection service	6,554	4,209
Training	5,123	2,313
Other operating expenses	15,610	3,061
	<u>1,139,839</u>	<u>601,899</u>

The average number of persons employed by the Bank during the year was made up as follows:

	2003	2002
	Number	Number
Directors and head of departments	15	5
Branch managers	7	2
Officers and clerks	85	49
	<u>107</u>	<u>56</u>
Of which:		
- Head office	75	47
- Branches	32	9
	<u>107</u>	<u>56</u>

8. PROVISIONS

	2003	2002
	MNT '000	MNT '000
Provision for loan losses	881,512	163,110
Provision for other assets	2,583	-
	<u>884,095</u>	<u>163,110</u>

9. TAXATION

	2003	2002
	MNT '000	MNT '000
Mongolian taxation based on results for the year		
- Current	-	235,539
	<u>-</u>	<u>235,539</u>

9. TAXATION (CONTD.)

Mongolian legal entities must individually report taxable income and remit income taxes thereon to the appropriate authorities. The income tax rate for the bank's profits is 15% for the first MNT100 million of taxable income, and 40% on the excess of taxable income over MNT100 million. Interest income on government bonds is not subject to income tax. The provision for probable loan losses is deductible for income tax purposes.

A reconciliation of income tax expense applicable to profit before taxation at the statutory income tax rate to income tax expense at the effective income tax rate of the Bank is as follows:

	2003 MNT '000	2002 MNT '000
Income tax at statutory rates based on profit before taxation	-	201,410
Tax exempt income	-	-
Non-deductible expenses	-	24,848
Over provision in current year	-	8,199
Overprovision in prior year	-	1,102
Tax expense for the year	<u>-</u>	<u>235,559</u>

Management believes that the Bank is in substantial compliance with the tax laws affecting its operations.

10. DIVIDENDS

Equity dividends on ordinary shares

	2003 MNT '000	2002 MNT '000
Declared and paid in the year	<u>285,941</u>	<u>-</u>
Dividends per share (MNT)	<u>81.70</u>	<u>-</u>

Dividends declared was in respect of financial year ended 31 December 2002.

11. SOCIAL DEVELOPMENT FUND

Social development fund represents funds allocated for the purposes of employees' social and welfare expenses. During the year, at the Shareholders' Meeting of the Bank on 11th April 2003, a distribution of retained earnings to the social development fund of the Bank amounting to MNT20,000,000 (2002: MNT400,000) was approved.

11. SOCIAL DEVELOPMENT FUND (CONTD.)

	2003 MNT '000	2002 MNT '000
Balance brought forward	3	-
Transfer to social development fund	20,000	400
Expenses for the year	(19,795)	(397)
Balance carried forward	<u>208</u>	<u>3</u>

12. CASH AND SHORT TERM FUNDS

	2003 MNT '000	2002 MNT '000
Cash and bank balances denominated in local currencies	593,510	306,985
Cash and bank balances denominated in foreign currencies	1,178,148	221,117
	<u>1,771,658</u>	<u>528,102</u>

13. DEPOSITS AND PLACEMENTS WITH OTHER BANKS AND FINANCIAL INSTITUTIONS

	2003 MNT '000	2002 MNT '000
Balances with Bank of Mongolia	2,763,249	2,141,903
Placements with other banks and financial institutions	1,799,807	557,796
	<u>4,563,056</u>	<u>2,699,699</u>

Balances with Bank of Mongolia are maintained in accordance with Bank of Mongolia requirements and bear no interest. The balances maintained with Bank of Mongolia are determined at set percentages based on 15 days average cash balances.

Placements with other banks and financial institutions represent foreign currency current accounts maintained with foreign financial institutions, which are generally denominated in United States Dollar ("USD") and bear interest of 3.60% to 8.25% per annum (2002 : 3.60% per annum).

14. INVESTMENT IN SECURITIES

	2003 MNT '000	2002 MNT '000
Bank of Mongolia treasury bills	1,203,154	2,784,625
Corporate bonds	545,611	50,000
	<u>1,748,765</u>	<u>2,834,625</u>
Accretion of discounts	43,293	14,070
Net balance of investment in securities	<u>1,792,058</u>	<u>2,848,695</u>

14. INVESTMENT IN SECURITIES (CONTD.)

Bank of Mongolia treasury bills are interest bearing short term bills with maturities of less than three months, and are issued at a discount. The effective annual interest rates of these bills range from 3.95% to 14.46% per annum (2002 : 7.23% to 12.13% per annum).

Corporate bonds are issued by a non-banking financial institution with maturity of less than one year. Annual interest rates are in the range of 20.40% to 21.60% per annum (2002: 21.60% per annum).

15. LOANS AND ADVANCES

	2003 MNT '000	2002 MNT '000
Term loans	18,111,342	12,125,718
Staff loans	26,489	5,822
Gross loans and advances	<u>18,137,831</u>	<u>12,131,540</u>
Provision for loan losses		
- specific	(773,800)	(73,000)
- general	(162,411)	(114,380)
Net loans and advances	<u>17,201,620</u>	<u>11,944,160</u>
Maturity structure		
Maturing within one year	16,875,400	10,982,400
One to five years	326,220	961,760
	<u>17,201,620</u>	<u>11,944,160</u>

Loans and advances analysed by their economic purpose are as follows:

	2003 MNT '000	2002 MNT '000
Trading	6,026,732	4,224,087
Processing related industries	4,501,154	2,373,566
Construction	2,199,237	2,017,011
Mining related	1,662,335	958,446
Services	1,394,338	1,615,759
Tourism	51,100	265,810
Utilities	1,238	-
Agriculture	-	67,100
Others	2,301,697	609,761
	<u>18,137,831</u>	<u>12,131,540</u>

Others include individuals and companies in industries such as financial, health, education, consumption and transportation.

15. LOANS AND ADVANCES (CONTD.)

Movements in the non-performing loans ("NPL") are as follows:

	2003 MNT '000	2002 MNT '000
Balance at beginning of year	510,000	-
NPL during the year - gross	2,808,420	529,083
Recoveries/regularised during the year	(1,234,994)	(18,500)
Amount written off	(151,500)	(583)
Transferred to other assets	(158,000)	-
Exchange rate loss	8,845	-
Gross balance at end of year	<u>1,782,771</u>	<u>510,000</u>
Less: Specific Provision	<u>(773,800)</u>	<u>(73,000)</u>
Net balance at end of year	<u>1,008,971</u>	<u>437,000</u>
Gross NPL ratio as a percentage of gross total loans	9.8%	4.2%
Net NPL ratio as a percentage of net total loans	5.9%	3.7%

Movements in the provision for loan losses are as follows:

	2003 MNT '000	2002 MNT '000
Specific Provision		
Balance at beginning of year	73,000	-
Provision made during the year	983,719	68,477
Amount written back in respect of recoveries	(159,926)	(185)
Transferred from general provision	28,054	5,291
Amount written off	(151,500)	(583)
Exchange rate loss	453	-
Balance at end of year	<u>773,800</u>	<u>73,000</u>
	2003	2002
	MNT '000	MNT '000
General Provision		
Balance at beginning of year	114,380	24,853
Provision made during the year	304,726	153,076
Amount written back in respect of recoveries	(247,007)	(58,258)
Transfer to specific provision	(28,054)	(5,291)
Exchange rate loss	18,366	-
Balance at end of year	<u>162,411</u>	<u>114,380</u>

At 31 December 2003, all loans and advances to borrowers are denominated in Togrog except for USD loans amounting to MNT8,280 million (2002: MNT4,787 million). Interest rate ranges from 18.00% to 34.80% (2002 : 22.80% to 38.40%) per annum.

15. LOANS AND ADVANCES (CONTD.)

Loans and advances amounting to approximately MNT16,355 million at 31 December 2003 (2002 : MNT11,622 million) were classified as normal and provided with a 1% loss reserve. Further, loans amounting to MNT1,783 million (2002 : MNT510 million) were classified as NPLs for the year and provisions of MNT1,038 million (2002 : MNT73 million) have been allocated against these NPLs.

Included in the loans and advances is an amount of MNT151 million due from a borrower, whose rights and ownership of certain assets are being transferred to the Bank. The Bank has represented that the rights and ownership of these assets have been reserved under its name and legal transfer of the title and ownership is in progress.

The provision for loan losses is considered adequate by the management based upon their formal review and analysis of existing credits using their knowledge of prevailing and anticipated economic conditions.

16. OTHER ASSETS

	2003 MNT '000	2002 MNT '000
Other real estate owned ("OREO")	128,254	12,014
Inventory	91,930	25,688
Prepaid expenses	65,146	2,779
Other receivables	13,292	4,518
	<u>298,622</u>	<u>44,999</u>
Provision for other assets	(2,583)	-
	<u>296,039</u>	<u>44,999</u>

OREOs are disclosed net of provisions totalling MNT1.3 million (2002: Nil). These provisions are as prescribed by the Regulations of Bank of Mongolia. Also included in the provision for other assets is a provision for the doubtful recovery of a prepayments amounting to MNT11.6 million (2002: Nil).

17. TAX RECOVERABLE

	2003 MNT '000	2002 MNT '000
Tax recoverable	<u>35,000</u>	<u>-</u>

Tax recoverable represents the excess of tax paid compared to the taxation payable and is subject to the approval of the Mongolian Tax Authority (MTA).

18. PROPERTY, PLANT AND EQUIPMENT

	Buildings MNT '000	Office Equipment & Vehicles MNT '000	Computers MNT '000	Construction in progress MNT '000	Total MNT '000
At cost					
Balance at beginning of year	23,500	206,173	219,368	5,175	454,216
Additions	43,630	258,123	112,883	-	414,636
Transfers	-	5,175	-	(5,175)	-
Balance at end of year	67,130	469,471	332,251	-	868,852
Accumulated depreciation					
Balance at beginning of year	294	16,513	16,653	-	33,460
Charge for the year	1,125	35,215	51,489	-	87,829
Balance at end of year	1,419	51,728	68,142	-	121,289
Net Book Value					
At 31 December 2003	65,711	417,743	264,109	-	747,563
At 31 December 2002	23,206	189,660	202,715	5,175	420,756
Depreciation charge for 2002	294	16,068	16,190	-	32,552

19. DEPOSITS FROM CUSTOMERS

	2003 MNT '000	2002 MNT '000
Current accounts	2,206,784	1,094,021
Demand deposits	1,989,620	1,166,577
Time deposits	18,143,730	11,887,491
Other deposits	1,051	3,000
	<u>22,341,185</u>	<u>14,151,089</u>

(i) The maturity structure of time deposits is as follows:

	2003 MNT '000	2002 MNT '000
Due within three months	5,715,883	3,561,803
Three months to six months	5,122,767	2,697,739
Six months to one year	5,363,869	4,919,040
One year to five years	1,941,211	708,909
	<u>18,143,730</u>	<u>11,887,491</u>

(ii) The deposits are sourced from the following customers:

	2003 MNT '000	2002 MNT '000
Individuals	20,014,844	13,141,991
Business enterprises	2,326,341	1,009,098
	<u>22,341,185</u>	<u>14,151,089</u>

Foreign currency current accounts bear an annual interest rate ranging from 1.20% to 3.00% (2002 : Nil) per annum, while for local currency current accounts interest rates range from 3.60% to 7.20% (2002 : Nil) per annum. Other deposits accounts generally do not bear any interest.

Demand deposits are interest bearing and may be withdrawn upon demand. Foreign currency demand deposits bear annual interest rate of 4.80% (2002 : 4.80% to 7.20%) per annum while the local currency demand deposits bear annual interest rate of 6.00% to 7.20% (2002 : 6.00% to 7.20%) per annum.

Foreign currency time deposits bear an annual interest rate ranging from 4.20% to 18.00% (2002 : 7.20% to 13.20%) per annum, while for local currency time deposits interest rates range from 8.40% to 24.00% (2002 : 12.00% to 24.00%) per annum.

**20. DEPOSITS AND PLACEMENTS OF OTHER BANKS
AND FINANCIAL INSTITUTIONS**

	2003	2002
	MNT '000	MNT '000
Deposit placed by a local bank	-	500,000
	<u>-</u>	<u>500,000</u>

The deposit placed by a local bank as at 31 December 2002, represents a local currency time deposit which bears an annual interest rate of 21.60%. The Bank did not hold any deposits and placements of other banks and financial institutions as at 31 December 2003.

21. OTHER LIABILITIES

	2003	2002
	MNT '000	MNT '000
Payables	39,219	28,283
Interest paid in advance	23,500	-
Delay on clearing settlement	5,940	30
Other payables	1,217	1,065
	<u>69,876</u>	<u>29,378</u>

22. STATUTORY FUND

	Number of Ordinary Shares		Amount	
	2003	2002	2003	2002
			MNT '000	MNT '000
At 1 January				
Issued during the year	3,500	3,500	3,500,000	3,500,000
At 31 December	500	-	500,000	-
	<u>4,000</u>	<u>3,500</u>	<u>4,000,000</u>	<u>3,500,000</u>

During the financial year, the Bank increased its statutory fund by MNT500 million by issuing 500 ordinary shares of MNT1,000,000 each.

23. RISK MANAGEMENT POLICIES

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

Credit risk

The Bank is exposed to credit risk which is the risk that a counter party will be unable to pay amounts in full when due. The Bank structures the levels of credit risk it undertakes by placing limits on the amount of risk accepted in relation to one borrower, or group of borrowers, and to 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 borrower and product are approved regularly by the Bank's management team.

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

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 assurance 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.

Apart from deposits and placements with other banks and financial institutions amounting to MNT1,113,965 (2002: Nil) all assets and liabilities were geographically concentrated in Mongolia.

23. RISK MANAGEMENT POLICIES (CONTD.)

Currency risk

The Bank is exposed to effects of fluctuations in the prevailing foreign currency exchange rates on its financial position and cash flows. The Bank's management sets limits on the level of exposure by currencies (primarily USD) and in total.

The Bank's concentration of assets and liabilities are as follows:

	2003 (MNT'000)		
	MNT	Foreign currencies	Total
Assets			
Cash and short term funds	593,510	1,178,148	1,771,658
Deposits and placements with other banks and financial institutions	1,359,389	3,203,667	4,563,056
Investment in securities	1,216,662	575,396	1,792,058
Loans and advances	8,920,678	8,280,942	17,201,620
Other assets	265,920	30,119	296,039
Tax recoverable	35,000	-	35,000
Property, plant and equipment	747,563	-	747,563
	<u>13,138,722</u>	<u>13,268,272</u>	<u>26,406,994</u>
Liabilities			
Deposits from customers	8,994,199	13,346,986	22,341,185
Other liabilities	6,429	63,447	69,876
	<u>9,000,628</u>	<u>13,410,433</u>	<u>22,411,061</u>
Net position	<u>4,138,094</u>	<u>(142,161)</u>	<u>3,995,933</u>

23. RISK MANAGEMENT POLICIES (CONTD.)

	2002 (MNT'000)		
	MNT	Foreign currencies	Total
Assets			
Cash and short term funds	306,985	221,117	528,102
Deposits and placements with other banks and financial institutions	760,986	1,938,713	2,699,699
Investment in securities	2,848,695	-	2,848,695
Loans and advances	7,157,642	4,786,518	11,944,160
Other assets	44,999	-	44,999
Property, plant and equipment	420,756	-	420,756
	<u>11,540,063</u>	<u>6,946,348</u>	<u>18,486,411</u>
Liabilities			
Deposits from customers	6,668,614	7,482,475	14,151,089
Deposits and placements of other banks and financial institutions	500,000	-	500,000
Other liabilities	1,253	28,125	29,378
	<u>7,169,867</u>	<u>7,510,600</u>	<u>14,680,467</u>
Net position	<u>4,370,196</u>	<u>(564,252)</u>	<u>3,805,944</u>

Liquidity risk

The Bank is exposed to frequent calls on its available cash resources from current deposits, maturing deposits and loan drawdowns. The Bank maintains liquidity management with the objective of ensuring that funds will be available at all times to honor all cash flow obligations as they become due. The Bank's Assets and Liabilities Management Committee sets limits on the minimum proportion of maturing funds available to cover such cash outflows and on the minimum level of interbank and other borrowing facilities that should be in place to cover withdrawals at unexpected levels of demand.

23. RISK MANAGEMENT POLICIES (CONTD.)

The contractual maturities of assets and liabilities for the year ended 31 December 2003 are as follows (MNT'000):

	Less than 3 months	3 to 6 months	6 months to 1 year	1 to 5 years	Over 5 years	Total
Assets						
Cash and short term funds	1,771,658	-	-	-	-	1,771,658
Deposits and placements with other banks and financial institutions	4,563,056	-	-	-	-	4,563,056
Investment in securities	1,792,058	-	-	-	-	1,792,058
Loans and advances	4,161,864	7,311,416	5,402,119	326,220	-	17,201,620
Other assets	296,039	-	-	-	-	296,039
Tax recoverable	35,000	-	-	-	-	35,000
Property, plant and equipment	-	-	-	264,109	483,454	747,563
	<u>12,619,675</u>	<u>7,311,416</u>	<u>5,402,119</u>	<u>590,329</u>	<u>483,454</u>	<u>26,406,994</u>
Liabilities						
Deposits from customers	9,913,339	5,122,767	5,363,868	1,941,211	-	22,341,185
Other liabilities	69,876	-	-	-	-	69,876
	<u>9,983,215</u>	<u>5,122,767</u>	<u>5,363,868</u>	<u>1,941,211</u>	<u>-</u>	<u>22,411,061</u>
Net liquidity gap	2,636,460	2,188,649	38,251	(1,350,882)	483,454	3,995,933
Accumulated gap	<u>2,636,460</u>	<u>4,825,109</u>	<u>4,863,361</u>	<u>3,512,479</u>	<u>3,995,933</u>	

23. RISK MANAGEMENT POLICIES (CONTD.)

The contractual maturities of assets and liabilities for the year ended 31 December 2002 are as follows (MNT'000):

	Less than 3 months	3 to 6 months	6 months to 1 year	1 to 5 years	Over 5 years	Total
Assets						
Cash and short term funds	528,102	-	-	-	-	528,102
Deposits and placements with other banks and financial institutions	2,699,699	-	-	-	-	2,699,699
Investment in securities	2,800,000	-	48,695	-	-	2,848,695
Loans and advances	2,312,542	4,952,774	4,194,819	484,025	-	11,944,160
Other assets	44,999	-	-	-	-	44,999
Property, plant and equipment	5,175	-	-	202,715	212,866	420,756
	<u>8,390,517</u>	<u>4,952,774</u>	<u>4,243,514</u>	<u>686,740</u>	<u>212,866</u>	<u>18,486,411</u>
Liabilities						
Deposits from customers	5,685,156	3,022,589	4,799,953	643,391	-	14,151,089
Deposits and placements of other banks and financial institutions	-	-	500,000	-	-	500,000
Other liabilities	29,378	-	-	-	-	29,378
	<u>5,714,534</u>	<u>3,022,589</u>	<u>5,299,953</u>	<u>643,391</u>	<u>-</u>	<u>14,680,467</u>
Net liquidity gap	2,675,983	1,930,185	(1,056,438)	43,349	212,866	3,805,944
Accumulated gap	<u>2,675,983</u>	<u>4,606,167</u>	<u>3,549,729</u>	<u>3,593,078</u>	<u>3,805,944</u>	

22. RISK MANAGEMENT POLICIES (CONTD.)

Interest rate risk

The Bank is exposed to the effects of fluctuations in the prevailing levels of market interest rates on its financial position and cash flows. Interest rate risk is measured by the extent to which changes in market interest rates impact margins and net income. To the extent the term structure of interest bearing assets differs from that of liabilities, net of interest income will increase or decrease as a result of movements in interest rates. The Bank's expected repricing and maturity dates do not differ significantly from the contract dates, which are disclosed in the liquidity risk table above.

Interest rate risk is managed by increasing or decreasing positions within limits specified by the Bank's management. These limits restrict the potential effect of movements in interest rates on interest margin and on the value of interest sensitive assets and liabilities.

The Bank's interest rate policy is reviewed and approved by the Bank's Assets and Liabilities Management Committee. The Bank's interest rates in 2003 and 2002 for monetary financial instruments are as follows:

	2003		2002	
	MNT	USD	MNT	USD
	%	%	%	%
Interest earning assets				
Deposits and placements with other banks and financial institutions	12.00 - 13.20	3.60 - 8.25	-	3.60
Bank of Mongolia treasury bills	3.95 - 14.46	-	7.23 - 12.13	-
Corporate bonds	20.40 - 21.60	-	21.60	-
Loans and advances	22.80 - 38.40	18.00 - 34.80	30.00 - 48.00	22.80 - 38.40
Interest bearing liabilities				
Current account deposits	3.60 - 7.20	1.20 - 3.00	-	-
Demand deposits from customers	6.00 - 7.20	4.80	6.00 - 7.20	4.80 - 7.20
Time deposits from customers	8.40 - 24.00	4.20 - 18.00	12.00 - 24.00	7.20 - 13.20
Deposits and placements of other banks and financial institutions	-	-	21.60	-

24. RELATED PARTY DISCLOSURES

Parties are considered to be related if one party has the ability to control the other party or exercise significant influence over the other party in making financial or operational decisions.

A number of banking transactions are entered into with related parties in the normal course of business. These include loans, deposits and foreign currency transactions. These transactions were carried out on commercial terms and at market rates. The volumes of related party transactions, outstanding balances at the year end, and relating expense for the year are listed below.

As at 31 December, balances and transactions with related parties included:

	2003 MNT '000	2002 MNT '000
a) Loans and advances:		
Petrovis LLC	<u>175,200</u>	<u>340,000</u>
b) Deposits from customers:		
Petrovis LLC	<u>32,620</u>	<u>13,949</u>
c) Rental of premises:		
Petrovis LLC	<u>227,520</u>	<u>115,756</u>

Directors' Remuneration

The executive directors received remuneration totalling MNT42.4 million (2002 : MNT24 million). The non-executive directors received fees totalling MNT21.6 million (2002 : MNT15.6 million).

25. CAPITAL ADEQUACY

Bank of Mongolia requires commercial banks to maintain a core capital adequacy ratio of 5% and risk weighted capital ratio of 10%, compiled on the basis of total equity and total assets as adjusted for their risk.

25. CAPITAL ADEQUACY (CONTD.)

The capital adequacy ratios of the Bank as at 31 December are as follows:

	2003	2002
Core capital ratio	20.67%	28.97%
Risk weighted capital ratio	20.67%	28.97%
	<u>2003</u>	<u>2002</u>
	<u>MNT '000</u>	<u>MNT '000</u>
<u>Tier I capital</u>		
Statutory fund	4,000,000	3,500,000
(Accumulated loss)/retained earnings	(4,275)	305,941
Total Tier I Capital/Capital Base	<u>3,995,725</u>	<u>3,805,941</u>

Breakdown of risk weighted assets in the various categories of risk weights are as follows:

	2003		2002	
	MNT '000	Risk	MNT '000	Risk
%	Assets	Weighted	Assets	Weighted
0	5,786,570	-	5,468,701	-
10	-	-	-	-
20	1,799,806	359,961	557,795	111,559
50	-	-	-	-
100	18,968,619	18,968,619	13,024,167	13,024,167
Total	<u>26,554,995</u>	<u>19,328,580</u>	<u>19,050,663</u>	<u>13,135,726</u>

26. OFF BALANCE SHEET ITEMS

	2003	2002
	MNT '000	MNT '000
Off balance sheet items	<u>372,217</u>	<u>82,863</u>

The off balance sheet items represents non-performing loans written off and the interest suspended.

27. FAIR VALUES OF FINANCIAL ASSETS AND LIABILITIES

Financial instruments comprise financial assets and financial liabilities. The fair value of a financial instrument is the amount at which the instrument could be exchanged or settled between knowledgeable and willing parties in an arm's length transaction, other than in a forced or liquidation sale.

Almost all of the financial instruments as at 31 December 2003 are short term in nature with maturities of less than one year. The estimated fair values of those financial assets and financial liabilities as at the balance sheet date approximate their carrying amounts as shown in the balance sheets due to the relatively short term maturity of the financial instruments.

28. COMPARATIVE FIGURES

Certain comparative figures have been reclassified to conform with current year's presentation.

	As Restated	As
	MNT'000	Previously
<u>Assets</u>		Stated
		MNT'000
Cash and short term funds	528,102	3,222,176
Deposits and placements with other banks and financial institutions	2,699,699	5,625

29. CURRENCY

All amounts are in Mongolian Togrog unless otherwise stated.

30. MONGOLIAN TRANSLATION

These financial statements are also prepared in the Mongolian language. In the event of discrepancies or contradictions between the English version and the Mongolian version, the English version will prevail.