

Strictly Confidential

Information Memorandum



PIVDENNYI BANK

**USD 30,000,000
SYNDICATED TERM LOAN FACILITY**

MANDATED LEAD ARRANGERS



APRIL 2008



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DISCLAIMER

This Information Memorandum (the “Memorandum”) is provided to selected banks in connection with an invitation to participate in a USD30,000,000 Term Loan Facility (the “Facility”), on condition that each recipient and its officers, employees, agents and advisors shall keep confidential the information contained in this Memorandum.

Pivdennyi Bank has mandated ABN AMRO, BayernLB and ING (hereafter the “Mandated Lead Arrangers”) to arrange on its behalf the Facility herein described and have authorised the issue of this Memorandum to potential participants in the Facility. Information in this Memorandum has been provided by Pivdennyi Bank and has not been independently verified by the Mandated Lead Arrangers. Furthermore, the Memorandum contains information based on general market intelligence. Pivdennyi bank has warranted (i) the accuracy and completeness of the information and (ii) the reasonableness and fairness of the information contained in the Information Memorandum as at the date of issue.

This Memorandum is not intended by the Mandated Lead Arrangers to provide the basis of any credit or other evaluation and should not be regarded as a recommendation by the Mandated Lead Arrangers that any recipient of this Memorandum participates in the Facility. Each potential participant should determine its interest in participating in the Facility based upon such investigations as it deems necessary for the purpose. Nothing contained in this Memorandum is, or shall be relied upon as, a representation of fact or a promise as to the future.

The Mandated Lead Arrangers, except as provided otherwise in the Facility documentation, make no representation or warranty, express or implied, as to the accuracy or completeness of the information and statements set out in this Memorandum or that these remain unchanged after the date of its issue. The Mandated Lead Arrangers accordingly have no liability for such information and statements. The Mandated Lead Arrangers are and will be entitled to enter into other and new business with Pivdennyi Bank next to their involvement as Mandated Lead Arrangers for the Facility described in this Memorandum. The Mandated Lead Arrangers shall not be under any obligation and do not undertake (nor shall the Mandated Lead Arrangers be liable in any way as a result of not doing so) to review the financial condition or affairs of Pivdennyi Bank at any time nor to advise any participant in the Facility of any information coming to their attention except as specifically provided in the Facility documentation.

The Facility documentation for the Facility has not been finalised at the date of this Memorandum and the Summary of Terms and Conditions of the Facility is qualified by reference to the final Facility documentation. The distribution of this Memorandum in certain jurisdictions may be restricted by law. Persons into whose possession this Memorandum comes are required by Pivdennyi Bank and the Mandated Lead Arrangers to inform themselves about and to observe and comply with any such restrictions.

Without limitation, the contents of this Memorandum and the proposals envisaged thereby are confidential and are being submitted to selected banks in connection with the Facility. This Memorandum is intended only for the person to whom it is supplied by the Mandated Lead Arrangers and may not be reproduced or used, in whole or in part, for any purpose other than that contemplated by it.



AUTHORIZATION LETTER

JOINT-STOCK BANK "PIVDENNYI" АКЦІОНЕРНИЙ БАНК "ПІВДЕННИЙ"

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AUTHORISATION LETTER

ABN AMRO Bank N.V.
Bayerische Landesbank
ING Bank N.V.

Odessa, April 2008

364-day, USD 30,000,000 Syndicated Trade Related Term Loan Facility

Dear Sirs,

We refer to the Information Memorandum April 2008 prepared in the context of the 364-day, USD 30,000,000 Syndicated Trade Related Term Loan Facility (the "Facility") for Pivdennyi Bank. We have assisted in the preparation of the Information Memorandum and been provided with its final version, which we have reviewed.

We hereby confirm that

- (i) all factual information on Pivdennyi Bank contained in the Information Memorandum is true and accurate in all material respects;
- (ii) all opinions, forecasts and projections contained in the Information Memorandum have been prepared on the basis of reasonable assumptions;
- (iii) the Information memorandum does not omit any information which, if disclosed, would render the former untrue or misleading in any material respect;
- (iv) all reasonable enquiries have been made to ascertain and verify the foregoing.

We understand that ABN AMRO Bank N.V., Bayerische Landesbank and ING Bank N.V. as the Initial Mandated Lead Arrangers have not independently verified the information, forecasts and projections contained in the Information Memorandum. The Initial Mandated Lead Arrangers are therefore relying on the confirmations given by us in this letter.

We hereby authorize AMRO Bank N.V., Bayerische Landesbank and ING Bank N.V. as the Initial Mandated Lead Arrangers to distribute copies of the Information Memorandum to potential participants in the Facility provided that Confidentiality Agreements have been executed prior hereto.

Yours sincerely,

Vadim Morokhovskiy
Chairman of the Board
Joint-Stock Bank "Pivdennyi"





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TRANSACTION TIMETABLE

April 2008						
M	T	W	T	F	S	S
	1	2	3	4	5	6
7	8	9	10	11	12	13
14	15	16	17	18	19	20
21	22	23	24	25	26	27
28	29	30				

May 2008						
M	T	W	T	F	S	S
			1	2	3	4
5	6	7	8	9	10	11
12	13	14	15	16	17	18
19	20	21	22	23	24	25
26	27	28	29	30	31	

Date:

Event

23 April 2008

Launch of Syndication

15 May 2008

Commitments subject to documentation due from potential lenders

15 May 2008

Draft documentation circulated to all potential lenders

22 May 2008

Deadline for comments on draft documentation

27 May 2008

Signing date



1. EXECUTIVE SUMMARY

1.1. Transaction Overview

ABN AMRO Bank N.V. (ABN AMRO), Bayerische Landesbank (“BayernLB”) and ING (“ING”) have been mandated to arrange USD 30,000,000 Syndicated Term Loan Facility (the “Facility”) for Pivdennyi Bank (“Pivdennyi” or the “Borrower”)

The main terms and conditions of the Facility are:

Facility Amount: USD 30,000,000 (Thirty Million United States Dollars). In the event of an oversubscription, the Facility Amount may be increased, subject to consultations between the Borrower and the Initial Mandated Lead Arrangers.

Purpose: Financing and refinancing of Financing Contracts.

Margin: 3.25% per annum.

Initial Maturity: 364 days from the date of signing of the Facility Agreement.

For more detailed terms and conditions of the Facility please refer to the Term Sheet section of the present Information Memorandum.

1.2. Bank Description

Bank

The Bank was registered on 3 December 1993 as a closed joint-stock commercial bank and is headquartered in Odessa, Ukraine. On 19 October 2006, the Bank changed its registered status to that of an open joint-stock commercial bank. As at 31 December 2007, according to statistics prepared by the NBU, the Bank was the 21th largest bank in Ukraine by total assets, 19th largest in terms of loans to customers, 14th largest in terms of corporate deposits and current accounts and 22rd largest in terms of total capital. The Bank’s principal businesses are corporate banking including small and medium-sized enterprises (“SMEs”), retail banking and treasury services. For further details, see “Bank in Details”.



Strategy

The Bank's strategy for the next five years is to continue its expansion in the Ukrainian banking sector through a combination of organic growth in its key customer segments (corporate (including SMEs) and retail) in the geographic regions where the Bank is already present and in other targeted regions in Ukraine.

The Bank's strategic objectives

- maintain and strengthen its position in the SME market (small companies with a maximum of 100 employees and UAH 10 million per year turnover and medium companies with a maximum of 1,000 employees and UAH 50 million per year turnover);
- focus on large and medium-sized corporate customers in the main sectors of the southern Ukraine;
- maintain a broad diversity of corporate customers in terms of both geography and industry sector;
- develop and broaden the product range offered to corporate customers;
- seek to attract new high net worth and professional retail customers;
- expand its distribution network;
- develop its range of retail banking products with residential mortgage loans, car purchase loans and credit cards;
- use alternative sales channels for retail banking products through its customer support services; and
- promote brand image and product lines.

Credit Ratings

Currently, the Bank is rated by Moody's and Fitch, which have issued the following credit ratings:

Fitch

Long-term issuer default rating: "B-"
Short-term issuer default rating: "B"
Outlook: "Stable"

Moody's

Foreign currency deposit rating: "B2/NP"
Domestic currency deposit rating: "B1/NP"
Outlook: "Positive"



1.3 Key investment considerations

Ukraine

- Key advantages of today's economic development of Ukraine which positively impact on foreign investments:
- Solid track record of prudent macroeconomic and financial policies
- Benefits from high level of foreign direct investment
- Accession to the WTO performed in 2008
- Intensified bonds with the EU, prospect of a free trade area with Ukraine (medium-term)
- Enhancement of the economy and its efficiency on the basis of the introduction of new technologies
- Normalisation of money circulation and formation of mechanisms for the financing of the real sector of economy
- Strengthening of the government role in the formation of the investment demand and transfer to the innovative-investment model of the economy development
- Cessation of the re-privatisation process
- High potential capacity of the internal market
- Stability of the national currency Hryvnia
- Potentially attractive investment projects, including in the area of high technologies
- Wide network of the social and economic, scientific and technical, transport infrastructure
- High-quality staff and scientific potential, cheap labour force
- Significant natural resources

Pivdennyi Bank

- Rated B- / B2
- Strong base of corporate customers
- Strong shareholder support
- Well positioned for growth and expansion
- Continuity of the Management Team
- Conservative Provisioning, satisfactory profitability, limited trading risks

The benefits of the Facility

- Trade related
- Aimed at trade finance funding of the most reliable customers of Bank Pivdennyi
- Short-term: 364 days
- Attractive all-in pricing



1.4 Trade Finance Transactions

Transactions to be financed by the Facility

Pivdennyi Bank is actively involved in the financing of export and import activities of its corporate customers. The proceeds of the Facility will go among other towards the financing and re-funding of export-import contracts concluded between the main following parties:

Import contracts:

Importer	Exporter	Value of the contract	CCY	Duration of the contract	Nature of the contract
LLC "Uventa"	Alfred Karcher GmbH & Co., Germany	5 000 000.00	USD	12.01.2005 - 22.01.2009	Cleaning equipment
LLC "Torgoviy dim Ukrainskiy kolyoroviy prokat"	OOO "Alkoa Rus", Russia	3 500 000.00	USD	30.11.2006 - 31.12.2009	Aluminium products
OJSC "Farlep-invest"	Huawei tech. investment Co., Ltd, Hong Kong	2 400 000.00	USD	23.03.2006 - *	Telecommunication equipment
CJSC "Medfarkom-tsentr"	Mili Healthcare Limited, U.K.	2 207 600.00	USD	14.12.2006 - 31.12.2009	Medical products
LTD Ukrprommash	Linyi Longma Wood Co., LTD, UK	5 000 000.00	USD	10.02.2007 - 30.12.2008	Plywood
Vostok-oil LTD	Kaspiy Service Int., UK	27 000 000.00	USD	06.11.2007 - 31.12.2008	Petrol
Casing group LTD	Novaprom food ingredients Ltd, UK	550 000.00	USD	10.11.2007 - 31.12.2008	Collagen fiber
Tomis PE	Berryman trading S.A.	10 000 000.00	USD	21.01.2008 - 31.12.2008	Gas oil, oil products
PP «UKRBUDPROEKT-HMZ»	PARKER GLOBAL LLP, UK	9 000 000.00	USD	10.04.2007 - 31.12.2008	Polietilen
TOV Alcotrade	LTD Kakhetian Traditional Winemaking, Georgia	1 000 000.00	USD	14.12.2007 - 31.12.2009	Alcoholic drinks
TOV Alcotrade	ZAO Firm Urozhay, Russia	500 000.00	USD	07.06.2007 - 31.12.2008	Alcoholic drinks
DP KVD LTD «L'empire du vin»	IM "Basarabia Lwin Inwest", Moldova	2 000 000.00	USD	23.01.2008 – 31.12.2008	Vine grape material
PP Tehno Plus	Techsoft industries Limited, China	16 000 000.00	USD	03.10.2007 – 31.12.2009	Household appliances
OJSC "Silur"	Baramist Limited, UK	9 000 000.00	USD	12.12.2005 - 31.12.2008	Zinc metal
"Alyans Group LTD"	OOO "Posuda", Russia	5 000 000.00	USD	19.07.2006 – 31.12.2009	Consumer goods
OJSC Odesfoodfactory	Vogler & Trummer GmbH&Co, Germany	2 000 000.00	USD	01.01.2008 - 31.12.2008	Green coffee Robusta
IC Antal-Industry LTD	Rockwool Polska Sp.z.o.o., Poland	1 000 000.00	USD	01.01.2008 - 31.12.2008	Insulating materials
НВПЦ Бриз	KJS International, USA	6 000 000.00	USD	10.03.2006 - 31.12.2008	Automobiles
НВПЦ Бриз	KJS International, USA	3 500 000.00	USD	10.03.2005 - 31.12.2008	Automobiles
CJSC " Medpharkom-South»	"SAGMEL, INC", USA	4 008 550.00	USD	31.08.2006 - *	Medicines
Company "Trading House "Palmira"	"Hercules Tianpu Chemical Co.Ltd"	800 000.00	USD	15.01.2007 - *	Additives for dry mixture production

115 466 150.00 USD



PIVDENNYI BANK

Bogus and Co LTD	Kaluga plant Remputmash, Russia	142 783 804.00	RUB	22.06.2007-30.06.2008	Equipment
Ukraudovaz CJSC	OJSC Autovaz, Russia	9 907 220 000.00	RUB	18.12.2007 – 01.06.2009	Cars
CUBERA PLUS Ltd	ZAO UGMK-Rudgormash Russia	70 000 000.00	RUB	23.11.2007-31.12.2008	Drilling equipment
OJSC "Silur"	OAo "Kamenskvolokno", Russia	20 000 000.00	RUB	04.12.2006 - 31.12.2009	Cloth, thread and polypropylene
OJSC "Silur"	OAo "Zavod Gornogo Voska", Belarus	14 250 000.00	RUB	18.12.2006 - 31.12.2009	Rustproof lubricants
LLC "Gloriya Jeans"	ZAO "Gloriya Jeans Corporation", Russia	1 000 000 000.00	RUB	04.10.2001 – 31.12.2009	Consumer goods
IC Antal-Industry LTD	ZAO "Pskovpischeprom", Russia	5 000 000.00	RUB	09.01.08-31.12.08	Acid-resisting slabs

11 159 253 804.00 RUB

ZAT "Pervy likerovodochny zavod"	Corporation "Premium and Design Ltd", U.K.	1 000 000.00	GBP	21.06.2006 - 31.12.2009	Glass bottles
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CJSC "Odessa brandy factory"	ICS FVD "Moldavsky Standart" SRL, Moldova	1 620 000.00	EUR	14.02.2006 - *	Cognac alcohol
CJSC "Odessa brandy factory"	«RUJI LTD», Georgia	2 200 000.00	EUR	12.04.2007 - 31.12.2008	Cognac alcohol
CJSC "Odessa brandy factory"	«PARAKAR»WINE-BRANDY HOUSE, ARMENIA	2 000 000.00	EUR	14.09.07-31.12.2008	Cognac alcohol
"Cement" LTD	SIMI «SOSIEDEDE INTERNACIONAL DE MONTAGENS INDUSTRIAIS.SA», PORTUGAL	1 867 372.22	EUR	28.08.2006 - *	Fabricated metals and platforms for cement storage bins
"Cement" LTD	Christian Pfeiffer Maschinenfabrik GmbH, Austria	2 850 000.00	EUR	10.11.2005 - *	Cement grinding equipment
OJSC "Chernigovskoe khimvolokno"	Polymer Engineering GmbH, Germany	22 195 000.00	EUR	19.05.2006 - 20.12.2009	Polyamide producing equipment
Manifik LTD	SESO spol. s.r.o., Vranov nad Toplou	6 677 660.00	EUR	01.08.2007- *	Equipment
CUBERA PLUS Ltd	TEKO GmbH, Germany	300 000.00	EUR	25.02.2008-31.12.2008	Cooling industrial equipment
AO ROSSA	TRADEX UNION LIMITED, UK	800 000.00	EUR	12.06.2007-31.12.2008	Aluminium sheets
AO ROSSA	DGS S.A., Poland	900 000.00	EUR	01.08.2006-31.12.2020	Aluminium sheets
IRM "Autodetal"	COMTHERM ES TSA KERESKEDELMI K.F.T., Hungary	1 200 000.00	EUR	03.12.06-31.12.08	Automatic devices for gas heating equipment
CJSC " Medpharkom-South»	Herbs Trading GmbH, Austria	1 239 630.96	EUR	01.01.2007 - *	Consumer goods
Company "Trading House "Palmira"	"Hercules Doel BVBA", Aqualon division	1 000 000.00	EUR	09.01.2007 - *	Consumer goods
Slobozhansky soap-boiler Ltd	GRAHAM INVEST AND TRADE CORPORATION, Hungary	1 000 000.00	EUR	03.09.2005-31.12.2009	Soap noodles

45 849 663.18 EUR

* Duration of the contract - till final fulfilment of engagements



Export contracts:

Exporter	Importer	Value of the contract	CCY	Duration of the contract	Nature of the contract
TH JSC XTZ Ltd	ZEROMAX GmbH, Switzerland	1 394 720.00	USD	29.08.2007 - *	Tractors and spare parts
TH JSC XTZ Ltd	SIA LAJA, Latvia	500 000.00	USD	24.07.2007 - 31.12.2008	Tractors and spare parts
Slobozhansky soap-boiler Ltd	LLC "KIGMA", Georgia	500 000.00	USD	10.03.2006 - 31.12.2008	For soap
CJSC "Enakievskiy koksochimprom"	CJSC "Energoprom Management", Russia	4 624 600.00	USD	04.12.2006 - *	Electrode coal pitch
OJSC "Silur"	MESEL TRADING LIMITED, Cyprus	25 000 000.00	USD	21.03.2006 - *	Metal-ware products
JSC "Olymp-krug"	"EMSA TECNOLOGIA QUIMCIA" S. A., Spain	182 500.00	USD	04.12.2007 - *	Copper sulphate
JSC "Olymp-krug"	"MARKEIN MANAGEMENT LLC", USA	1 001 000.00	USD	16.10.2007 - *	Copper sulphate
PE "Tsito"	SPE "Sardor Pharm Sanoat", Uzbekistan	500 000.00	USD	21.09.2007 - 31.12.2008	Medical products
PE "Tsito"	"AVERSIPHARMA", Georgia	180 000.00	USD	02.02.2007 - *	Medical products
JSC CF "Nagolchanska"	"INDUSTRY EAST EUROPE INVESTMENTS" LTD, UK	10 000 000.00	USD	27.03.2007 - *	Coal

43 882 820.00 USD

OJSC "Chernigovskoe khimvolokno"	Expert LTD, Russia	500 000 000.00	RUB	15.03.2007 - 31.03.2008	Polyamide string
TH JSC XTZ Ltd	LLC "Trade house "XTZ Belgorod", Russia	600 000 000.00	RUB	26.03.2007 - 31.12.2008	Tractors and spare parts
JSC "Rossa"	LLC "Rossa", Russia	100 000 000.00	RUB	26.10.2005 - 31.12.2008	Alluminium capsules for bottles
Slobozhansky soap-boiler Ltd	LLC "Unitek", Russia	50 000 000.00	RUB	08.01.2008 - 31.12.2010	Soap
Slobozhansky soap-boiler Ltd	LLC "Koktem", Kazakhstan	20 000 000.00	RUB	04.01.2006 - *	Soap
DP KVD LTD «L'empire du vin»	TH Megapolis LTD, Russia	300 000 000.00	RUB	02.01.2007 - *	Wine

1 570 000 000.00 RUB

LTD Artmotion	"DANAHER LINEAR GMBH", Germany	2 000 000.00	EUR	01.04.2004 - *	Metal-working machines
SIE "Complex"	"DANAHER LINEAR GMBH", Germany	5 000 000.00	EUR	05.04.2004 - *	Metal-working machines
OJSC "Silur"	Mesel Trading Limited, Cyprus	25 000 000.00	EUR	21.03.2006 - *	Metal-ware products
LLC "Domberg"	LORILLARD, France	250 000.00	EUR	08.02.2007 - *	Three-ply glued timber for windows (oak)

32 250 000.00 EUR

* Duration of the contract - till final fulfilment of engagements



2. TERM SHEET

Borrower:	Pivdennyi Bank, Ukraine ("Pivdennyi" or the "Borrower").
Facility:	Syndicated Trade Related Term Loan Facility (the "Facility").
Initial Mandated Lead Arrangers:	ABN AMRO Bank N.V. ("ABN AMRO"), Bayerische Landesbank AG ("BayernLB") and ING Bank N.V. ("ING") (the "Initial Mandated Lead Arrangers", each an "Initial Mandated Lead Arranger" or an "MLA").
Bookrunners:	ABN AMRO, BayernLB and ING.
Lenders:	A syndicate of banks, including the Initial Mandated Lead Arrangers, as selected by the Initial Mandated Lead Arrangers in consultation with the Borrower.
Facility Agent:	ING
Documentation Agent:	ING
Information Memorandum Agent:	BayernLB
Signing and Publicity Agent:	ABN AMRO
Facility Amount:	USD 30,000,000 (Thirty Million United States Dollars). In the event of an oversubscription, the Facility Amount may be increased, subject to consultations between the Borrower and the Initial Mandated Lead Arrangers.
Purpose:	Financing and refinancing of Trade Financing Contracts including the refinancing of a USD 45,000,000 syndicated term loan facility dated 22 nd May 2007.
Availability:	Upon satisfaction of conditions precedent and subject to three business days' (definition of business days to be agreed in the Facility Agreement) prior written notice to the Facility Agent the Facility will be available for drawing for a period of up to 15 days, commencing with the Signing Date (the "Availability Period") and shall be drawn in full in one amount.
Repayment:	The Facility will be repaid in one amount on the Final Maturity Date.



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- Final Maturity Date:** 364 days from the date of signing of the Facility Agreement.
- Interest Rate:** The aggregate of:
- (a) the Margin
 - (b) the appropriate London Inter Bank Offered Rate (“LIBOR”) for United States Dollars (“USD”) for the relevant Interest Period and
 - (c) Mandatory Costs (if applicable).
- Interest will be payable at the end of each Interest Period. Interest will be calculated on the basis of the actual number of days elapsed in a year of 360 days.
- Interest Period:** 3 or 6 months, provided that no Interest Period may end after the Final Maturity Date.
- Margin:** 3.25% per annum.
- Mandatory Costs:** The Borrower shall indemnify the Lenders for any mandatory costs, if applicable, in respect with compliance with the requirements of the Bank of England, the U.K. Financial Service Authority, the European Central bank or any other relevant regulating authority, calculated in accordance with a formula to be set out in the Facility Agreement.
- Prepayment:** Prepayment of the Facility will be permitted without premium or penalty in minimum amounts of USD 10 million and integral multiples of USD 5 million thereof, at the end of an Interest Period, subject to 30 days’ prior written notice to the Facility Agent. Any amounts prepaid may not be reborrowed. Prepayment of the Facility before the end of an Interest Period will be permitted only in cases of illegality, increased costs, market disruption or grossing-up for tax purposes. In these cases the Borrower will have to pay any breakage costs. No amount prepaid may be reborrowed.



Financing Contracts:

Financing agreements between the Borrower and its customers (reasonably acceptable to the Initial Mandated Lead Arrangers) under which the Borrower provides financing to its customers for their respective entering into trade financing agreements in relation to acceptable goods (weapon, nuclear equipment, drugs and other unacceptable imports excluded). The aggregate amount outstanding under such financing agreements shall not be less than the Facility Amount. The Initial Mandated Arrangers shall have the right to reasonably require satisfactory evidence of the Financing Contracts being financed or refinanced by the Facility. The Facility Agreement will contain a list of the Financing Contracts.

Conditions Precedent:

Standard for this type of financing. The obligation of the Lenders to make any advances under the Facility will be subject to the satisfaction of customary conditions which will include, without limitation, the following:

1. signed Facility Agreement and related documentation;
2. receipt by the Facility Agent, the Initial Mandated Lead Arrangers and the Lenders of all fees required to be paid, and all expenses for which invoices have been presented;
3. receipt by the Facility Agent of all documentation evidencing the corporate authority of the Borrower, and the incumbency and specimen signatures of the officers of the Borrower executing the Facility Agreement and related documentation;
4. receipt of information with respect to the Borrower as may be deemed necessary by the Initial Mandated Lead Arrangers to complete due diligence of the Borrower;
5. receipt by the Facility Agent of all required regulatory and other governmental approvals, if any, which shall be in full force and effect;
6. receipt by the Lenders of satisfactory audited accounts of the Borrower for the most recent fiscal year ended prior to the date of signing of the Facility Agreement for which such accounts



are available and

7. the absence of any (actual or potential) event of default;
8. each of the representation and warranties being true and correct as of the date of the drawdown before and after giving effect to such;
9. receipt by the Facility Agent of satisfactory evidence of the appointment by the Borrower of an agent for service of process in London;
10. receipt by the Facility Agent of satisfactory legal opinions from the relevant legal counsels, and
11. No market disruption in relation to the proposed loan; and
12. there shall not have occurred any change in national (including in relation to Ukraine) or international, financial, political, economic or market conditions which could, in the opinion of the Majority Lenders, make it impossible or materially impractical to make any disbursement of a loan.

Representations and Warranties:

To be made by the Borrower at the signing of the Facility Documents and to be repeated on the date of giving a drawdown notice and on the first day of each Interest Period, and to include, inter alia:

1. the Borrower is duly organised, validly existing and in good standing under the laws of the jurisdiction of its incorporation and has the power and authority to carry on its business, to own its assets and to enter into and perform its obligations pursuant to the credit agreement, and all corporate actions required in relation thereto have been taken;
2. the obligations expressed to be assumed by the Borrower in the Facility Documents are valid, legally binding, direct and unconditional obligations enforceable against it in accordance with their terms;



3. no Event of Default or potential Event of Default has occurred and is continuing;
4. no proceedings are pending or threatened for the winding-up, dissolution or similar process against the Borrower;
5. no material litigation is pending against the Borrower;
6. the Borrower's latest audited and unaudited accounts give a true and fair view of the financial condition of the Borrower and no Material Adverse Change has occurred since the latest accounts;
7. no conflict with, breach of, other agreements, laws or treaties exists;
8. no requirement exists on the Borrower to create any encumbrance as a result of the entering into the Facility Documents;
9. the obligations of the Borrower under the Facility Documents rank at least pari passu with all its other external unsecured and unsubordinated obligations other than obligations preferred by the operation of laws of general application;
10. no withholding or deduction from payments, save for withholdings required by applicable law will occur;
11. no stamp, registration or similar transaction tax, etc. will have to be paid;
12. no immunity from suit exists;
13. the written information provided by the Borrower to the Initial Mandated Lead Arrangers is, to its knowledge, true, complete and accurate in all material aspects.

Covenants / Undertakings:

For as long as any amount remains outstanding under the Facility, the Borrower will, inter alia:

Financial information



1. provide to the Lenders:
 - a. the Borrower's annual audited consolidated and unconsolidated financial statements in accordance with International Financial Reporting Standards ("IFRS") within 120 days of the end of each financial year;
 - b. the Borrower's interim audited or unaudited accounts within 90 days of the end of the first half of each financial year in accordance with IFRS; and
 - c. such further information about the Borrower that the Facility Agent may reasonably require.

Financial Covenants

2. ensure that:
 - a. its Bank for International Settlements ("BIS") Capital Adequacy Ratio shall at all times be no less than the higher of (a) twelve (12) percent (12%) and (b) such other minimum percentage as may be required by the BIS and National Bank of Ukraine from time to time;
 - b. it maintains at all times a ratio (expressed as a percentage) of its Non Performing Loans, to its Gross Loan Portfolio, of not more than two (2) percent (2%);
 - c. it maintains a coverage ratio Loan Loss Reserves to the Non Performing Loans of at least 200%; and
 - d. it maintains at all times a minimum total equity of at least USD 165,000,000

With respect to b, c and d it has been agreed that compliance with these covenants will be represented semi-annually and any term used in b, c and d should be as defined and listed in the most recent Financial Statements of the Borrower prepared in accordance with IFRS as delivered to the Facility Agent.

Affirmative covenants

3. obtain and promptly renew from time to time all necessary actions, conditions, authorisations and consents as may be required by law of the



relevant jurisdiction;

4. effect and maintain such insurance over its assets and business as is reasonable and prudent for the business;
5. ensure that at all times the claims of the Facility Agent and the Lenders against it under the Facility Documents rank at least pari passu with the claims of all its other external unsecured and unsubordinated creditors save those whose claims are mandatorily preferred by any bankruptcy, insolvency, liquidation or other similar laws of general application;
6. give prompt notice of any event of default, etc.

Negative Covenants

7. not, without prior consent of the Facility Agent acting on behalf of the Majority of Lenders create or have outstanding any security over all or any of its present or future assets or revenues as security for any financial indebtedness, subject to the following exceptions:
 - a) any lien arising by operation of law and in the ordinary course of the Borrower's banking business and not arising as a result of a default (howsoever described);
 - b) any Security created with the prior consent of the Facility Agent acting on the instructions of the Majority Lenders;
 - c) any Security upon, or with respect to, any present or future assets or revenues of the Borrower or any of its Subsidiaries or any part thereof which is created pursuant to any securitisation of receivables, asset-backed financing or similar financing structure or special SME financing bilateral loans and whereby all payment obligations secured by such Security or having the benefit of such Security, are to be



discharged solely from such assets or revenues, provided that the aggregate principal amount of indebtedness the subject of such Security at any time shall not exceed 20 per cent. of the aggregate value of loans and advances to customers before allowances for impairment, as determined at any time by reference to the most recent financial statements of the Borrower prepared in accordance with IFRS as delivered to the Facility Agent;

d) any security which has been disclosed in writing to the Facility Agent and the Lenders prior to the date of signing of the Facility;

e) any Security and securing indebtedness the principal amount of which (when aggregated with the principal amount of any other indebtedness which has the benefit of Security other than any permitted under sub-paragraphs (a) to (d) above) does not exceed \$10,000,000 (or its equivalent in another currency or currencies).

8. not to exceed the maximum level of Borrower's aggregate Financial Indebtedness (other than Financial Indebtedness under the Finance Documents) of 400% of the Total Equity as determined at any time by reference to the most recent financial statements of the Borrower prepared in accordance with IFRS as delivered to the Facility Agent. For avoidance of doubt, "**Financial Indebtedness**" means any indebtedness for or in respect of:

- (a) moneys borrowed;
- (b) any amount raised by acceptance under any acceptance credit facility or dematerialised equivalent;
- (c) any amount raised pursuant to any note purchase facility or the issue of bonds, notes, debentures, loan stock or any similar instrument;
- (d) the amount of any liability in respect of any lease or hire purchase contract which would, in accordance with IFRS, be treated as a finance



or capital lease;

- (e) receivables sold or discounted (other than any receivables to the extent they are sold on a non-recourse basis);
- (f) any amount raised under any other transaction (including any forward sale or purchase agreement) having the commercial effect of a borrowing;
- (g) any derivative transaction entered into in connection with protection against or benefit from fluctuation in any rate or price (and, when calculating the value of any derivative transaction, only the marked to market value shall be taken into account);
- (h) any counter-indemnity obligation in respect of a guarantee, indemnity, bond, standby or documentary letter of credit or any other instrument issued by a bank or financial institution; and
- (i) the amount of any liability in respect of any guarantee or indemnity for any of the items referred to in paragraphs (a) to (h) above;

but excluding any indebtedness pursuant to "Due to the National Bank of Ukraine", "Customer accounts" and "Subordinated Debt" (each as defined and listed in the most recent financial statements of the Borrower prepared in accordance with IFRS as delivered to the Facility Agent);

9. not grant any credits whatsoever other than in the ordinary course of business, and all transactions with any affiliate shall be conducted on an arm's length basis;

10. not sell, transfer, lease out, lend or otherwise dispose of any part of its assets. The following disposals, inter alia, will not be taken into account:

- (i) disposals in the ordinary course of business;
- (ii) disposals for cash for full value on arm's length



terms;

(iii) disposals other than for cash for full value on arm's length terms;

(iv) disposals to which the Facility Agent acting on behalf of the Majority of Lenders shall have agreed; and

11. not materially change the nature of the Borrower's business.

Events of Default:

Events of Default will comprise, without limitation:

1. failure by the Borrower to pay any sum due from it under the credit agreement (subject to 3 business days' grace period in respect of administrative or technical difficulties affecting the transfer of funds);
2. any financial indebtedness of the Borrower other than under the Facility Documents is not paid when due or is declared to be or otherwise becomes due and payable prior to its originally specified maturity or any creditor becomes entitled to declare any financial indebtedness other than under the Facility Documents due prior to its originally stated maturity, subject to an aggregate threshold amount to be agreed upon;
3. undertakings or other obligations under the Facility are breached (if capable of remedy, subject to remedy within a customary grace period);
4. representations, warranties or other statements are untrue in any material aspect as of the date when they are given or deemed to be repeated (if capable of remedy, subject to remedy within a customary grace period);
5. change in control of the Borrower;
6. insolvency events and proceedings relating to the Borrower;



7. nationalisation or expropriation of the Borrower or any of its material assets, and

8. the occurrence of a Material Adverse Change.

Upon an Event of Default occurring and continuing, the remedies available to the Lenders will include: acceleration of outstandings and other remedies as permitted under applicable law.

Documentation:

The Facility will be subject to the negotiation, preparation and execution of documentation satisfactory to all parties concerned. The Facility Agreement will incorporate clauses currently standard in the syndicated Euroloan market for this type of transaction and mainly based on Pivdennyi Bank's USD 30 million Syndicated Trade Related Term Loan Facility dated 29 October 2007 incorporating, inter alia, Conditions Precedent (including legal opinions from English and Ukrainian legal counsels in form and substance satisfactory to the Lenders, all documents to satisfy the Lender's KYC requirements), representations and warranties, covenants/undertakings (including inter alia *pari passu* ranking of sums due under the Facility Agreement with other indebtedness, negative pledge), financial covenants, events of default (including, inter alia, cross default, material adverse change, change of control, transfer restriction imposed by the relevant national authorities), set-off (with matured and unmatured obligations owed to the Borrower), indemnities (incl. currency indemnity), other costs and expenses, breakage costs, clawback rights of Facility Agent and Fronting Bank reimbursement of increased costs and of costs of enforcement and preservation, indemnities, and other general provisions.



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- Material Adverse Change:** The occurrence of any event or series of events which in the opinion of the Facility Agent acting in the accordance with instruction of the Lenders which combined commitments total at least 66 $\frac{2}{3}$ percent of the Facility Amount (the “Majority Lenders”), could have a material adverse effect on the ability of the Borrower to perform their respective obligations under the Facility.
- Material Adverse Effect:** An event or circumstance which (when taken alone or together with any previous or current event or circumstance) has, or may in the opinion of the Facility Agent have, a materially adverse effect on (a) the assets, business or financial condition or prospects of the Borrower; (b) the ability of the Borrower to perform its obligations under the finance documents under the Facility; or (c) the validity or enforceability of any finance document or the right or remedies of any party hereunder.
- Taxes/Gross-up:** All amounts payable under the Facility Agreement will be paid in full without set-off or counterclaim or other restrictions and free and clear of and without any deductions or withholding for or on account of any taxes or any charges or otherwise. The Borrower will agree with the MLAs on an acceptable formula by which to reimburse withholdings made pursuant to applicable law.
- Assignment and Transfer:** The Lenders’ rights and obligations under the credit agreement will be fully transferable without the prior consent of the Borrower.
- Governing Law and Arbitration:** The Facility Agreement shall be governed by and construed in accordance with the laws of England.
- Any dispute, controversy or claim arising out of or in connection with the Facility Agreement or any other related
- Finance Document, shall be referred to, and finally settled by, arbitration under the LCIA (London Court of International Arbitration) rules, as in force at the date at which the proceedings are referred to arbitration. In addition the Lenders may commence legal proceedings against the Borrower in England and in other countries (this concept remains subject to final legal advice from Lenders' legal advisor in Ukraine).



3. PIVDENNYI BANK IN DETAILS

3.1. Overview

Joint-stock Bank “Pivdennyi” (the “Bank”) is an open joint-stock commercial bank with its registered office in Odessa, south-western Ukraine. The Bank offers a range of banking services to corporate and retail customers through a network of branches, outlets and other offices. The network comprises 18 branches, 200 exchange offices, 115 outlets and three self-service outlets, all in key business centres throughout Ukraine. As at 31 December 2007, Mr. Yuriy O. Rodin, Mr. Mark Is. Bekker and Mr. Vadim V. Morokhovskiy beneficially owned (through direct ownership, holding companies and relatives) approximately 67 per cent., 22 per cent. and 10 per cent., respectively, of the Bank’s outstanding share capital (see “Share Capital and Principal Shareholders”).

According to official statistics of the National Bank of Ukraine (the “NBU”) (as calculated under Ukrainian accounting standards (“Ukrainian Accounting Standards”) and based on statutory reporting requirements), as of 31 December 2007, the Bank was the 21th largest bank in Ukraine in terms of total assets, the 19th largest bank in Ukraine in terms of loans to customers, the 14th largest in terms of corporate deposits and current accounts and the 22rd largest bank in Ukraine in terms of total capital.

As at 31 December 2007, the Bank’s total assets were UAH 8,662,362 thousand, an increase of 96.4 per cent. as compared to total assets of UAH 4,410,137 thousand as at 31 December 2006. This growth rate of the Bank’s total assets in 2007 compared favourably to that of the Ukrainian banking sector as a whole for the year ended 31 December 2007, which was reported by the NBU to be 76.0 per cent.

For the year ended 31 December 2007, the Bank made a net profit of UAH 107,132 thousand, compared to UAH 71,892 thousand for the year ended 31 December 2006, an increase of 49.0 per cent.

The Bank’s principal activities are corporate banking (including small and medium-sized enterprises (“SMEs”)), retail banking and treasury services. Corporate banking has traditionally been the main focus of the Bank’s business, representing 88.4 per cent. and 88.9 per cent. of the Bank’s gross loan portfolio as at 31 December 2007 and 31 December 2006, respectively, and 59.9 per cent. and 56.3 per cent. of the Bank’s deposit base (current accounts and term deposits) as at 31 December 2007 and 31 December 2006, respectively.

The Bank’s corporate banking business includes corporate lending, deposit taking, trade finance (including the issuance of letters of credit and bank guarantees), arrangement and underwriting services for corporate bond issues, receivables finance and factoring, leasing and treasury services. For corporate lending and trade finance purposes, the Bank uses funds provided to it by international financial institutions including, among others, The Bank of New York, ING Bank, Commerzbank AG, HVB AG, American Express Bank and funds borrowed from the syndicated loan markets.



3.2. History

The Bank was formed as a closed joint-stock company under the law of Ukraine “On Banks and Banking Activity” on 3 December 1993. It operates under Banking Licence No. 65 of the NBU for all major types of banking operations and is regulated by Ukrainian banking legislation and supervised by the NBU. Since its formation, the Bank has grown its business, often participating in joint projects with its shareholders.

In 1994, lending was the Bank’s main activity. At the end of 1994, Mr. Yuriy O. Rodin became the head of the Supervisory Council. In 1995, the Bank ranked sixth compared with other commercial Ukrainian banks in terms of asset growth according to NBU data. The Bank also established relationships with foreign banks, including Hapoalim Bank, Finansbank (Suisse) and MeesPierson Bank N.V.

In 1996, the Bank became one of the leading operators in the sovereign bond market and actively participated in the corporate securities market, acting as broker for its customers. The Bank has been a member of the Society for Worldwide Interbank Financial Telecommunication (“SWIFT”) since 1997. In 1997, the Bank also became a member of the Interbank Currency Stock Exchange, the Professional Association of Registers and Custodians and an associate member of the international payment system EUROPAY INTERNATIONAL. The Bank also became an official dealer of the travel company Thomas Cook and a participant of the Interregional Stock Union.

In 1999, the Bank further strengthened its position in the market by supporting many of its customers affected by the domestic economic crisis by providing stabilisation loans and restructuring repayment schedules. That same year, the Reuters-Dealing system was put into operation to increase efficiency. Mr. Vadim V. Morokhovskiy was elected as Chairman of the Management Board.

In 2000, the Bank was the first Ukrainian commercial bank to issue domestic corporate bonds. The following year, the Bank was one of the first Ukrainian banks to act as underwriter for its customers in securities transactions.

In 2004, the Financial Action Task Force on Money Laundering (“FATF”) examined the possibility of excluding Ukraine from the FATF’s list of non-cooperative countries or territories. The NBU appointed the Bank to represent the Ukrainian banking system in the course of examination by FATF. FATF representatives examined the Bank’s achievements in anti-money laundering and “know your client” procedures which contributed to the FATF’s decision to exclude Ukraine from the FATF’s list of non-cooperative countries or territories in February 2004.

In December 2005, the shareholders of the Bank voted to increase the Bank’s capital to UAH 208,896 thousand (inflation adjusted). Fitch gave the Bank its first international rating. In January 2006, Dmitrijs Bekkers sold 49 per cent. of the shares of Regional Investment Bank (“RIB”) to the Bank. As of 31 December 2007, the Bank owned 89 per cent. of the RIB shares.



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In February 2006, the shareholders of the Bank voted to increase the Bank's capital to UAH 258,896 thousand (inflation adjusted) and further again in April 2006 to UAH 282,396 thousand (inflation adjusted). In August 2006, Fitch upgraded the Bank's long-term issuer default rating to "B-" and its short-term issuer default rating to "B".

In November 2006, Bank Austria Creditanstalt and Landesbank Berlin arranged a debut syndicated trade loan to the value of U.S.\$25,000,000 for the Bank. Despite oversubscription, the amount of loan was not increased. That debut syndicated loan was repaid in full in May 2007.

In October 2006, the Bank was reorganised as an open joint-stock company. The reorganisation was undertaken to improve the transparency of the Bank and to enable it to list its shares as a preliminary step toward a possible initial public offering.

In May 2007, Moody's upgraded the Bank's national currency rating and its rating for debt liabilities in foreign currency to B1, changed the outlook for basic B2/NP foreign currency deposits from "stable" to "positive" and assigned a national scale rating of "AA3UA".

In May 2007, the Bank attracted its second U.S.\$45 million syndicated loan facility arranged by Landesbank Berlin AG, Standard Bank Plc and VTB Bank (OJSC). The loan has a one year maturity with an additional one year extension option and was raised for the purposes of the Bank's trade financing activities.

In July 2007, the Bank issued its debut Loan Participation Notes in amount of U.S.\$100 million. The Lead Managers of the issue were Standard Bank Plc and PNP Paribas. The 3-year notes are listed at Swiss Stock Exchange. The proceeds from the offering of the notes were used by Standard Bank Plc (being a legal issuer) for the purpose of funding a loan to the Bank in amount of U.S.\$100 million. The Bank used such proceeds to fund growth in its loan portfolio and for other general corporate purposes.

In October 2007 the Bank attracted its third U.S.\$30 million syndicated loan facility arranged by Bayerische Landesbank AG and Standard Bank Plc. The loan has a one year maturity with an additional one year extension option and was raised for the purposes of the Bank's trade financing activities.

In January 2008 East Capital Explorer Financial Institutions Fund has contracted to purchase a 9.98% stake in Pivdennyi Bank for approximately EUR 54m via a new share issue – confirmation from the National Bank of Ukraine was obtained on February 29, 2008. This new successful and extremely transparent deal with East Capital has brought additional positive promotion to the Bank along with a 40% increase in capital.

3.3. Licences

As a Ukrainian bank, the Bank is regulated and supervised by the NBU.

The Bank was registered with the NBU on 3 December 1993 and its current banking licence was reissued on 23 January 2007. Pursuant to article 2 of the Bank's by-laws, the Bank is



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entitled to conduct various types of banking operations provided for under applicable Ukrainian legislation and specified in the written permit issued by the NBU renewed on 23 January 2007. In particular, the Bank may:

- attract and place foreign currency in Ukraine and abroad;
- open and operate current and deposit accounts for clients and correspondent banks;
- conduct foreign exchange and money market operations;
- sell and purchase securities both for its own account and on behalf of its clients;
- provide guarantees;
- carry out factoring and leasing operations;
- issue and settle cheques, bills of exchange and other payment instruments;
- issue bank cards; and
- provide asset management services.

The Bank holds a licence to conduct professional securities market operations (including activities related to the issuance and trading of securities in the securities markets and the provision of custodial services) issued by the Securities and Stock Market State Commission (the "SSMSC"). This renewable licence will expire on 28 December 2011.

3.4. Strategy

The Bank's strategy for the next five years is to continue its expansion in the Ukrainian banking sector through a combination of organic growth in its key customer segments (corporate (including SMEs) and retail) in the geographic regions where the Bank is already present and in other targeted regions in Ukraine. The Bank's strategic objectives are as follows:

- maintain and strengthen its position in the SME market (small companies with a maximum of 100 employees and UAH 10 million per year turnover and medium-sized companies with a maximum of 1,000 employees and UAH 50 million per year turnover);
- focus on large and medium-sized corporate customers in the main sectors of southern Ukraine;
- maintain a broad diversity of corporate customers in terms of both geography and industry sector;
- develop and broaden the product range offered to corporate customers;
- seek to attract new high net worth and professional retail customers;
- expand its distribution network;
- develop its range of retail banking products with residential mortgage loans, car purchase loans and credit cards;
- use alternative sales channels for retail banking products through its customer support services; and
- promote brand image and product lines.



To grow its Corporate Banking business

The Bank plans to develop and grow its corporate banking business by continuing to focus on large and medium-sized corporate customers in the main business sectors of southern Ukraine such as trading, food-processing, production of beverages, shipping, stevedoring, ship-building, communications, transport, construction, as well as on growth industries such as cash and carry and home shopping networks, food production, and agriculture. The Bank will also seek to maintain a broad diversity of corporate customers in terms of both geography and industry sector to achieve more stable funding. The Bank will seek to grow its corporate customer base by continuing to develop and broaden the product range offered to corporate customers, in particular by offering its corporate customers individually tailored lending products and by effective implementation of cross-selling techniques. In addition, in 2005, the Bank launched lending products for SMEs to facilitate its entry into this segment of the market. The Bank also intends to develop further its advanced credit products (including syndicated loans, structured finance and international trade finance) in co-operation with the Bank's branch network, its subsidiary bank, Regional Investment Bank, located in Riga, Latvia ("RIB"), international banks and financial institutions. The Bank is also considering acquiring additional subsidiaries in EU countries such as Bulgaria and Romania.

To grow its Retail Banking business

The Bank intends to increase its share of the retail banking market in Ukraine. The proportion of the Bank's retail loan portfolio to the total gross loans to customers was 7.5 per cent. as at 31 December 2005, 11.1 per cent. as at 31 December 2006 and 11.6 per cent. as at 31 December 2007.

The Bank intends to target growth of its retail loan portfolio to a maximum of 30 per cent. of its total gross loan portfolio by the end of 2010.

The Bank will seek to attract new high net worth and professional retail customers by offering a wide range of banking products through its expanded distribution network, and by developing various partnership and loyalty programmes for those customers. In particular, the Bank plans to develop its range of retail banking products with residential mortgage loans, car purchase loans and credit cards.

The Bank also intends to make its car loans more flexible in terms of maturity, fees and repayment schedule. In addition, the Bank plans to introduce additional personal banking services, which would allow the Bank's most important customers access to the Bank's services at any time. The Bank also intends to expand its client base through joint marketing efforts with its existing corporate clients by offering banking services to the customers of the Bank's corporate clients.

The Bank will also focus on providing services to high net worth and professional retail clients, mid-level customers, and their family members by using alternative sales channels for retail banking products through its customer support services such as its call centre, telephone banking, internet banking and other client relationship management ("CRM") technologies (see "Description of the Borrower – Banking Activities – Retail Banking – Alternative sales channels").



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The Bank's call centre offers clients access to the Bank's services 24 hours a day, seven days a week. The Bank is also implementing a mobile offices project. In addition, the Bank is targeting growth of retail deposits to a maximum of approximately 55 per cent. of its total deposits by the end of 2010.

To widen existing and create new distribution channels

The Bank is pursuing the growth of its customer base and its loan and deposit portfolios by expanding its network in the most economically developed and heavily populated regions of Ukraine.

The Bank plans to expand its distribution network to approximately 200 branches and outlets in the next few years. New branches will target both corporate and retail banking customers and smaller outlets will mostly target retail banking customers. The Bank intends to focus heavily on training the staff it recruits for these new branches and outlets in order to provide a consistently high standard of customer service. See "Description of the Borrower – Banking Activities – Distribution Network".

The Bank also intends to increase its network of automated teller machines ("ATMs") and expand its participation in its partners' ATM networks to cover all regions of Ukraine with a specific focus on economically developed and heavily populated regions. In particular, the Bank increased the number of its ATMs to 160 by the end of the year 2007 and plans to further increase this to over 200 ATMs in the next few years. In addition, the Bank will increase its ATM capability by providing for a fuller range of services to be available through its ATMs. The Bank was the first in southern Ukraine to install deposit ATMs.

The Bank is expanding its telephone banking system called GSM-Banking ("GSM Banking") (which allows customers to review their accounts and access information via an automated telephone banking system) and internet banking services to make a variety of banking products available on-line, including effecting payments and money transfers. The Bank's Management plans to increase the Bank's co-operation with strategic partners (for example, mobile communication operators) to use their points of sale for acquiring new clients and offering certain banking products.

To promote brand image and product lines

The Bank is implementing a network-wide corporate branding strategy in order to broaden public awareness of the Bank. The Bank is actively promoting its brand and product lines via intensive marketing to existing and new customers through the targeted use of printed and broadcast media advertising. The Bank will also seek to enhance its profile by using alternative advertising media such as direct e-marketing to potential customers and web advertising. The Bank's corporate branding strategy is also being used to give its branches a consistent corporate style, thereby enhancing the Bank's corporate image. The Bank actively participates in various charities and community projects and is founder of a charitable fund that supports educational, scientific and research activities of Odessa State Economic University. The Bank plans to continue its sponsorship initiatives, and to extend the variety of its charities and community projects that it supports.



3.5. Market Position and Competition

As at 31 December 2007, there were 198 commercial banks registered in Ukraine, 175 of which were licensed by the NBU to perform banking transactions. Commercial banks operating in Ukraine were divided by the NBU into four groups according to the size of their assets as at 1 December 2007.

Seventeen major banks with total assets of more than UAH 11 billion each were classified in the first group: Privatbank, Raiffeisen Bank AVAL, UkrSibbank, UkrSotsbank, Ukreximbank, Prominvestbank, Bank Nadra, Oschadbank, OTP Bank, Alfa-bank, Finance and Credit Bank, Bank Forum, FUIB, Kreditprombank, Brokbusinessbank, VTB Bank and Ukrprombank. According to NBU classifications as at 31 December 2007, the Bank was included in the second group. The second group consists of 17 banks with total assets from UAH 3 billion to UAH 11 billion. The third group consists of 34 banks with total assets from UAH 1 billion to UAH 3 billion, and the fourth group consists of 105 banks with total assets of less than UAH 1 billion. The NBU reviews the classification of banks by groups once a year and, due to stable growth (at 31 December 2007 the Bank was already ranked as 21th in terms of total assets), Management believes that in December 2008 the Bank will be upgraded to the first group of major banks. As at 31 December 2007, the minimum regulatory capital requirement for a national bank (being a bank which may operate throughout Ukraine), a regional bank and a cooperative bank that existed before 1 January 2002 was EUR 8 million, EUR 5 million and EUR 1.5 million, respectively. Two of the largest banks in Ukraine, Ukreximbank and Oschadbank, are state owned.

Although the Bank believes it is well placed to compete in the Ukrainian banking sector, being as at 31 December 2007 the 21th largest bank as determined by the NBU (as calculated under Ukrainian Accounting Standards and based on statutory reporting requirements) in terms of total assets, the 19th largest bank in Ukraine in terms of loans to customers, the 14th largest in terms of corporate deposits and current accounts, and the 22rd largest in terms of total capital, the Bank faces competition from a number of existing participants in the banking sector in Ukraine. The Bank generally considers the 20 other largest banks in Ukraine as its principal competitors, of which the Bank considers Bank Forum, Ukrprombank and TAS-Kommerzbank to be its main competitors.

As at 31 December 2007, 47 banks in Ukraine had direct foreign capital, including 17 banks that were wholly owned by foreign investors.

Management believes that the Bank's principal competitive strengths are:

- **Highly qualified management team** The Bank has an experienced and committed management team with an established track record in the Ukrainian banking sector which has managed the Bank's recent growth.
- **Strong shareholder support** The Bank currently has sufficient regulatory capital to allow development of its lending portfolio and the Bank's Management believes that, due to the strong financial support of the Bank's majority shareholders, the Bank will be able to continue the extension of its lending portfolio and expansion of its presence throughout Ukraine. On 30 January 2007, the shareholders of the Bank made a decision to issue 110 million shares totalling UAH 110,000 thousand. The placement of



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shares commenced on 26 February 2007 and was completed on 26 March 2007. All shares were fully paid by the end of March 2007. On 2 April 2007, the NBU registered the relevant changes to the Bank's governing charter and on 6 April 2007, the changes to the state register were also made. The Bank's share capital as at 31 December 2007 amounted to UAH 563,896 thousand and the total equity of the Bank amounted to UAH 844,261 thousand.

- **Diversified funding base** The Bank has a diversified funding structure, which includes customer deposits, loans and credit lines from international banks and financial institutions, and equity funding. The Bank co-operates with a number of international financial institutions including, among others, The Bank of New York, ING Bank, Commerzbank AG, HypoVereinsbank AG, American Express Bank Ltd, Standard Bank Plc, Bank Austria Creditanstalt AG and Landesbank Berlin AG. This co-operation enables the Bank to access international funds which are often longer term than those generally available to Ukrainian banks.
- **Focus on established corporate banking relationships** The Bank has traditionally been focused on the corporate banking sector. The Bank's focus on lending to corporate entities in Ukraine allows it to maintain a lower risk loan portfolio. The Bank intends to continue to strengthen its relationships with corporate customers, in particular, in the following industry sectors: commerce, retail and wholesale trade, wine and beverages, manufacturing, transport, telecommunications, construction and real estate.
- **Clear strategy for the next five years** The Bank intends to build on the success it has achieved to grow its business in the Ukrainian banking sector through a combination of organic growth in its key customer segments (corporate (including SME) and retail) in the geographic areas where it is already located and by moving into new target areas in the manner outlined above.

3.6. Banking Activities

Overview

The Bank's main business activities are corporate banking, retail banking and investment banking and treasury services. Corporate banking currently accounts for the largest proportion of the Bank's loans and deposits. The Bank is currently focusing on increasing the volume of loans extended to and deposits placed by retail customers in its loan and deposit portfolios.

As at 31 December 2007, the Bank had outstanding UAH 6,872,032 thousand in loans to customers (net of allowance for impairment losses), UAH 1,538,821 thousand in customers' current accounts and UAH 4,427,693 thousand in term deposits from customers. As at 31 December 2006, the Bank had outstanding UAH 3,230,276 thousand in loans and advances to customers (net of allowance for impairment losses), UAH 968,924 thousand in customers' current accounts and UAH 2,320,568 thousand in term deposits from customers.



Corporate Banking

Corporate Banking

Corporate banking has historically been the Bank's strength and is the Bank's largest business segment, representing 88.4 per cent. of the Bank's gross loan portfolio, 75.3 per cent. of the Bank's customers' current accounts and 59.9 per cent. of the Bank's deposit base as at 31 December 2007, compared to 88.9 per cent. of the gross loan portfolio, 76.2 per cent. of the Bank's customers' current accounts and 56.3 per cent. of the Bank's deposit base as at 31 December 2006. Corporate banking includes lending, deposit taking, opening and maintaining current accounts, trade finance and cash settlement transactions. For the three month period ended 31 December 2007, the Bank's main income contributors were (i) loans (66.79 per cent.), (ii) cash transactions (9.69 per cent.) and (iii) foreign exchange (4.93 per cent.).

The Bank has also developed a range of advanced credit products, such as syndicated loans and trade finance.

The Bank services its corporate customers through branches which cover 12 regions of Ukraine including branches located in the Odessa region, the Kyiv region, the Dnipropetrovs'k region, Kharkiv, Luhansk, Donetsk, Lviv, Mykolayiv, Kherson, the Autonomous Republic of Crimea, Kyrovograd and Zaporizhya and through other outlets (see "Description of the Borrower – Banking Activities – Distribution Network"). In 2008, the Bank plans to open a new branch in Chernigiv.

Corporate lending

Corporate lending activities include the provision of loan facilities, overdraft facilities, loans to finance working capital (including purchase of property, plant and equipment), revolving credit facilities and standby facilities by the Corporate Banking Division. Corporate lending represented 88.4 per cent. of the Bank's total gross loan portfolio, or UAH 6,219,071 thousand, as at 31 December 2007. As at 31 December 2007, the largest concentration of the Bank's corporate loans were in the trade and commerce sector (64.6 per cent. of the Bank's total gross corporate loan portfolio), the agriculture and food sector (11.4 per cent.), the manufacturing sector (6.6 per cent.), the transport and communications sector (7.4 per cent.) and to other sectors of the economy (10.0 per cent.).

The Bank has strong relationships with large corporate entities. The Bank classifies corporate customers with sales in excess of UAH 50 million as "large", corporate customers with sales in excess of UAH 10 million but less than UAH 50 million as "medium" and corporate customers with sales of less than UAH 10 million as "small". The top ten aggregate loan exposures of the Bank represent 17.9 per cent. of the Bank's loan portfolio, or UAH 1,665,690 thousand, as at 31 December 2007, compared to 21.3 per cent. as at 31 December 2006 and 20.3 per cent. as at 31 December 2005. The Bank is cautious to avoid concentration on a single borrower or group of borrowers. The maximum credit limit for a single borrower (or group of borrowers) is set by the NBU at 25 per cent. of the Bank's regulatory capital. As at 31 December 2007, the Bank's largest exposure to a single borrower or group of borrowers and largest single loan amounted to 17.8 per cent. of the Bank's equity (calculated in accordance with IFRS). According to the NBU standards, the Bank's largest exposure to a



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single borrower or group of borrowers and largest single loan amounted to 22.7 per cent. of the Bank's regulated capital.

As at 31 December 2007, the Bank had 18,143 legal entities as customers and 97 per cent. of these entities were SMEs. The Bank intends to further target the SME lending markets in order to diversify its loan portfolio and further reduce lending concentration. As at 31 December 2007, the loan portfolio of the Bank consisted of 59 per cent. loans to SMEs, 29 per cent. loans to large corporate entities and 12 per cent. retail loans.

The following table sets out an analysis by economic sector of the Bank's corporate loan portfolio as at 31 December 2007¹, 31 December 2006 and 31 December 2005:

Loans by economic sector	31	31 December	31 December
	December	2006	2005
	2007		
	(unaudited)		
		<i>(UAH thousand)</i>	
Trade and commerce	4,020,224	2,028,292	944,898
Transport and communication	458,377	223,038	154,295
Agriculture and food industry	708,115	374,473	217,907
Manufacturing	407,750	240,134	193,198
Other	624,605	118,689	122,019
Total loans to customers (gross) (excluding loans to individuals)	6,219,071	2,984,626	1,632,317

The following table sets out analysis by currency of the Bank's loan portfolio (including retail customers) as at 31 December 2007, 31 December 2006 and 31 December 2005:

	31 December 2007				
	(unaudited)				
	UAH	USD	EUR	Other	Total
	<i>(UAH thousand)</i>				
Loans to customers less allowance for impairment losses	3,348,221	3,216,116	275,516	32,179	6,872,032
	31 December 2006				
	(unaudited)				
	UAH	USD	EUR	Other	Total
	<i>(UAH thousand)</i>				
Loans to customers less allowance for impairment losses	1,255,759	1,776,915	173,613	23,989	3,230,276
	31 December 2005				
	(unaudited)				
	UAH	USD	EUR	Other	Total
	<i>(UAH thousand)</i>				
Loans to customers less allowance for impairment losses	745,503	836,893	60,271	—	1,642,667

¹ Please note that the final audited accounts are now available on Intralinks.



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Loans are granted in currencies requested by customers based on their needs; however, the currency of a loan is subject to approval based on the Bank's planned net exposure to foreign exchange risk.

As at 31 December 2006, the principal rates of exchange used for translating foreign currency balances as used in the Bank's 2006 annual financial statements were: USD 1 = UAH 5.0500 (2005: USD 1 = UAH 5.0500); EUR 1 = UAH 6.6509 (2005: EUR 1 = UAH 5.9716); LVL 1 = UAH 9.5394 (2005: LVL 1 = UAH 8.5160).

As at 31 December 2007 the principal rates of exchange used for translating foreign currency balances as used in the Bank's interim financial statements were: USD 1 = UAH 5.0500 (31 December 2006: USD 1 = UAH 5.0500); EUR 1 = UAH 7.41946 (31 December 2006: EUR 1 = UAH 6.6509); LVL 1 = UAH 10.644849 (31 December 2006: LVL 1 = UAH 9.5394).

Deposit taking

Corporate deposits accounted for 59.9 per cent. of the Bank's deposit base (current accounts and term deposits) as at 31 December 2007. The Bank's top ten corporate depositors accounted for 22.0 per cent. of the Bank's deposit base as at 31 December 2007. These top ten deposits were in the trade and commerce, municipal authorities, transport and communication sectors of the economy as at 31 December 2007. The corporate deposit base increased by UAH 1,722,602 thousand, or by 93.1 per cent., from UAH 1,851,032 thousand as at 31 December 2006 to UAH 3,573,634 thousand as at 31 December 2007.

As of 31 December 2007, SMEs accounted for 40 per cent. of all customer accounts, 34 per cent. of all term deposits and 55 per cent. of all demand accounts. The following table sets out analysis by economic sector of the Bank's corporate deposit base as at 31 December 2007, 31 December 2006 and 31 December 2005:

Deposit base by economic sector	31	31 December	31 December
	December 2007 (unaudited)	2006	2005
		<i>(UAH thousand)</i>	
Trade and commerce	2,620,323	956,955	443,750
Transport and communication	186,268	148,746	116,758
Finance and insurance	331,313	305,110	35,646
Manufacturing	130,777	133,912	74,403
Other	304,953	306,309	136,503
Total customer accounts (excluding individuals)	3,573,634	1,851,032	807,060

The following table sets out analysis by currency of the Bank's deposit portfolio (including retail customers) as at 31 December 2007, 31 December 2006 and 31 December 2005:



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31 December 2007 (unaudited)

	UAH	USD	EUR	Other	Total
			(UAH thousand)		
Customer accounts	3,624,750	1,941,029	344,213	56,868	5,971,664

31 December 2006

	UAH	USD	EUR	Other	Total
			(UAH thousand)		
Customer accounts	1,581,604	1,465,052	169,556	73,280	3,289,492

31 December 2005

	UAH	USD	EUR	Other	Total
			(UAH thousand)		
Customer accounts	906,490	656,731	33,861	2,891	1,600,063

Trade finance

As a part of its corporate business, the Bank provides its customers with a full range of trade finance services. The Bank implemented and continues to develop a wide range of trade finance products and applies a variety of schemes for supporting the export-import businesses of its clients. The Bank issues documentary and stand-by letters of credit and bank guarantees, provides post-import and pre-export financing and related consultancy services and assistance.

The Bank funds its trade financing activities under schemes implemented with the participation of major banks and international financing companies including The Bank of New York, ING Bank, Commerzbank AG, HypoVereinsbank AG, American Express Bank Ltd., Standard Bank PLC, Bank Austria Creditanstalt AG, Landesbank Berlin AG, Cargill Financial Services International, Inc. and others. The terms of financing vary from one to five years with amounts from UAH 100,000 to UAH 20 million. The Bank estimates that the overall volume of trade finance services carried out by the Bank in 2006 exceeded UAH 500 million.

Income from the Bank's trade finance activities was UAH 16,123 thousand for the year ended 31 December 2007, compared to UAH 10,788 thousand for the year ended 31 December 2006. As of 31 December 2007, SMEs accounted for 74.3 per cent. of the Bank's trade finance activities.

Other corporate services

In addition to the main corporate banking services described above, the Bank is also expanding services to corporate clients to include cash settlement transactions, for example payroll services to corporates and securities transactions.



Retail Banking

Although the Bank has been involved in the retail banking market since 1998, the Bank's retail strategy is relatively new. Since 2005, the Bank, specifically the Department of Operations, has been focusing on expanding its retail banking business in order to take advantage of the rapidly growing retail banking market in Ukraine. Retail banking includes providing current and deposit accounts, customised loans and residential mortgage loans to individuals, debit and credit cards, foreign currency exchange services and money transfers.

As at 31 December 2007, the Bank's retail loan portfolio amounted to UAH 812,455 thousand, or 11.6 per cent. of the Bank's gross loan portfolio, an increase of 117.5 per cent. as compared to UAH 373,493 thousand as at 31 December 2006. As at 31 December 2007, the Bank had approximately 150,000 retail banking customers, compared to approximately 121,700 as at 31 December 2006.

The Bank is currently placing emphasis on developing its retail banking business, both in terms of numbers of customers and products offered to those customers. The main focus in expanding the Bank's retail customer base will be on high net worth (with a monthly income of over UAH 10,000) and professional individuals. Following the Bank's recent strategy review, the Bank will also focus on servicing middle-class customers. To this end, the Bank has been expanding its branch network in order to increase its presence in locations where it can attract new retail customers.

The Bank plans to increase its product offering to retail customers in the near future, with the introduction of loyalty schemes for the Bank's card holders, unsecured consumer loans for employees of the Bank's corporate customers, flexible repayment schedules and fees for consumer loans, residential mortgage loans, and various additional services to be offered from the Bank's ATM network. The Bank also intends to expand its retail client base through joint marketing efforts with its existing corporate clients by offering banking services to the customers of the Bank's corporate clients.

The Bank's retail banking activities are divided into the following categories:

Retail Lending

Retail lending activities include the provision of customised loans, residential mortgage loans, credit cards and debit cards with overdrafts. As at 31 December 2007, the Bank had UAH 812,455 thousand in outstanding retail loans, constituting 11.6 per cent. of the Bank's gross loan portfolio, compared to 11.1 per cent. as at 31 December 2006. Approximately 65.9 per cent. of the gross retail loan portfolio was comprised of mortgage loans, approximately 30.7 per cent. of consumer loans and approximately 3.4 per cent. of credit cards and overdrafts.

The main types of retail loans offered by the Bank are mortgage, consumer and credit card loans.

Mortgage loans are denominated in U.S. Dollars or Hryvnia, are typically fixed-rate and are for a term of up to 15 years. However, the majority of the mortgage loans are for a period of one to five years as they are categorised as mortgage loans due to the nature of the security not the use of the proceeds of the loan. Mortgage loans are advanced and secured by



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existing residential property, and are not made against property not yet constructed. As at 31 December 2007, the Bank had UAH 535,260 thousand in mortgage loans.

Consumer loans are denominated in U.S. Dollars, Euro or Hryvnia, are typically fixed-rate and are for a term of up to one year. As at 31 December 2007, the Bank had UAH 249,452 thousand in consumer loans.

Credit card loans are denominated in U.S. Dollars, Euro or Hryvnia, are typically fixed-rate and are for a term of up to one year. As at 31 December 2007, the Bank had UAH 27,743 thousand in credit card loans.

The Bank has a policy to carefully monitor its retail loan portfolio to assess its risk profile.

Current Accounts and Deposit Taking

The Bank offers its retail customers both current account and term deposit facilities denominated in UAH, U.S. Dollars and Euro. Retail customers' current accounts amounted to UAH 379,365 thousand as at 31 December 2007, or 24.7 per cent. of the Bank's total customers' current accounts, compared to UAH 230,194 thousand, or 23.8 per cent., as at 31 December 2006. Term deposits from retail customers amounted to UAH 2,013,515 thousand as at 31 December 2007, or 33.7 per cent. of the Bank's total deposits from customers (deposit base), compared to UAH 1,208,266 thousand, or 36.7 per cent. as at 31 December 2006. According to the NBU, as at 31 December 2007, the Bank was the 18th largest bank in Ukraine as determined by the NBU in terms of retail deposits and customer accounts. The top 10 retail deposits constituted UAH 208,852 thousand, or 8.7 per cent. of the Bank's retail deposit base, or 3.5 per cent. of the Bank's total deposit base as at 31 December 2007.

ATM network

The Bank offers its customers the ability to withdraw cash from current accounts via its ATM network. As at 31 December 2007, the Bank had a network of 160 ATMs, owned by the Bank. Customers can access a variety of services, including cash withdrawals and information on their accounts. The Bank intends to further widen the range of services offered by the Bank's ATMs. ATMs are located both in branches and outlets and in other locations, subject to appropriate security measures.

As at 31 December 2007, the Bank had a network of 1100 point-of-sale ("POS") terminals. A POS terminal is an electronic device which gives customers the ability to make payments for products, work or services in a trade network, automated cash payout operations, and the execution of payment documentation in electronic form for operations using payment cards issued by the Bank.

Management believes that ATM services are important for attracting customers and increasing the cross-selling opportunities of the Bank's card business.

Cash settlement transactions

The Department of Operations of the Bank offers a variety of cash settlement and transfer services to retail customers, including current accounts, deposit services, foreign exchange operations, cheque book operations, cash transfer operations and cash withdrawals over the counter or via ATMs.



Bank card products and services

The Bank's card business is a growing source of fee and commission income and provides cross-selling opportunities to the Bank. The Bank is a member of the Visa International payment system and a member of the MasterCard Worldwide payment system. The Bank offers both debit cards with an overdraft option and credit cards to its retail customers.

According to the Ukrainian Interbank Payment Systems Member Association, the Bank is 26st amongst the credit and debit card issuers in Ukraine in terms of total cards issued as at 31 December 2007.

As at 31 December 2007, the Bank had issued approximately 201,796 debit cards and 104,732 credit cards. Among other card products and services, the Bank offers salary payment cards which are issued to employees of corporate customers for which it provides payroll services.

Alternative sales channels

During the period from 2000 to 2006 the Bank launched alternative sales channels for its retail banking products, including its customer support services such as the Bank's call centre (launched in May 2004), telephone GSM-Banking (launched in May 2003), internet banking (launched in March 2001) and other customer relationship management technologies. The Bank's call centre offers easy access to information on the Bank's services, as well as convenient and easy management of clients' accounts 24 hours a day, seven days a week. The Bank plans to expand the range of GSM-Banking and internet banking services to include making payments and money transfers.

Funds management activities

The Bank manages the fund for financing of construction (the "FFC") which is one of the structures for financing construction of residential real estate used in Ukraine. The FFC currently finances construction of two residential complexes having the value of UAH 5 million and UAH 60 million. Apart from receiving a management fee, the Bank grants loans to investors of the FFC, earns on commissions from cash settlement transactions conducted through the Bank and benefits from balances on the accounts of the developer opened at the Bank.

Treasury and Capital Markets

The Bank provides a range of treasury and capital markets services, primarily to corporate customers and certain high net worth individuals. Treasury and capital markets services include debt capital markets, brokerage services, securities trading and ancillary services such as custodian services.

Debt capital market services

The Bank launched its corporate bond financial advisory and underwriting service in 2000, when the Bank was the first Ukrainian commercial bank to issue its own domestic corporate bonds. These bonds were in Hryvnias, of an average term of one year and an average interest rate of 11 per cent.

The following year, the Bank was one of the first Ukrainian banks to act as underwriter for its customers in securities transactions. The Bank considers the Ukrainian domestic bond market to be comparatively under-developed and this market represents an opportunity for further



expansion. The debt capital markets services are provided by the Securities Division of the Bank.

Brokerage services and securities trading

The Bank's trading and brokerage business includes the execution of trades in debt securities for corporate customers. The brokerage business involves primarily Hryvnia denominated debt securities of Ukrainian corporate issuers. The Bank engages in brokerage activities on behalf of its corporate customers and high net worth private banking clients, primarily on the First Stock Trading System, (Persha Fondova Torgivelnna Systema) (the "PFTS"). The Bank also maintains a securities portfolio and engages in securities trading on its own account.

Inter-bank Activities

Activities on the inter-bank market include settlement transactions, foreign exchange operations, servicing of correspondent bank accounts, and the granting and accepting of inter-bank loans and deposits. The Bank is ranked as one of the top 20 in the Ukrainian market by daily volumes of inter-bank operations.

Custodian services

The Bank provides a broad range of basic and supplementary custodian services for legal entities and individuals holding securities of Ukrainian issuers. The Bank's current licence authorising it to engage in professional depository services was issued by the State Commission on Securities and Stock Market (the "SCSSM") on 28 December 2006. The bank is ranked as sixth in Ukraine by volume of custodian portfolio.

3.7. Distribution Network

The Bank offers its services through a network of 18 branches, 112 smaller outlets and three self-service outlets (fully automated outlets providing a range of retail banking services) as at 31 December 2007, which are located throughout the industrially and economically developed regions of Ukraine. The Bank's branches are located in the Odessa region, the Kyiv region, and the Dnipropetrovs'k region, Kharkiv, Luhansk, Lviv, Mykolayiv, Kherson, the Autonomous Republic of Crimea, Kyrovograd, Zaporizhya and Donetsk. The Bank plans to expand its distribution network to approximately 200 branches and outlets in the next few years.

The Bank's branches and outlets offer a wide range of banking services including lending, documentary transactions, securities operations, foreign currency transactions, settlement and payment transactions and international payment card operations. Transaction limits for each activity within each branch or outlet are set by the appropriate committees or commissions of the Bank.

Branches offer the full range of the Bank's services to the Bank's corporate and retail customers. Each branch has its own lending limits and decision-making bodies. The Bank's outlets are smaller and may not offer the full range of the Bank's services. All outlets offer current and deposit customer accounts, settlement transactions, lending to retail customers and foreign exchange services. The Bank acknowledges that in order to have a major presence in the Ukrainian corporate and retail banking market, it must have a sufficient network of branches and outlets. The Bank is expanding its distribution network of branches and outlets in the most economically developed and densely populated regions of Ukraine. As



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at 31 December 2007, the Bank had a presence in 12 regions of Ukraine including the Autonomous Republic of Crimea. The Bank intends to expand its presence to 180 districts in Ukraine in the next few years.

The Bank also had, as of 31 December 2007, 200 exchange offices which provide customers with foreign exchange services. Through its subsidiary Regional Investment Bank, located in Riga, Latvia, the Bank intends to continue its expansion into other countries in Central Eastern Europe.

All Ukrainian banks require the approval of the NBU to open new branches and outlets. To date the Bank has not experienced any difficulties in gaining such permissions. Due to the strong real estate market in Ukraine, particularly in Kiev, the Bank faces strong competition for prime locations to open its branches and outlets. The Bank competes for prime retail locations not only with other banks, but also with other types of business.

The Bank spent UAH 292,705 thousand of capital expenditure in relation to its distribution network for the year ended 31 December 2006 and UAH 289,013 thousand of capital expenditure for its distribution network for the year ending 31 December 2007.

3.8. Correspondent and foreign banking relationships

The Bank has a broad network of correspondent banks and, as at 31 December 2007, had correspondent relationships with 46 banking institutions globally, including 22 in Ukraine, 8 in the Commonwealth of Independent States (“CIS”) countries (including Russia and Kazakhstan), 2 in the Baltic region (Estonia and Latvia) and 13 in other countries such as the United States of America (“USA”), Germany, Japan, the Netherlands, Belgium, Austria, Denmark, Poland, and the United Kingdom. The Bank carries out settlement transactions, foreign exchange operations, servicing of correspondent bank accounts, granting and accepting of interbank loans and deposits with correspondent banks.

As at 31 December 2007, the Bank had 57 “Nostro” accounts (accounts with other banks) including accounts with major foreign banks available for international settlements in different currencies, including U.S. Dollars, Euro, pounds sterling, Japanese yen and others, and 37 “Vostro” accounts (accounts held with the Bank by other banks).

3.9. Funding

The main sources of the Bank’s funding are corporate deposits, current accounts held by corporate customers, deposits and salary payment card accounts (whereby the Bank’s corporate customers pay funds directly into accounts of employees held with the Bank) from retail clients and other borrowed funds. Access to other funding sources, including syndicated loans and international capital market issuances, has historically been limited for financial institutions in Ukraine. However, due in part to its cooperation with the World Bank’s programmes in Ukraine, the Bank has been able to attract funding from international financial institutions.

In 2006, the Bank began attracting funding from the international syndicated loan markets.



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The following table sets out the Bank's principal sources of funding as at 31 December 2007, 31 December 2006 and 31 December 2005:

	31 December 2007 (unaudited)	31 December 2006	31 December 2005
		<i>(UAH thousand)</i>	
Due to the National Bank of Ukraine	90,000	82,000	—
Due to other banks	1,013,789	274,871	300,194
Total due to banks	1,103,789	356,871	300,194
Term deposits	4,427,693	2,320,568	1,063,421
Current accounts	1,538,821	968,924	536,642
Total customer accounts	5,966,514	3,289,492	1,600,063
Debt securities in issue	136,661	163,280	27,170
Loan participation notes	522,532	-	-
Other borrowed funds	-	15,718	—
Total principal sources of funding	7,729,495	3,825,361	1,927,427

The Bank's customer deposits increased to UAH 5,966,514 thousand as at 31 December 2007, as compared to UAH 3,289,492 thousand and UAH 1,600,063 thousand as at 31 December 2006 and 31 December 2005, respectively.

Deposits with terms of up to one year are classified as short-term deposits. Deposits with terms exceeding one year are classified as long-term deposits. Current accounts (also short-term, being available on demand) increased to UAH 1,538,821 thousand as at 31 December 2007 compared to UAH 968,924 thousand as at 31 December 2006 and UAH 536,642 thousand as at 31 December 2005.

Term deposits were UAH 4,427,693 thousand as at 31 December 2007 compared to UAH 2,320,568 thousand as at 31 December 2006 and UAH 1,063,421 thousand as at 31 December 2005.

The volume of the Bank's corporate deposits and current accounts increased to UAH 3,573,634 thousand as at 31 December 2007 as compared to UAH 1,851,032 thousand as at 31 December 2006 and UAH 807,060 thousand as at 31 December 2005. Customer accounts include UAH 1,463,509 thousand in deposits held as collateral for loans to customers as at 31 December 2007.

As at 31 December 2007, the aggregate balances of 10 largest customers held with the Bank totalled UAH 1,312,478 thousand, representing 22.0 per cent. of total customer accounts, compared to 13.8 per cent. and 18.7 per cent. as at 31 December 2006 and 31 December 2005, respectively.



3.10. Debt Funding

In November 2006, the Bank drew down on its first U.S.\$25 million syndicated loan facility arranged by Bank Austria Creditanstalt AG (Austria) and Landesbank Berlin AG (Germany). The loan had a six months maturity with an additional six month extension option and was raised for the purposes of the Bank's trade financing activities. The Bank fully repaid this loan in May 2007.

In May 2007, the Bank drew down on its second U.S.\$45 million syndicated loan facility arranged by Landesbank Berlin AG (Germany), Standard Bank Plc (United Kingdom) and VTB Bank (OJSC) (Russia). The loan has a one year maturity with an additional one year extension option and was raised for the purposes of the Bank's trade financing activities.

In July 2007, the Bank drew down a loan from Standard Bank Plc which was funded by issue of the Bank's debut Loan Participation Notes in amount of U.S.\$100 million. The Lead Managers of the issue were Standard Bank Plc and PNP Paribas. The 3-year notes are listed at Swiss Stock Exchange. The Bank used the loan to fund growth in its loan portfolio and for other general corporate purposes.

In October 2007 the Bank attracted its third U.S.\$30 million syndicated loan facility arranged by Bayerische Landesbank AG and Standard Bank Plc. The loan has a one year maturity with an additional one year extension option and was raised for the purposes of the Bank's trade financing activities.

3.11. Equity Funding

The Bank's authorised, registered and issued share capital amounted to UAH 208,896 thousand (inflation adjusted) as at 31 December 2005. In February 2006 the Bank's shareholders voted to increase the Bank's authorised, registered capital to 258,896 thousand and in April 2006 the Bank's shareholders voted to further increase the Bank's capital to UAH 281,896 thousand. As at 31 December 2006, the Bank's authorised, registered and issued capital amounted to UAH 362,396 thousand. During the year 2007, the Bank's shareholders voted to further increase the Bank's capital by UAH 201,500 thousand. As at 31 December 2007, the Bank's authorised, registered and issued capital amounted to UAH 563,896 thousand (inflation adjusted).

In January 2008 East Capital Explorer Financial Institutions Fund has contracted to purchase a 9.98% stake in Pivdennyi Bank for approximately EUR 54m via a new share issue – confirmation from the National Bank of Ukraine was obtained on February 29, 2008. This new successful and extremely transparent deal with East Capital has brought additional positive promotion to the Bank along with a 40% increase in capital.



3.12. Capital Adequacy

The Bank complies with the NBU's mandatory minimum capital adequacy ratios for Ukrainian banks. The NBU's mandatory minimum capital adequacy ratio is currently 10 per cent. The Bank's capital adequacy ratio calculated in accordance with the NBU methodology (being the ratio of capital to total risk-weighted assets) was 11.1 per cent. as at 31 December 2007 compared to 11.9 per cent. as at 31 December 2006 and 11.5 per cent. as at 31 December 2005.

The Bank also complies with the Basel Committee on Banking Supervision (the "Basel Committee") standards on capital adequacy. In accordance with a decision by the shareholders, the Bank must maintain a total capital ratio (calculated in accordance with the Basel Committee standards) in excess of 12 per cent. As at 31 December 2007, the Bank's capital adequacy calculated in accordance with the Basel Committee standards was 12.9 per cent. As at 31 December 2006, the Bank's capital adequacy calculated in accordance with the Basel Committee standards was 13.7 per cent, and as at 31 December 2005 it was 13.7 per cent. According to the Bank's internal policies, it must transfer a minimum of 5 per cent. of profits to a reserve fund but this amount must not exceed 25 per cent. of the Bank's capital. The reserve fund is included in the retained earnings of the Bank.

The following table sets out the Bank's risk weighted asset and capital adequacy ratios (calculated in accordance with the Basel Committee standards) as at 31 December 2007, 31 December 2006 and 31 December 2005.

	31 December 2007 (unaudited)	31 December 2006	31 December 2005
		<i>(UAH thousand)</i>	
Total Risk Adjusted Assets, Off-Balance Sheet Commitments And Market Risk	6,552,318	3,925,022	1,885,261
Share capital	563,896	362,396	208,896
Retained earnings	167,049	64,483	16,090
Minority interest	13,451	52,737	—
Currency translation reserve	7,434	—	—
Tier-1 capital	751,830	479,616	224,986
Tier-1 capital ratio	11.5%	12.2%	11.9%
Revaluation reserve for fixed assets	91,332	48,117	26,348
Revaluation reserve for investment securities available-for-sale	1,099	—	—
Subordinated debt	-	8,107	7,747
Tier-2 capital	92,431	56,224	34,095
Tier-1 and Tier-2 capital	844,261	535,840	259,081
Capital adequacy ratio	12.9%	13.7%	13.7%



3.13. Property

The Bank owns the premises it uses for its head office in Odessa and most of its branches and the Bank leases premises for its branches in Simferopol and Kherson and for its outlets and other banking units. As at 31 December 2007 and 31 December 2006, the net book value of the Bank's premises was UAH 532,934 thousand and UAH 433,375 thousand, respectively as at 31 December 2007.

3.14. Information Technology

The Bank is committed to developing and maintaining an operations and information technology ("IT") infrastructure to ensure the Bank's provision of a high quality service to its clients and minimise operational risk and business interruption.

In 1995, the Bank installed SFTBank software (a product of "40.5" LLC, Ukraine) as its core banking software enabling the Bank to process and account for banking transactions, including customer service, settlement operations and the production of management reports. The Bank has continuously upgraded all of its principal IT systems over the last ten years.

In 2007, the Bank established an off-site back-up centre (five kilometres from the Bank's head office) in order to improve the reliability of the IT system. Back-up of the entire Bank's IT systems are made at this centre in case of any internal errors, interruptions or damage to the main computer communication network. The Bank has also established additional 'mirror' servers which allows for the prompt restoration of the Bank's IT system.

For the purposes of debit card, credit card and salary payment card processing, the Bank utilises the Ukrainian Processing Centre ("UPC"). Since 2000, the Bank's wide area network ("WAN") connects its existing branches to a single network throughout Ukraine. A call centre was established in 2004. The Bank has budgeted approximately UAH 17 million for development of its IT systems from 2007 to 2010 (approximately UAH 5 million for 2007). In 2005 and 2006 the Bank spent UAH 2 million and UAH 3 million, respectively, on IT.



4. RISK MANAGEMENT

4.1. Overview

The Bank's asset, liability and risk management strategy aims to evaluate, monitor and manage the size and concentration of risks arising in the course of the Bank's activities. The Bank carries out risk management in respect of financial, operational and legal risks. Financial risks include credit risk, liquidity risk, interest rate risk and currency exchange risk. Operational and legal risk management involves ensuring that the Bank's internal procedures and policies are complied with in order to minimise exposure to operational and legal risks. The Bank's risk management policies and systems are continuously modified and enhanced to reflect changes in the market and products.

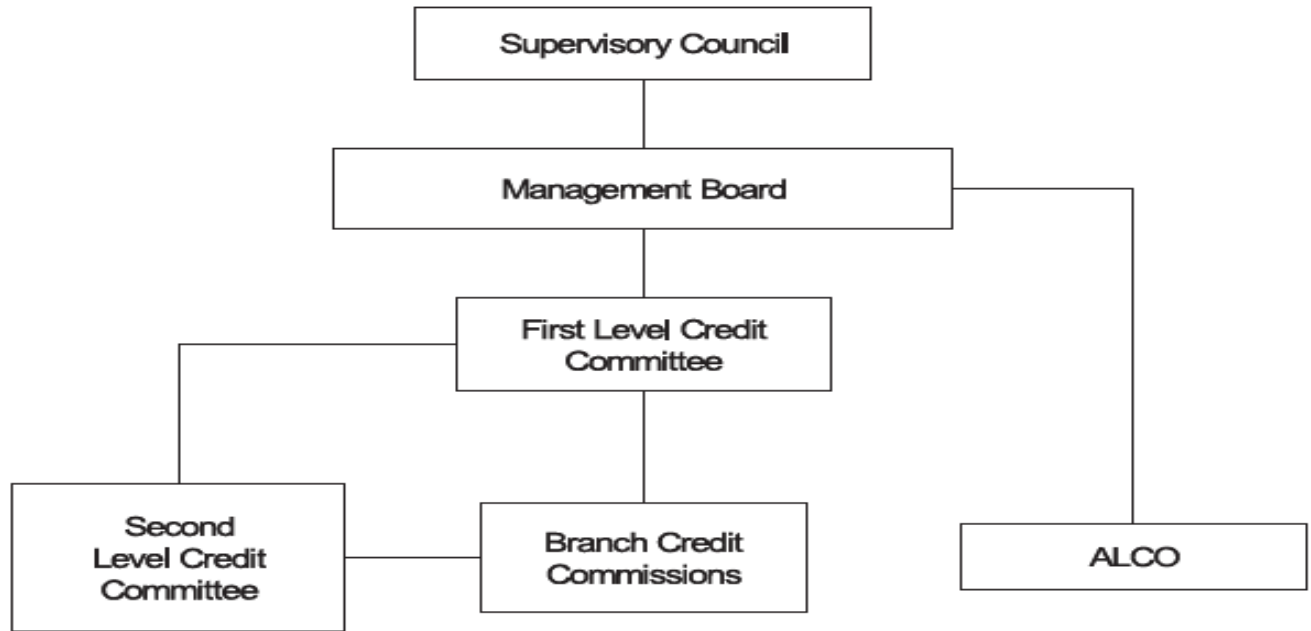
The Bank's strategy for asset and liability management is based on diversification of its assets and liabilities in terms of counterparty, sector and geography, and on balancing assets and liabilities in terms of maturity, sensitivity to interest rate movements and currency risk. The purpose of risk management is to control and monitor the size and concentration of risks arising from the Bank's activities. The principal categories of risk inherent in the Bank's business are liquidity risk, credit risks (risks of possible losses on commercial and consumer loans), and risks arising from inter-bank business, foreign currency rate risk, interest rate risk, operational risk, market risk and litigation risk.

The Bank manages risk in an integrated manner, evaluating it in terms of the correlation of the overall risk level and the Bank's capital. The Bank's risk management and control systems are based on the requirements of the National Bank of Ukraine and the recommendations of the Basel Committee.

4.2. Risk Management Bodies

Risk management policy, monitoring and control are conducted by a number of specialised bodies and units within the Bank. The bodies most actively involved in such management are the Risk Management Division reporting directly to the Management Board and functionally to the Second Level Credit Committee and First Level Credit Committee (as appropriate) and the Assets and Liabilities Management Committee ("ALCO"). In order to minimise credit risks, the Bank has a multi-tier credit approval system for operations which includes the Second Level Credit Committee and First Level Credit Committee of the head office, and Branch Credit Commissions ("BCCs"). In addition, the Supervisory Council and the Management Board are involved in the support, application and monitoring of compliance with the Bank's risk management policies.

The organisational structure and reporting lines of the Bank's risk management bodies are set out in the diagram below.



(a) Supervisory Council and Management Board

The Supervisory Council supervises the activity of the Management Board, First and Second Level Credit Committees and the ALCO, and the credit policy of the Bank submitted to it by the Management Board. The Management Board is generally responsible for the activities of the Bank, including those relating to risk management. The Management Board determines the composition of the Bank’s Credit Committees and the ALCO. In addition, the Management Board is responsible for development and approval of the Bank’s credit policy.

(b) Asset and Liability Management Committee

The ALCO sets its asset, liability and risk management policy in line with its business strategy and makes necessary corrections in light of the Bank’s financial and market position and in accordance with the growth and diversification of its business. The ALCO also sets targets for asset and liability allocations and exposure limits for various banking operations, determines the optimal allocation of the Bank’s funds, and establishes funding policies, including base and target interest rates for assets and liabilities.

The ALCO is delegated its powers with respect to the overall asset and liability management of the Bank by the Management Board. The ALCO currently consists of ten of the Bank’s senior managers and is chaired by the Chairman of the Management Board. The current composition of the ALCO is as follows:

- Vadim V. Morokhovskiy, Chairman of the Management Board and Committee Chairman
- Liya S. Morokhovskaya, Deputy Chairman of the Management Board
- Lyudmila V. Kovalyonok, Chief Accountant
- Elena G. Tsvetkova, Director of Regional Network and Reporting Department
- Vadim V. Mokin, Director of Treasury and International Business Department
- Galina V. Chekeres, Head of Lending Division
- Igor Yu. Dashkovskiy, Head of Dealing Operations Division



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- Tatiana V. Lukanova, Head of Control and Operations Book-keeping Division
- Oksana S. Azarova, Head of Risk Management Division – Committee Secretary
- Olga N. Sapega, Head of Securities Division

The ALCO's composition is determined by the Management Board. The ALCO meets at least once a month and reports directly to the Management Board. It is responsible for controlling the risks arising from the Bank's activities and the development and implementation of policies and methods of risk control as well as asset and liability management policies.

The responsibilities and objectives of the ALCO include:

- monitoring and managing assets and liabilities in accordance with the Bank's business plan and acceptable liquidity levels, market risk levels and inter-bank credit risk levels;
- review of factors affecting profitability and risk exposure of the Bank's transactions;
- determining and controlling implementation of the Bank's policy with regard to interest rate risk management, liquidity risk management, currency risk management, market risk management and inter-bank credit risk management;
- evaluating the Bank's exposures to risks assumed;
- analysing the Bank's activities results: cost of liabilities, assets profitability, net interest margin, spread and trading income;
- establishing and updating the set of limits on particular risks (including counterparty credit limits for financial institutions) and control over their observance;
- establishing limits for interest rates for credit and debit operations of the Bank, limits for total credit portfolio, limits for credit portfolio per currency, limits on maximum tenor and minimum weighted-average profitability for loans; and
- providing information on the Bank's risks to the Management Board.

(c) First Level Credit Committee, Second Level Credit Committee and Branch Credit Commissions

The Bank's credit approval bodies are the First Level Credit Committee, the Second Level Credit Committee and the BCCs which adhere to the established credit policy and strategy of the Bank. The Management Board approves limits for lending decisions made by the First Level Credit Committee, the Second Level Credit Committee and the BCCs, lending decisions for credit exposures over 10 per cent. of the Bank's regulatory capital and loans to insiders and managers. The Supervisory Council approves loans for the Bank's top managers for amounts of EUR 5,000 and higher.

The First Level Credit Committee is responsible for:

- implementing the Bank's credit policy;
- monitoring loan portfolio diversification;
- approving credit transactions and their terms (excluding credit transactions with financial institutions);
- monitoring credit performance and the quality of the Bank's loan portfolio;
- monitoring compliance with NBU requirements concerning credit operations;
- setting provisioning levels for credit operations of the Bank;



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- evaluating credit risk and establishing credit limits for BCCs in co-operation with the Management Board; and
- recognising non-performing and bad credit transactions in co-operation with the Management Board.

The First Level Credit Committee is established in accordance with the Bank's governing statute and internal regulations by the Management Board and currently consists of nine of the Bank's senior managers, chaired by the Chairman of the Management Board. The current composition of the First Level Credit Committee is as follows:

- Vadim V. Morokhovskiy, Chairman of the Management Board and Committee Chairman
- Lyudmila V. Kovalyonok, Chief Accountant
- Valentina D. Grechko, Head of Legal Division
- Grigoriy N. Lyashko, Head of Security Division
- Elena G. Tsvetkova, Director of Regional Network and Reporting Department
- Galina V. Chekeres, Head of Lending Division
- Igor Yu. Dashkovskiy, Head of Dealing Operations Division
- Anna O. Svoboda, Head of Corporate Banking Division
- Oksana S. Azarova, Head of Risk Management and Economical Work Department (who has veto power which cannot be overruled)

The approval of the First Level Credit Committee is required for loan application amounts which exceed the lending limits of the BCCs and Second Level Credit Committee (see below). Decisions are adopted by the First Level Credit Committee by a vote of all members required to make a quorum at the relevant meeting. The number of members of the First Level Credit Committee required for a meeting to constitute a quorum is two-thirds of the total members. A decision of the First Level Credit Committee requires a simple majority and the Chairman has a deciding vote (if necessary).

The Second Level Credit Committee is established by and reports to the Management Board. The Second Level Credit Committee may approve loans to individuals of amounts up to U.S.\$100,000 or UAH 500,000 (for mortgage and cash secured loans) and loans to corporates of amounts up to U.S.\$200,000 or UAH 1,000,000 (for mortgage and cash secured loans) or lower limits depending on the security provided or for non-secured loans. Loan applications may be further referred to the First Level Credit Committee if a decision is not made by the Second Level Credit Committee. The number of members of the Second Level Credit Committee required for a meeting to constitute a quorum is two-thirds of the total members and a decision requires a simple majority (the Chairman has a deciding vote if necessary).

The current composition of the Second Level Credit Committee is as follows:

- Galina V. Chekeres, Head of Lending Division and Committee Chairman
- Natalia A. Kulchitskaya, Deputy Head of Lending Division
- Vadim V. Rodomanov, Deputy Head of Lending Division
- Nina A. Sarycheva, Head of Problem Loans Department
- Igor N. Smetanyuk, Head of Economical Security Department



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Each BCC is established and its composition approved by the Head of the respective Branch. Each BCC consists of the Head of the respective Branch (as the Head of the BCC), Head of the Lending Department of the Branch, Chief Accountant of the branch, branch lawyer and a security official. Each BCC is authorised to approve loans within limits set for it by the First Level Credit Committee, depending on the branch. The maximum limit for total loans to an individual is set at UAH 300,000 (for mortgage loans) and for total loans to a corporate at UAH 1,000,000 (for mortgage loans).

Additionally, depending on BCC's quality appraisal, the limit for each total BCC portfolio is up to a maximum of UAH 15,000,000. The number of members of the BCC required for a meeting to constitute a quorum is two-thirds of the total members and a decision requires a simple majority (the Head of the respective Branch has a deciding vote if necessary).

Each of the Credit Committees and the BCCs is responsible for considering and approving credit decisions and monitoring and reviewing the quality of the Bank's credit portfolio as well as its compliance with the established limits and adequacy of the Bank's provisioning.

The principal categories of market risk to which the Bank, in common with other Ukrainian banks, is exposed through its operations and the way the Bank manages these risks are described below. To date, there have been no material failures of the Bank's risk management system.

4.3. Credit Risk

As a result of its lending operations, the Bank takes on exposure to credit risk, which is the risk that a customer (or counterparty bank, as the case may be) will be unable to pay the amounts due to the Bank in full when due. The Bank manages its credit risk by establishing internal policies and procedures aimed at maintaining credit risk exposure within accepted parameters. It achieves this by monitoring and reviewing the financial standing, ratings and performance of customers and counterparties, by setting and monitoring lending limits, by obtaining corporate guarantees and taking security over borrowers' assets as collateral for loans, by monitoring the creditworthiness of its customers and by maintaining provisions for loan impairment in accordance with NBU requirements and Ukrainian Accounting Standards.

The evaluation of a customer's credit risk is performed through determining the "financial class" of the customer. "Financial class" is assigned on the basis of specific parameters, defined in terms of both the nature of the potential borrower's business and the specific transaction. For corporate borrowers these parameters include the general financial condition of the customer (determined on the basis of indices pursuant to the financial statements of the customer, financial plans and forecasts); the qualitative characteristics of the customer's business, internal and external factors affecting the customer's business and its financial condition (its market position, prospects for the industry sector, level of competition, its management and structure, valuation of its production capacity and other factors); and the level of devaluation (deterioration of quality of collateral, conflicts within the ownership structure of the customer, increase in the amount of overdue accounts receivable and accounts payable). For individual borrowers "financial class" is determined on the basis of appraisal of creditworthiness, social position (i.e. age, marital status, work position,



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education), level and stability of income of the customer, their ability to provide collateral, credit and other records with the Bank and certain other factors.

When considering loan applications, different financing options are examined, taking into account the analysis of possible sources for repayment of the loan and the availability of collateral or guarantees. Accordingly, different credit products (including term loans, credit lines, overdrafts, guarantees, trade finance, and operations with promissory notes) are offered to clients depending on their needs, their financial performance, specific credit risks and the type of collateral proposed.

All loan applications are subject to a detailed review procedure as set forth in “Lending Policies and Procedures”.

The Bank structures the levels of credit risk it assumes by placing limits on the amount of risk accepted in relation to one borrower, or group of borrowers, limits for total credit portfolio and limits on maximum tenor for loans. The Bank also places limits on the amount lent per sector of economy and on the amount of unsecured loans. Such risks are monitored by the Bank on an ongoing basis.

The maximum credit limit for a single borrower (or group of borrowers) is set by the NBU at 25.0 per cent. of the Bank’s regulatory capital. As at 31 December 2007, the Bank’s largest exposure to a single borrower and largest single loan amounted to (i) 17.8 per cent. of the Bank’s equity (calculated in accordance with IFRS) or (ii) 22.7 per cent. of the Bank’s regulatory capital (calculated in accordance with NBU methodology).

The Bank reviews the outlook for the borrower’s industry sector and any current or potential changes in factors influencing the borrower’s business and its financial condition, and the political and economic situation, governmental control and regulations in its country or region. In addition, the Bank carries out analysis of the effectiveness of the borrower’s management structure, organization structure and production model. The Bank also examines risks connected with the activities of related parties such as the borrower’s contract counterparties and their potential influence on the ability of the borrower to meet their repayment obligations under the loan.

Credit officers within the Bank monitor operations with its customers on a regular basis and notify the Committees, the BCCs, and the Management Board both periodically and in the event of any exceptional change in a customer’s circumstances. The Bank either confirms the existing terms of a loan agreement or contacts the customer if it is necessary to review the conditions of a loan or enforce early repayment.

The Bank imposes limits on the amounts which individual branches are authorised to lend. Limits are set with respect to the amount of individual loans and total loans that can be granted by a branch. The First Level Credit Committee regularly reviews the lending activity of all branches in order to examine the branches’ compliance with the Bank’s credit procedures and conduct analysis of the quality of the branches’ loan portfolio. Depending on the results of such review the Management Board may elect to increase or decrease credit limits assigned to a particular branch. If the amount of a loan requested by a customer exceeds the limits



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established for the respective BCC, the case is escalated to the Second Level Credit Committee or the First Level Credit Committee.

The Bank's corporate loan book is broadly diversified over different sectors of the economy. The credit policy of the Bank seeks to maintain the diversification of credit risks avoiding concentrations of total indebtedness per individual borrower or particular sector of the national economy. The control of risks related to any individual borrower or group of borrowers in a sector is carried out by carefully monitoring adherence to the existing limits. The Bank is focused on further diversifying its credit risk profile by increasing its presence in the SME lending market, and also actively developing its retail business.

Credit Risk is one of the principal risks of the Bank. As loans constitute a significant portion of its assets, credit risk management is therefore a priority for the Bank. The identification and adequate measurement of credit risk is one of the key factors contributing to the increased efficiency of the Bank's operation. The Bank manages its credit risk by establishing exposure limits for single borrowers, groups of borrowers and industries, as well as by complying with other exposure limits established by the NBU. The Bank also mitigates its credit risk by conducting thorough reviews of prospective borrowers, obtaining collateral, corporate and personal guarantees and ongoing credit monitoring. Credit Risk is also reduced by forming appropriate provisions for loan impairment and loan losses.

Credit Risk for off-balance sheet financial instruments such as guarantees is defined as a 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 First Level Credit Committee sets exposure limits for off-balance sheet exposures and the ALCO sets counterparty limits for off-balance sheet transactions with banks and other financial institutions. They review transactions that would exceed these limits and, if necessary, adjust the limits. The Bank's back office departments monitor the compliance with limits for off-balance sheet transactions with corporate clients and banks on a daily basis.

All loan applications are subject to a detailed review procedure.

The Bank has developed a set of credit products which make it possible to facilitate the credit risk management system and unify the fundamental approaches to assessment of a borrower, security requirements, and structure of credit operations. On top of this, the Bank offers a number of credit products which require specific approaches to credit risk management; structured and trade finance, as well as project finance, are the most complex of these.

Control over loan quality is a relevant element of the Bank's credit risk management. The Bank has developed a mechanism of control which ensures the highest possible protection of the Bank's interests in the process of loan issuing. It includes the monitoring of documentation in the credit file to make sure that it remains complete and valid until maturity.

The credit risk management system is complemented by:

- constant monitoring of borrowers and collateral for issued loans;
- management of problematic assets; and



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- the creation of adequate loan loss provisions.

The Bank's risk management policies are of utmost concern to the Bank's management. The general approach follows a rather conservative pattern. A number of general ratios related to risk evaluation are enforced in conformity with the regulations of the NBU, and the Bank fully complies with these requirements.

Credit Risk related to Corporate Lending

The Bank's Corporate Banking sector (including SMEs) policy is to maintain a broad spread of exposure across business sectors which reflects the Bank's areas of expertise. Credit exposure to businesses is assessed individually by the Assets and Liabilities Management Committee ("ALCO").

The quality of the overall portfolio is monitored using a credit grading system calibrated to the probability of incurring losses. All aspects of credit management are controlled centrally for the Bank and branches network. The Management Board receives regular reports from the ALCO on new facilities and changes in facilities, sector exposures, bad debt provisions and problem loans.

The evaluation of a potential corporate borrower includes the analysis of certain risks including financial standing, industry, market, management and operational risks. On the basis of the complex analysis of the customer and in conformity with the Bank's procedures, experts in the Lending Division assess a borrower's creditworthiness with regard to each particular transaction and total exposure to the borrower and define the borrower's risk category. Corporate loans account for 95 per cent. of all non performing loans ("NPLs") of the Bank.

Credit Risk related to Retail Lending

Retail lending is tightly controlled through advanced credit and scoring techniques by the ALCO. The Management Board is regularly informed on the performance of the portfolio by the ALCO. On the basis of expert appraisals and using mathematical models, the Bank has developed certain methods for different products which allow the acceptable extent of credit risk to be determined. The Lending Division is responsible for structuring the credit transaction on the basis of its analysis of the customer. Assessment of collateral is performed by another member of staff from the independent Division of Expert Assessment and Collateral Liquidity Analysis which carries out the assessment of loan security. Retail loans account for 5 per cent. of all NPLs of the Bank.

Credit Risk related to Inter-Bank Operations

Credit risk in relation to inter-bank operations arises mainly as a result of such loans being unsecured, although such loans typically have relatively short-term maturities, generally ranging from one day up to one month. The Department of Operations follows limits set out by the ALCO.



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These limits define blank (unsecured) inter-bank credits and deposit swap operations (which are secured). The maturity of blank credits is normally from overnight (one day) up to 30 days. The maturity of swap operations is from overnight (one day) up to 30 days. As at 31 December 2007, amounts due from other banks amounted to 0.5 per cent. of the Bank's total assets, as compared to 0.7 per cent. as at 31 December 2006. The Bank sets separate limits for bank counterparties based on an evaluation of their financial condition and on any available non-financial information (such as the counterparty's shareholders, customers, the quality of its management, its market position, the concentration of its activity and the rate of its growth). These limits restrict the amount and terms of the loan.

The ALCO approves credit risk limits for loans issued to banks. The Bank uses its own methods for assessment of banks' solvency and an automated system designed for monitoring financial statements of credit institutions. The fixed inter-bank limits can be exceeded when exposure is secured by certain assets, such as government securities and cash.

Monitoring Credit Risk

The Bank monitors performance by borrowers of their obligations under their loan agreements, primarily a borrower's obligation to pay interest and repay principal. Lending Division monitors the financial condition of borrowers and the quality of underlying collateral on the basis of information provided by borrowers on a quarterly basis to determine whether loans are being used for the purposes prescribed, whether a corporate borrower is meeting targets set in its business plans, collateral values, and certain non-financial information, such as information on actual or pending legal proceedings involving the relevant borrowers. Regular monitoring of the Bank's loan portfolio and underlying collateral enables the Bank to react to changes in the quality of particular loans and determine whether changes to the Bank's standard terms and conditions of lending are necessary. The Management Board Credit Committees and BCCs are notified of the results of this monitoring on a regular basis or on the occurrence of any particular warning signs. Based on its analysis, the Bank either confirms the terms and conditions of the relevant outstanding loans or, where necessary, negotiates amendments with the borrower or enforces an early repayment.

Off-Balance Sheet and Related Party Credit Risk

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 Department of Treasury and International Business Securities Division of the Bank applies the same credit policies and procedures for evaluating and monitoring credit risk for any off-balance sheet and contingent liabilities. The department applies the same approach to transactions with related parties as to arm's length transactions. If the level of risk does not fall within the parameters set by the Bank, it will either reject the loan application or require the transaction to be secured by cash collateral. Off-balance sheet activities include the provision of guarantees, letters of credit and guaranteeing promissory notes with "avals" (endorsements). As at 31 December 2007 the value of guarantees (including promissory notes endorsements) and letters of credit issued by the Bank amounted to UAH 354,577 thousand and UAH 33,722 thousand, respectively.



4.4. Liquidity Risk

Liquidity risk arises from mismatches between the maturities of assets and liabilities, which may result in the Bank being unable to meet its obligations in a timely manner. It arises in the general funding of the Bank's activities and in the management of its positions and includes both the risk of being unable to fund assets at appropriate maturities and rates and the risk of being unable to liquidate an asset at a reasonable price and within an appropriate period of time. Managing and controlling mismatches of the maturities and interest rates of assets and liabilities is fundamental to the management of the Bank. An unmatched position may potentially enhance a bank's 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.

The Bank's policy in relation to liquidity risk is that liquidity prevails over profitability. The Bank has developed a comprehensive set of procedures and systems to implement its liquidity risk management strategy. These procedures define the structure of relations between different bodies within the Bank for the purposes of risk management and liquidity monitoring and allocate responsibility for monitoring compliance (and taking actions to correct any potential non-compliance) within established limits.

The Bank manages the liquidity risk at three levels. Within the first level, the Risk Management Division develops the balance sheet ratios with regard to the volumes and structure of the Bank's assets and liabilities from a strategic planning perspective and submits them for approval by ALCO. Following ALCO's approval, the respective balance sheet ratios are incorporated into the Bank's business plan by the Financial Politics Division.

At the second level, the Risk Management Division prepares the liquidity measurement reports (asset liability mismatch (gap) report and cash-flow projection report) on a monthly basis to be submitted for ALCO's approval. The decisions of ALCO made on the basis of these reports are mandatory for implementation by the Bank's units, which implementation is monitored by ALCO. This level provides the basis for funding and pricing decisions. The third level of liquidity management provides for matching cash in-flows with cash out-flows on a day-to-day basis and is performed by the Department of Treasury and International Business of the Bank subject to internal procedures of the Bank and ALCO's decisions. The Department of Treasury and International Business manages the Bank's balances with the NBU and with other correspondent banks during a day on the basis of information provided by other departments of the Bank generating cash flows.



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The liquidity position of the Bank as at 31 December 2007 (unaudited) 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	From 12 months to 5 years	Over 5 years	No stated maturity	Total
Assets							
Cash and cash equivalents	1 037 975	-	-	-	-	-	1 037 975
Securities at fair value through profit or loss	70 878	-	32 066	16 344	-	-	119 288
Due from other banks	-	30 330	9 559	-	-	-	39 889
Loans and advances to customers	1 004 856	738 306	1 477 164	3 238 957	412 750	-	6 872 032
Investment securities available for sale	-	-	-	-	-	11 230	11 230
Other financial assets	9 674	1 173	7 636	20 851	-	-	39 335
Total financial assets	2 123 383	769 809	1 526 425	3 276 152	412 750	11 230	8 119 749
Liabilities							
Due to the NBU	-	-	90 000	-	-	-	90 000
Due to other banks	631 185	22 145	360 459	-	-	-	1 013 789
Customer accounts	1 735 189	444 910	1 795 972	1 978 622	11 820	-	5 966 514
Debt securities in issue	-	-	30 250	106 411	-	-	136 661
Loan participation notes	-	-	-	522 532	-	-	522 532
Other financial liabilities	16 934	9 317	21 772	-	-	-	48 024
Total financial liabilities	2 383 309	476 372	2 298 453	2 607 566	11 820	-	7 777 519
Net liquidity gap at 31 December 2007	-259 925	293 437	-772 028	668 587	400 930	11 230	342 230
Cumulative liquidity gap at 31 December 2007	-259 925	33 511	-738 517	-69 930	331 000	342 230	

The Management of the Bank believes that, despite a substantial portion of customer accounts having maturity on demand or less than one month, diversification of these balances by number and type of customers, including certain related party balances (comprising only 13.7 per cent. of customer accounts), and the past experience of the Bank, indicate that these balances provide a reliable and relatively stable source of funding for the Bank. However the Bank is seeking to redress the mismatches in the Bank's liquidity position, and any further mismatches which may arise with the growth of the Bank's corporate and retail operations, by borrowing more funds on the domestic market along with taping international syndicated loan markets and by borrowing funds under the Loan Agreements to funded by the issue of the Notes.



In addition, the Bank is subject to liquidity requirements set by the NBU. The Bank's risk management system incorporates the NBU's requirements and does not permit limits set by the NBU to be exceeded.

The liquidity management policy of the Bank is based on classic requirements which enforce the ratios applied in respect of various groups of liquid assets and liabilities. The estimation of such internal ratios was carried out based on the facts of the 2004 banking crisis, that is, a maximum possible fluctuation of the resource base was taken into account. The level of liquidity is monitored on a daily basis and is examined monthly by the Risk Management Division. In this context, it is to be noted that the Bank is not dependent on large depositors.

The Liquidity Management Department within the Department of Treasury and International Business supervises payment position daily using a calendar of payments and gap-tables. However, the Management of the Bank approved changes to make the liquidity management policy less aggressive and more conservative at the beginning of 2007. Thus, obtaining attractive ratings from international rating agencies and entrance to international money and capital markets brings the ability to attract long-term funds and forms the basis for the application of the new conservative policy.

4.5. Interest Rate Risk

The Bank is exposed to interest rate risk, principally as a result of lending at fixed rates in amounts and for periods which differ from those of term deposits at fixed interest rates. 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. The Bank may incur losses in the event of unfavourable movements in interest rates. The Bank does not have an active derivatives hedging practice.

Net interest spread and margin is checked by ALCO every month. Projected interest rate risk is evaluated in the framework of a Sensitive Asset and Liabilities Revaluation Report (Interest Rate Sensitive Gaps). The evaluation and analysis of the size of interest rate risk is performed at least once a month. The results of such evaluation and analysis are discussed at ALCO meetings.

For the Bank, market risk manifests itself primarily in the form of interest rate risk. Interest risk policy statements, approved by the Bank's Management Board, specify the scope of the Bank's market activity, market risk limits and delegated authorities. The policy is executed by the ALCO, which meets on a monthly basis. Its prime task is to assess the interest risk inherent in the maturity and re-pricing characteristics of the Bank's assets and liabilities. It sets limits within which the Bank's Department of Treasury and International Business manages the effect of interest rate changes on the Bank's overall net interest income. The principal analytical techniques involve assessing the impact of different interest rate scenarios and changes in balances over various time periods.



The following are key elements of the Bank's interest rate risk management policy:

- An established system of strict gap limits for interest rate changes of assets and liabilities;
- Permanent monitoring of market interest rates;
- Monthly data collection and research analysis pertaining to interest rate movements; and
- Assessment of level of possible negative influence on budgeted income – as per VAR calculation.

4.6. Currency Risk

Currency risk is the risk of losses resulting from adverse movements in different foreign currency exchange rates. Currency risk results from the Bank having long and short positions in different currencies. Such positions are calculated as differences between assets and liabilities in the same currency. Currency risk (the risk of open currency positions) is limited by open currency position regulatory ratios (limits) set by the NBU and ALCO. The exchange rate of the most important currency pair – UAH/USD – is administratively regulated and is effectively fixed. Changes of this rate occur at the discretion of the NBU. The maximum daily FX value at risk in December 2007 amounted to less than 0.5 per cent. of the Bank's capital.

The ALCO sets limits on the level of exposure by currency and in total for both overnight and intraday positions, which are monitored daily. Currency risk is centrally controlled at the head office level by the Department of Treasury and International Business. Limits on open currency positions are set for the Bank as a whole, for its branches and business departments from which the risks originate.

The Department of Treasury and International Business monitors compliance with these and submits reports for consideration to the Risk Management Division and the ALCO.

The net currency position of the Bank at 31 December 2007 is set out below:

	UAH	USD	Euro	Other	Non-monetary	Total
Assets	<i>(In thousands of Ukrainian Hryvnias)</i>					
Cash and cash equivalents and mandatory reserve balances	693 228	181 427	49 997	113 324	0	1 037 975
Other securities at fair value through profit or loss	58 301	25 491	11 402	24 093	0	119 288
Due from other banks	12 309	13 076	7 808	6 696	0	39 889
Loans and advances to customers	3 348 221	3 216 116	275 516	32 179	0	6 872 032
Investment securities available-for-sale	11 230	0	0	0	0	11 230
Current income tax prepayment	5 168	0	0	0	0	5 168
Intangible assets	0	0	0	0	4 511	4 511
Premises and equipment	0	0	0	0	532 934	532 934
Other assets	27 187	4 688	4 171	3 288	0	39 335
Total assets	4 155 645	3 440 798	348 894	179 580	537 445	8 662 362
Liabilities						
Due to the National Bank of Ukraine	90 000	0	0	0	0	90 000
Due to other banks	257 445	739 051	1	17 292	0	1 013 789



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Customer accounts	3 624 750	1 941 029	343 916	56 819	0	5 966 514
Debt securities in issue	0	76 809	59 852	0	0	136 661
Loan participation notes	0	522 532	0	0	0	522 532
Deferred income tax liability	40 460	0	0	122	0	40 581
Provisions for liabilities and charges and other liabilities	7 124	22 402	15 079	3 418	0	48 024
Total liabilities	4 019 778	3 301 823	418 849	77 651	0	7 818 101
Less fair value of currency derivatives						
Net balance sheet position, excluding currency derivatives	135 866	138 976	(69 955)	101 929	537 445	844 261
Currency derivatives	90 800	(134 483)	43 683			
Net balance sheet position, including currency derivatives	226 666	4 493	(26 272)	101 929	537 445	844 261

NBU sets the following limits on open foreign currency positions:

- General open foreign currency position limit not more than 30 per cent. of regulatory capital;
- General long open foreign currency position limit not more than 20 per cent. of regulatory capital;
- General short open foreign currency position limit not more than 10 per cent. of regulatory capital;
- Long open foreign currency position limit in any (one) hard currency not more than 15 per cent. of regulatory capital;
- Open foreign currency position limit in soft currencies and in all banking metals together – not more than 5 per cent. of regulatory capital; and
- Open forward foreign currency position limit not more than 10 per cent. of regulatory capital.

The Bank presents its currency swap arrangements on a net basis as derivatives in other assets on other liabilities respectively. Currency risk is significantly limited by the regulations enforced by the NBU according to which the open position in all currencies should not exceed 30 per cent. of a bank's regulatory capital. The Bank's activity on foreign exchange markets is focused on customer related foreign exchange operations on covered spot basis. The Bank does not hold open positions on the 'hard forex' market.

In addition to the open position limits, the Bank has established stop-loss limits which are being reconsidered on a one-day Value at Risk calculation basis. The following are key elements of the Bank's currency risk management policy:

- The system in place sets limits for amount of open currency position and monitors and controls all types of currency risk;
- Trading limits are applicable to transactions of the Department of Operations and cash exchange transactions;
- There is a stop-loss limit employed that restricts losses;
- All open positions supervision is conducted on-line in real-time system; and
- The level of stated limits confines the amount of probable one-time losses to below one per cent. of equity.



4.7. Risk Monitoring

The monitoring of compliance with procedures for financial risk management and the maintenance of their constant adequacy and efficiency is performed by the Risk Management Department which reports its findings to the ALCO.

4.8. Risks Related to Trading in Securities

The Bank's Management believes that analysis of market risk is of limited usefulness in Ukraine. Analysis of market risk (as the term is more commonly used in economically more developed countries) in the Ukrainian financial market is relatively less valuable than an appropriate credit analysis of the particular security issuer. Traded debt securities, although available for sale, are not always liquid (although the Bank considers them generally to be a good investment, if a holder is able and intends to hold them to maturity).

In addition, trade volumes are small, deals are sporadic, terms of deals are individually set by buyers and sellers in an over-the-counter manner, and there is no actual market-making institution. A similar situation exists with traded shares (with less transparency and much smaller trade volumes).

The Bank's investment securities available-for-sale are specified in the table below:

	31 December 2007 (unaudited)	31 December 2006	31 December 2005
		<i>(UAH thousand)</i>	
Corporate bonds	—	6,707	60,842
Corporate shares	12,912	11,017	4,375
Promissory notes	—	—	150
Less: provision for impairment of investment securities available-for-sale	(1,682)	—	(2,825)
Total investment securities available-for-sale	11,230	17,724	62,542

The Bank's other securities at fair value through profit or loss are specified in the table below:

	31 December 2007 (unaudited)	31 December 2006	31 December 2005
		<i>(UAH thousand)</i>	
Ukrainian corporate bonds	50,236	28,590	4,951
Ukrainian municipal bonds	5,297	5,340	5,039
Ukrainian corporate shares	3,441	40	225
Latvian government debt securities	23,827	52,966	—
Latvian corporate debt securities	1,870	5,017	—
Other non-OECD region corporate debt securities	34,616	22,846	—
Total other securities at fair value through profit or loss	119,288	114,799	10,215



The Bank has minor volumes of equities. Debt securities in the Bank's portfolio are intended mostly for liquidity management purpose.

4.9. Operational and Legal Risk

Operational risk arises from the potential for key systems failures, breaches in internal controls or from external events resulting in financial loss or reputation damage. Key operational risks include outsourced contracts, payment systems and information systems. Operational risk is controlled and mitigated through comprehensive, ongoing risk management practices which include formal internal control procedures, training, segregation of duties and responsibilities, delegated authorities and contingency planning. The Internal Audit and Control Division performs a programme of operational reviews and reports regularly to the Management Board. The division managers are responsible for controlling operating risks within their areas of accountability and for compliance with the Bank's policies which are extensively documented.

In 2006, the Bank developed and implemented a complex system of operational risk management, which classifies all operational risks to which the Bank is exposed, sets forth the procedure for revealing and assessment of operational risks and establishes specific operational risk control and reporting systems. The system of operational risk management has been developed according to recommendations of the Basel Committee and applies to all divisions of the Bank.

The Bank also uses the following procedures to minimise its operational risk:

- authority separation when performing bank operations and transactions (incorporated in operating procedures);
- access rights to information systems are limited appropriately;
- audits (registration and monitoring) of users' actions are performed;
- access to the non-public areas of the Bank's premises is restricted;
- data back-up is performed and back-up data storage is supported;
- the Bank's primary information system is duplicated – there is a standby IT centre (Reserve Centre) located outside the Bank's Head Office;
- there is an Uninterrupted Operating Support Plan (emergency plan and procedures for switching to standby IT centre and supporting its operations); and
- consistent with the practice of other Ukrainian banks, the Bank insures the premises and official vehicles which are owned by it but the Bank does not insure leased premises or vehicles, nor does it insure equipment, property, ATMs or cash in ATMs. The Bank, however, has established security measures to protect these items including CCTV, alarm systems and the protection of the State security force. ATMs are, by design, constructed to prevent robbery or damage and contain a limited amount of cash. Property and equipment purchased by the Bank is covered by warranties from the manufacturer which provide for replacements in the event of theft or damage. The Bank is planning to insure items currently un-insured by the end of July 2007.



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 legal advice the Management is of the opinion that no material losses will be incurred in respect of claims. Accordingly, as at 31 December 2007, and before at year-end 2006, no respective provisions were made.

The Bank's Legal Division monitors and oversees the management of legal risks. This includes applying procedures to protect against the risk of providing loans to entities which lack requisite power or authority and against the risk of failure to secure loans over relevant assets in an effective manner.

4.10. Lending Policies and Procedures

First Level Credit Committee, Second Level Credit Committee and Branch Credit Commissions

The Bank's First Level Credit Committee and the ALCO are responsible for implementing the Bank's lending strategy and forming a balanced and diversified loan portfolio. Lending decisions are made by the ALCO, Credit Committees and BCCs within the limits of their respective authorities. The information below sets out the lending limits established by the Bank, which are in accordance with the NBU requirements:

Corporate Lending

First Level Credit Committee

- Loans and other credit exposures up to 10 per cent. of the Bank's regulatory capital.
- Credit exposures for amounts equal or exceeding 10 per cent. of the Bank's regulatory capital are subject to approval of the Management Board.

Second Level Credit Committee

- Mortgage and cash secured loans for legal entities of amounts up to U.S.\$200,000 or UAH 1,000,000 (lower limits for other loans depending on the security).

Branch Credit Commissions ("BCCs")

- Limits set depending on a branch's performance and credit portfolio's quality. The maximum limit currently existing for loans is UAH 1,000,000 per borrower (for mortgage loans) or lower limits depending on the security provided.

Retail Lending

First Level Credit Committee

- Loans and other credit exposures up to 10 per cent. of the Bank's regulatory capital. Credit exposures for amount equal or exceeding 10 per cent. of the Bank's regulatory capital are subject to approval by Management Board.

Second Level Credit Committee

- Loans up to U.S.\$100,000 or UAH 500,000 (for mortgage and cash secured loans) or lower limits depending on security provided or for non-secured loans subject to respective limits.



Branch Credit Commissions

- Lending limits set depending on a branch's performance and credit portfolio quality. The maximum limit currently existing for loans is UAH 300,000 per borrower (for mortgage loans) and lower limits depending on the security provided. The maximum existing limit for a branch is UAH 5,000,000 for lending to individuals.

Inter-Bank Lending

Asset and Liability Management Committee

- Credit exposures up to 25 per cent. of the Bank's regulatory capital. Credit exposures for amount equal or exceeding 10 per cent. of the Bank's regulatory capital are subject to approval by the Management Board.

Credit Review Process

Credit applications to the Bank are considered by a variety of decision-making bodies. Over 95 per cent. of corporate lending decisions are made by credit bodies of the Bank's head office, the First Level Credit Committee and the Second Level Credit Committee.

Retail lending decisions are made in branches (by BCCs) within predefined authority limits. Any applications and decisions that are not standard or exceed authority of the branch are referred for consideration to the Bank's head office.

The approval procedure for both corporate and retail customers is illustrated below:

Initiation

- Preliminary negotiations with a potential borrower;
- Informing clients of parameters, terms and conditions of lending; and
- Explaining loan approval process.

Preparatory stage

- Collecting documentation, verifying company and management background (in the case of corporate borrowers);
- Assessing strengths and weaknesses of the borrower (financial, market and commercial risks); and
- Based on the conclusions of a credit officer, an authorised employee of the Bank may make a decision at this stage to reject a loan.

Verification stage

- Borrower's business activity is verified (corporate) or borrower's creditworthiness analysis is conducted (individual).

Decision-making

- A decision on the loan is made by the appropriate BCC/Credit Committee (as the case may be).

Finalisation

- Preparation of credit file; and
- Disbursement of funds.



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The Bank extends very few unsecured loans (the Management estimates this to be approximately 10 per cent. of the Bank's total loan portfolio to corporates as at 31 December 2007). The unsecured loans extended by the Bank include mostly overdraft facilities.

ALCO determines the Bank's loan pricing strategy. ALCO sets minimum rates for lending and reviews them regularly depending on market rates and the Bank's performance indices. The actual lending rates are established by Credit Committees/BCCs and are based upon the term and currency of a particular loan and sources of funding for such loan, together with information on the borrower including credit record, rating, collateral and use of funds.

Projects in respect of which branches receive loan applications in excess of their respective lending limits are subject to a procedure of coordination with the Bank's head office. Officers within the Credit Committees check each loan application exceeding such authorised limit to ensure that it conforms to internal regulations and to the Bank's credit policy and then the Second Level Credit Committee or the First Level Credit Committee approve or refuse the disbursement of funds.

The Bank is continuously working on the improvement of its lending procedures and training of staff working in this field to reduce credit risks.

Security Division

When considering a credit application, the Security Division of the Bank verifies the authenticity of the data given by the borrower and checks the client's reputation and history. In addition, the NBU has recently established a central credit bureau in Ukraine which is intended to maintain records of individuals' credit histories and, therefore, there will be additional databases from which the Bank expects to obtain credit records.

Collateral

The Bank in most cases requires collateral, personal or corporate guarantees and/or assurance arrangements as security for each loan. As of 31 December 2007, 90 per cent. of loans were collateralised. Acceptable collateral includes real property, securities, industrial equipment, vehicles, airplanes, ships, precious metals, raw materials and inventory. In most cases, collateral, guarantees and assurance arrangements, separately or together, exceed the principal of the loan, accrued interest and commissions. The following table sets out the Bank's collateral by type:

The Bank believes that collateral is an essential means of minimising credit risk, although it should not be considered to be the principal source of repayment of a loan. Collateral eligibility is determined by taking into account the form of ownership of the borrower, its credit history, financial performance, credit rating and the term of the loan being considered.

Property to be pledged as collateral is also subject to independent appraisal or appraisal by the Bank's Division of Expert Assessment and Collateral Liquidity. Collateral is required to



offset the risk of non-payment of principal and interest. The provision of collateral is normally required for all types of loans, except for unsecured overdrafts.

The monitoring of pledged property is carried out through inspections made by Collateral Monitoring Department or a branch's credit officers every three months. The portion of collateralised loans was approximately 90 per cent. of the Bank's total loan portfolio as at 31 December 2006 and as at 31 December 2007.

Loan Classification and Allowances

The classification of loans for the purpose of risk assessment and establishing of loan impairment provisions is done according to the NBU regulations.

The NBU requires that when classifying loans the following economic factors must be taken into account:

Main economic factors of a borrower's activity

Additional economic factors

1. Solvency Factors

- Current liquidity
- Term liquidity
- Total liquidity

2. Financial Stability Factors

- Mobility of the own funds
- Independence

3. Profitability Factors

- Asset profitability
- Sales profitability

4. Net turnover on a borrower's current accounts

- Autonomy factor
- Financial stableness factor
- Business activity factor
- Principal activity profitability
- Ratio of due from amount and due to amount
- Ratio of the turnover amount and lending liabilities amount



In addition, the following factors contribute when determining the “financial class” of a borrower:

Increasing factors

- Positive credit history
- Stable market position (market share)
- Very liquid collateral
- State order/demand and state support
- Positive business image and professionalism of management
- Presence of financial guarantors
- Progressive increase of turnover
- Increase of a borrower's securities' quotations

Decreasing factors

- Non-fulfilment of the business plan
- Progressive decrease of turnover
- Significant decrease of a borrower's securities' quotations
- Criminal procedure against a borrower's management
- Significant loss of market share
- Negative credit history
- Bankruptcy proceeding against a borrower
- Lack of collateral (insufficient collateral)
- Absent or late financial reporting by a borrower (loans become maximum D-class (see below) automatically)

The Bank calculates a borrower's “financial class” by using an internal grading system. Depending on the debt servicing, a risk category (standard, watch, substandard, doubtful or bad) (see “Risk Categories of Credit Operations”) is assigned to each particular loan. Taking into account the value and type of security, the amount of provision is then determined.

Performance of loans in the sense of repayment and necessity of any enforcement is assessed by the Management according to the following criteria:

- loans recognised by the Bank as being doubtful to be repaid;
- loans extended to the persons or entities directly or indirectly related to a borrower whose loans are recognised by the Bank as doubtful to be repaid;
- regular delays in payments under credit agreements;
- actual or expected strong decrease in a borrower's business activity;
- major negative changes in balance sheet structure and ratios between balance sheet items or large drop in the value of a borrower's premises and equipment;
- threatened or actual enforcement against any property pledged to the Bank as a security for due payments under a loan agreement, initiated by any other lienor;
- threatened or actual damage or injury to the property pledged to the Bank as a security for due payments under a loan agreement, including its deterioration, misuse, decrease in value by more than physical depreciation, actual, partial or full lack of the pledged property;
- breach of a loan agreement conditions by a borrower; and



- other similar factors at the discretion of the initiating officer.

By using the internal grading system (taking into account NBU requirements and actual performance) the Bank ensures that its loans, according to IFRS, cannot perform worse than allowed for by NBU classification.

Provisioning Policy for Statutory Reporting Purposes

The First Level Credit Committee and BCCs set the amounts of provisions for potential losses on loans and advances to customers. In accordance with existing NBU regulations, the Bank creates provisions based on the following three risk evaluation factors:

- the borrower’s financial status and creditworthiness;
- loan servicing; and
- loan security.

A borrower’s financial status and creditworthiness is based on a five-level credit rating system (from A to E in descending order). Loan servicing is rated on the basis of compliance with the schedule of repayment of principal and payment of interest. According to the NBU regulations, a loan is regarded as poorly-serviced if the delay in the repayment of principal or any interest payment is over seven calendar days. The credit ranking matrix currently in use is based on lowering the credit rating as the borrower descends to a lower class or if the debt servicing index worsens.

Loan security assessment is based on the pledged property evaluation system used in the Bank. Depending on the kind of pledged property and debt classification, the cost of pledged property is discounted at the established rate.

Risk Categories of Credit Operations

The table below sets forth the risk classification of credit operations relating to the Bank’s provisioning policies in terms of risk categories prescribed by the NBU:

Class of Borrower in terms of financial condition	Debt servicing		
	Good⁽¹⁾	Poor⁽²⁾	Unsatisfactory⁽³⁾
A (the best)	Standard	Watch	Substandard
B	Watch	Substandard	Substandard
C	Substandard	Substandard	Doubtful
D	Doubtful	Doubtful	Bad
E (the worst)	Doubtful	Bad	Bad



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- (1) If principal and interest payments are made when due or are overdue by 7 days or less; or a loan has been prolonged (without the borrower's downgrading) for less than 90 days and interest payments are overdue by 7 days or less.
- (2) If principal payments are overdue by more than 7 days but less than 90 days and interest payments under such loan are paid when due or are overdue by less than 30 days; or a loan has been prolonged (with the borrower's downgrading) for more than 90 days but less than 180 days and interest payments under such loan are overdue by not more than 30 days.
- (3) If principal payments are overdue by more than 90 days; or the loan has been prolonged (with the borrower's downgrading) for more than 180 days.

The following table sets out NBU requirements on the percentage of the value of collateral used when calculating necessary loan loss provision(s) depending on the security category and the classification of the secured loan prescribed by the NBU:

Lending operation classification	Titles to money deposits and registered deposit certificates issued by the creditor bank, title to money deposits for interbank operations		Banking metals	Government securities	Non-government securities	Residential real estate UAH credits	Residential real estate foreign currency credits	Other real estate	Property rights for future residential real estate (used for calculations during 2 years from the credit date)	Movable property and precious metals	Other property rights
	The same currency as the credit/freely convertible currency	Currency different from that of the credit									
Standard	100%	90%	80%	100%	40%	70%	50%	50%	50%	50%	30%
Watch	100%	90%	80%	80%	20%	70%	50%	50%	40%	40%	20%
Substandard	100%	90%	60%	50%	10%	40%	40%	40%	20%	20%	10%
Doubtful	100%	90%	20%	20%	0%	20%	20%	20%	10%	10%	5%
Bad	0%	0%	0%	0%	0%	0%	0%	0%	0%	0%	0%

Based on the risk category of the credit operation and the valuation of the collateral performed as outlined in the previous two tables, the Bank calculates the amount of net risk subject to provisioning according to the rates specified in the table below:

Risk Category of the credit operation	Provisioning rate for foreign currency credit operation			Provisioning rate for uniform consumer loans ⁽¹⁾
	Provisioning rate for UAH credit operation	If borrower has proceeds in the respective foreign currency	If borrower has no proceeds in the respective foreign currency	
Standard	1 %	2 %	2 %	2 %
Watch	5 %	7 %	10 %	10 %
Substandard	20 %	25 %	40 %	40 %
Doubtful	50 %	60 %	80 %	80 %
Bad	100 %	100 %	100 %	100 %

(1) Uniform consumer loans are loans extended for consumer needs to an individual borrower as a single loan or a series of loans not exceeding UAH 20,000 in aggregate.

The Bank's internal credit rating system is based upon the existing NBU requirements. The Bank has also established an internal credit rating system for assessing each loan, which is



based on its expert assessment of the expected level of losses that the Bank may incur based on its evaluation of risks and its historical loss experience. The Bank’s internal credit risk rating system forms the basis of the calculation of the provision for loan impairment.

The following table sets out information on the percentage of the value of unconditional guarantees used when calculating necessary loan loss provision(s), depending on the type of guarantor:

Lending operation classification	Cabinet of ministers of Ukraine	Government of category “A” country	International mutual banks	Banks with credit rating of at least investment grade, collateralised guarantees by Ukrainian banks
Standard	100%	100%	100%	100%
Watch	100%	100%	100%	100%
Substandard	50%	100%	100%	100%
Doubtful	20%	20%	20%	20%
Bad	0%	0%	0%	0%

Assessment of Provision for Loan Impairment for IFRS Reporting Purposes

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

A loan impairment estimation exercise follows certain steps and procedures, as described below:

1. Identification of loans that are individually significant, i.e. those loans which if fully impaired would have a material impact on the expected average level of operating profit of the Bank.
2. Determination of whether an individually significant loan shows objective evidence of impairment or not. Special emphasis is placed on the timing of the contractual cash flows from interest payments and principal repayments. If the Bank expects to collect all interest and principal due in full, but it is probable that those cash flows will be received later than the date agreed in the original contract, an impairment calculation is performed. Other impairment indicators include but are not limited to: any significant financial difficulty of the borrower; an actual breach of the loan contract; a high probability of bankruptcy or other financial reorganisation of the borrower, recognition of an impairment loss on that asset in a prior financial reporting period; or a historical pattern of collections of loans that indicates that the entire principal and interest amount of a loan portfolio will not be collected.
3. Review for impairment of individually significant loans that show objective evidence of impairment. An impairment review requires an estimate of the expected amounts of cash flows from interest and principal repayments and other cash flows, including amounts



recoverable from guarantees and collateral, and discounting them at the loan's original effective interest rate.

In cases where the Bank's management feel unable to make a reliable evaluation of an expected cash flow, an expert evaluation is used. The loan is impaired if its carrying amount exceeds the estimated recoverable amount as defined above. A separate impairment loss on an impaired individually significant loan is recorded.

4. All remaining loans that have not been identified as individually significant should be assessed on a portfolio basis if there are signs that impairment is present in those portfolios. For the purpose of such a review, the portfolio of loans should be grouped in pools, based on similar credit risks characteristics. Such pools should be further assessed for impairment as if they were a single asset. An expert evaluation is used in regard to such pools, as the Ukrainian market does not contain adequate statistics for loss probability.

The Bank monitors the quality of its loan portfolio and reviews its risk assessment results on a monthly basis. Such assessments are performed for each of the Bank's loans. The existence of an impairment loss for a loan is based on the credit risk assigned to an individual borrower or group of similar borrowers and the relevant historical loss experience. The Bank also analyses any risk mitigating factors, such as guarantees received and the fair value and quality of collateral.

The Bank's provision for loan impairment on its loan portfolio was UAH 159,495 thousand as at 31 December 2007. The provision for loan impairment on the Bank's loan portfolio as at 31 December 2006 and 2005 was UAH 127,843 thousand and UAH 121,844 thousand respectively, an increase of 4.9 per cent, corresponding with growth of the Bank's net loan portfolio of 96.6 per cent. for the year ended 31 December 2006.

Problem Loan Recovery

The Bank has internal procedures relating to problem loan recovery developed on the basis of requirements of Ukrainian legislation and detailed in a series of internal regulations of the Bank.

These internal regulations contain a set of procedures, intended to enable the Bank to obtain repayment on non-performing loans ("NPLs"). The Bank has established the Problem Loans Department ("PLD") which is a specific unit within the Bank's Lending Division responsible for taking any necessary economic and legal measures in respect of defaulting borrowers (or borrowers whose default can reasonably be expected) to ensure repayment of NPLs or probable NPLs. The PLD is authorised to engage representatives of any of the Bank's units and divisions (including those of branches) in order to efficiently perform its functions. The PLD is based in, and managed from, the Bank's head office in Odessa. Upon submission of information to the Head of the Lending Division and the Head of the Management Board by the relevant unit or division of the Bank engaged in credit transactions with the client, loans will be reviewed and, if appropriate, designated as NPLs according to the following rating. If the Lending Division fails to settle conflict with the borrower on mutual basis the PLD is engaged. Upon referral of a problem loan to the PLD, the latter carries out a comprehensive economic and legal analysis of the problem



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indebtedness and contacts the Security Division and Collateral Monitoring Department to determine possible sources of debt recovery. A plan of action with different scenarios is developed by PLD and submitted to Head of Management Board for consideration and approval or further consideration by the First Level Credit Committee.

After the action plan being approved, the units and divisions of the Bank mentioned in the plan (including Legal Division and Security Division or respective units of the branches) take any steps necessary to remedy or prevent the borrower defaulting, as the case may be.

The main actions which may be taken by the PLD for debt collection include contractual set-off of funds held by the Bank, initiating and handling enforcement proceedings and taking measures to sell property of the debtor and/or the guarantor, initiating bankruptcy proceedings, communicating with debtors and/or guarantors to identify additional property, receivables and other resources which can be used for the debt repayment and cooperating with law enforcement agencies and other governmental authorities aimed at efficient satisfaction of the Bank's claims under problem loans.

The PLD also holds discussions with the borrower over a problem loan either simultaneously or prior to initiating any legal proceedings against the borrower. Negotiations are usually aimed at debt restructuring and include obtaining additional security, guarantees by shareholders, increased interest rates and revised repayment schedules, all subject to approval by the First Level Credit Committee.

If enforcement action on overdue debt collection against a borrower or its guarantors or enforcement of collateral have not resulted in repayment, and it is confirmed that the borrower has no financial means or property to settle the debt and there are grounds to consider such debt as a bad debt, the First Level Credit Committee and Management Board make the decision to write such debt off against the Bank's provision for impairment. The procedure for writing off bad debts is regulated by the NBU and internal procedures of the Bank.

Non Performing Loans

As at 31 December 2007, the Bank had UAH 8,993 thousand of NPLs and the average percentage of the Bank's loans that have been classified as NPLs was approximately 0.13 per cent. For the year ended 31 December 2005, UAH 16,315 thousand of loans were declared by the Bank as NPL. For the year ended 31 December 2006, UAH 6,869 thousand of loans were declared as NPLs.



5. SELECTED STATISTICAL DATA AND OTHER INFORMATION

5.1. Average Balance Sheet and Interest Rate Data

The tables below present the simple average balances for interest-earning assets (after provision for impairment) and interest-bearing liabilities together with the related income and expense amounts, resulting in the presentation of the average yields and rates for the three month period ended 31 December 2007 and the years ended 31 December 2006 and 2005. Average balances are based on the Bank's balances as at the beginning and at the end of the respective reporting periods.

	Year ended 31 December 2007 (unaudited)			Year ended 31 December 2006			Year ended 31 December 2005		
	Average Balance	Interest	Average Yield	Average Balance	Interest	Average Yield	Average Balance	Interest	Average Yield
	UAH thousands		% annualised	UAH thousands		% annualised	UAH thousands		% annualised
Assets									
Interest-earning assets									
Due from other banks(1)	302,125	23,722	7.9	145,286	3,053	2.1	72,637	3,985	5.5
Loans and advances to customers	5,051,154	640,938	12.7	2,436,472	358,030	14.7	1,419,403	230,931	16.3
Securities(2)	131,520	10,785	8.2	106,813	7,494	7.0	53,160	2,867	5.4
Total average interest-earning assets	5,484,799	675,445	12.3	2,688,570	368,577	13.7	1,545,199	237,783	15.4
Non-interest-earning assets									
Cash and cash equivalents and balances with the Central Banks	254,195	N/A	N/A	299 329	N/A	N/A	215,783	N/A	N/A
Guarantee deposits with the National Bank of Ukraine	275,869	N/A	N/A	—	N/A	N/A	14,869	N/A	N/A
Current income tax prepayment	3,211	N/A	N/A	627	N/A	N/A	—	N/A	N/A
Other assets	31,600	N/A	N/A	14,234	N/A	N/A	4,453	N/A	N/A
Premises and equipment	483,154	N/A	N/A	299,489	N/A	N/A	109,251	N/A	N/A
Intangible assets	3,422	N/A	N/A	2,070	N/A	N/A	1,298	N/A	N/A
Deferred tax asset	—	N/A	N/A	—	N/A	N/A	1,281	N/A	N/A
Total average non-interest-earning assets	1,051,450	N/A	N/A	615,748	N/A	N/A	346,934	N/A	N/A
Total average assets	6,536,250	N/A	N/A	3,304,318	N/A	N/A	1,892,133	N/A	N/A

Note:

(1) Due from other banks includes correspondent accounts and overnight placements with other banks and balances due from other banks.

(2) Securities include trading securities, other securities at fair value through profit or loss and investment



securities available-for-sale.

Liabilities and equity

	Three months ended 31 December 2007 (unaudited)			Year ended 31 December 2006			Year ended 31 December 2005		
	Average Balance	Interest	Average Yield	Average Balance	Interest	Average Yield	Average Balance	Interest	Average Yield
	UAH thousands		% annualised	UAH thousands		% annualised	UAH thousands		% annualised
Interest-bearing liabilities									
Due to banks ⁽¹⁾	730,330	60,596	8.3	328,533	34,812	10,6	316,420	17,158	5,4
Customer accounts	4,628,003	288,475	6.2	2,444,778	148,770	6,1	1,330,703	117,810	8,9
Debt securities in issue	149,971	15,866	10.6	95,225	3,007	3,2	25,371	1,732	6,8
Other borrowed funds	7,859	1,063	13.5	7,859	108	1,4	—	N/A	N/A
Loan participation notes	261,266	23,558	9.0	-	N/A	N/A	-	N/A	N/A
Subordinated debt	4,054	258	6.4	7,927	789	10,0	3,874	631	16,3
Total average interest-bearing liabilities	5,781,482	389,817	6.7	2,884,321	187,486	6,5	1,676,367	137,331	8,2
Non-interest-bearing liabilities and equity									
Current income tax liability	—	N/A	N/A	274	N/A	N/A	452	N/A	N/A
Provisions for liabilities and charges other liabilities	35,560	N/A	N/A	14,073	N/A	N/A	6,753	N/A	N/A
Deferred tax liability	33,212	N/A	N/A	16,117	N/A	N/A	3,195	N/A	N/A
Total equity	685,997	N/A	N/A	389,534	N/A	N/A	205,367	N/A	N/A
Total average non-interest-bearing liabilities and equity	754,769	N/A	N/A	419,997	N/A	N/A	215,766	N/A	N/A
Total average liabilities and equity	6,536,250	N/A	N/A	3,304,318	N/A	N/A	1,892,133	N/A	N/A

(1) Due to banks include balances due to the National Bank of Ukraine and due to other banks.



5.2. Bank Performance Ratios

	Year ended 31 December 2007 (unaudited) %	Year ended 31 December 2006 %	Year ended 31 December 2005 %
Net interest margin ⁽¹⁾	5.2	6.7	6.5
Net non-interest income to income before operating expenses ⁽²⁾	33.6	36.6	44.3
Cost to income ratio ⁽³⁾	62.3	65.5	73.7
Return on average assets ⁽⁴⁾	1.6	2.2	1.5
Return of average equity ⁽⁵⁾	15.6	18.5	14
Balance sheet ratios			
Customer loans to customer accounts ⁽⁶⁾	115.2	98.2	102.7
Customer loans to total assets ⁽⁷⁾	79.3	73.2	74.7
Equity to total assets ⁽⁸⁾	9.7	12	11.4
Capital adequacy ratio ⁽⁹⁾	12.9	13.7	13.7
NBU total capital adequacy ratio ⁽¹⁰⁾	11.1	11.9	11.5
Asset quality ratios			
Provision for impairment of loan portfolio to total loans to customers ⁽¹¹⁾	2.3	3.8	6.9
Provision charge to total customer loans ⁽¹²⁾	0.7	0.5	1.2

(1) The net interest margin was calculated as net interest income before impairment of interest earning assets divided by the simple average of interest earning assets after provision for impairment as at the beginning and the end of the period (i.e. due from other banks, loans to customers and securities). Ratios were annualised, where necessary.

(2) The ratio of net non-interest income to income before operating expenses was calculated as net non-interest income (operating profit, excluding net interest income before administrative and operating expenses) divided by operating profit before operating expenses.

(3) The cost to income ratio was calculated as administrative and operating expenses divided by operating profit before administrative and operating expenses.

(4) The return on average assets was calculated as net profit for the period divided by the simple average of total assets at the beginning and the end of the period. Ratios were annualised, where necessary.

(5) The return on average equity was calculated as net profit for the period divided by the simple average of total equity at the beginning and the end of the period. Ratios were annualised, where necessary.

(6) The ratio of loans to customers to customer accounts was calculated as loans to customers after provision for impairment as at the end of the period divided by customer accounts at the end of the period.

(7) The ratio of loans to customers to total assets was calculated as loans to customers after provision for impairment as at the end of the period divided by total assets as at the end of the period.

(8) The ratio of equity to total assets was calculated as total equity as at the end of the period divided by total assets as at the end of the period.

(9) The capital adequacy was calculated based on the requirements and methodology defined in the 1988 Basel Accord.

(10) The capital adequacy was calculated based on the requirements and methodology defined by the National Bank of Ukraine.

(11) The ratio of provision for impairment of loan portfolio to total loans to customers was calculated as provision for impairment of total loans to customers as at the end of the period divided by total loans to customers before provision for impairment as at the end of the period.

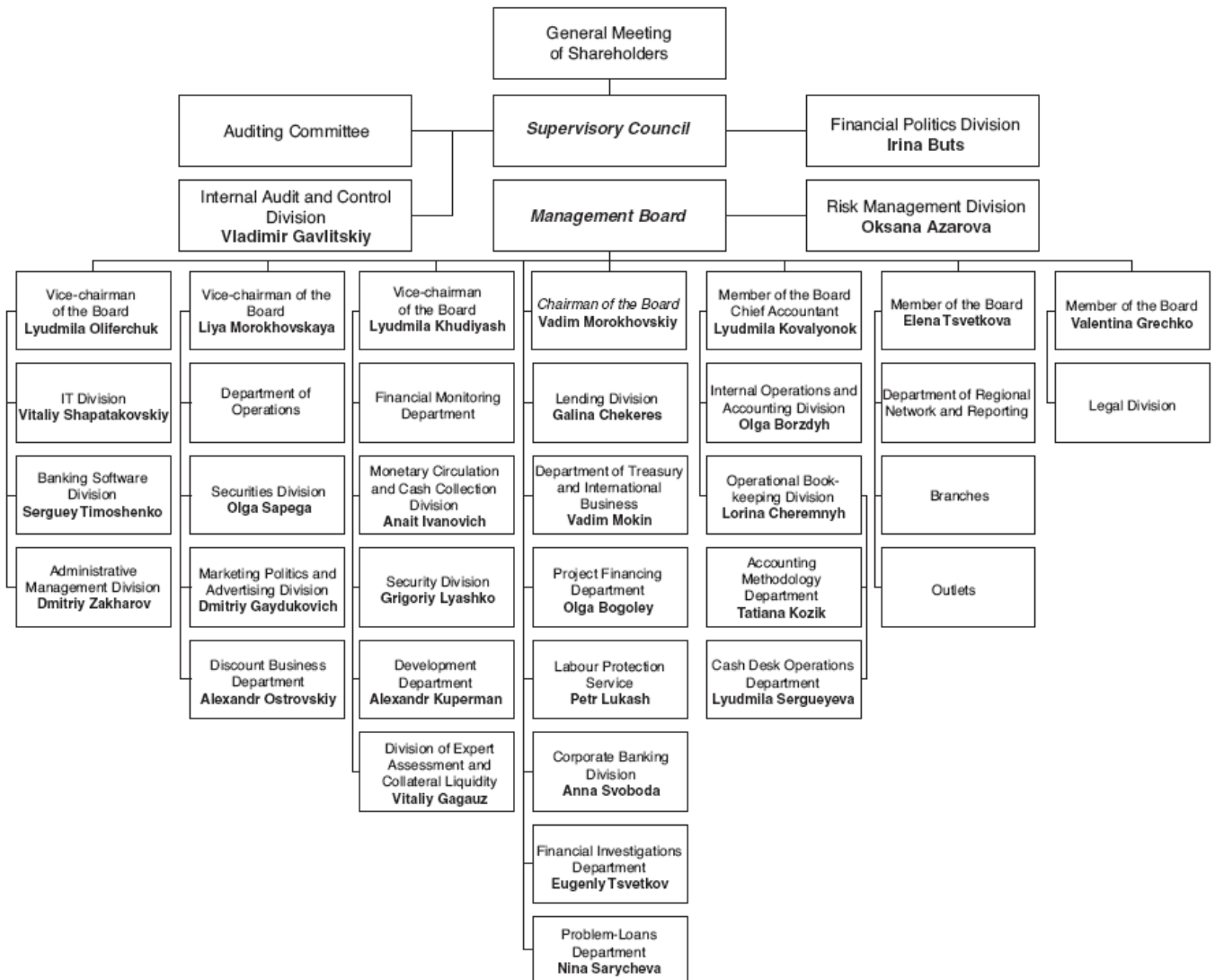
(12) The ratio of provision charge to total loans to customers was calculated as impairment charge for total loans to customers for the period divided by total loans to customers before provision for impairment as at the end of the period. Ratios were annualised, where necessary.



6. MANAGEMENT

The current charter of the Bank was approved by the General Meeting of Shareholders on 23 October 2006 and was registered by the NBU on 20 December 2006. In accordance with the Bank's charter, the management bodies of the Bank are the General Meeting of Shareholders, Supervisory Council and Management Board. The supervisory bodies of the Bank are the Auditing Committee and Internal Audit and Control Division.

The following diagram sets out the organisational structure and reporting lines of the Bank:





6.1. General Meeting of Shareholders

The General Meeting of Shareholders is the supreme governing body of the Bank. The authority of the General Meeting of Shareholders includes, amongst others, the following:

- determining the main areas of operations for the Bank and approving reports on implementation thereof;
- approving the Bank's charter and amendments thereto;
- approving changes to the share capital of the Bank;
- appointing and dismissing the Chairman and the members of the Supervisory Council and the Auditing Committee;
- approving annual results of the Bank's activities (including any subsidiaries), the procedure for profit distribution, terms and procedure for payment of dividends;
- approving reports and conclusions made by the Audit Committee and external auditors; and
- terminating the business activity of the Bank (by way of reorganisation or liquidation of the Bank).

The powers listed above lie within the exclusive scope of authority of the General Meeting of Shareholders and may not be delegated to the other governing bodies of the Bank. Being the supreme body of the Bank, the General Meeting of Shareholders is also authorised to make any other decisions concerning the Bank's activity. The General Meeting of Shareholders may decide to delegate certain functions, other than those listed above, to the Supervisory Council or the Management Board of the Bank.

Decisions to (i) approve amendments to the Bank's charter and (ii) terminate the Bank's business activity require a qualified majority of 75 per cent. of voting shares. Other matters are decided by a simple majority vote.

6.2. Supervisory Council

The Supervisory Council is not directly involved in the day-to-day management of the Bank but plays a significant role in overseeing and monitoring the business activities of the Bank. The Supervisory Council represents the interests of the Bank's shareholders between the General Meetings of Shareholders and exercises control over the activities of the Management Board. The Supervisory Council consists of four members who are elected by the General Meeting of Shareholders from among the Bank's shareholders (in the case of individuals) or their representatives (in case of legal entities). The Supervisory Council meets to the extent necessary and at least every three months. Extraordinary meetings of the Supervisory Council may be convened by the Chairman of the Supervisory Council, one-third of the members of the Supervisory Council, or the Management Board. The Supervisory Council is accountable to the General Meeting of Shareholders.



The responsibilities of the Supervisory Council include, among others, the following:

- appointing and dismissing the Chairman and members of the Management Board;
- determining the terms and conditions of remuneration for the Chairman and members of the Management Board;
- exercising control over the activities of the Management Board;
- approving how to cover the Bank's losses;
- appointing the Bank's external auditor;
- establishing, re-organising and liquidating subsidiaries, branches and representative offices of the Bank, and approving their charters and regulations; and
- approving wages and bonuses of the members of Management Board.

The name, position, qualifications and other information relating to each member of the Supervisory Council are set out below:

Name	Age	Position in the Supervisory Council
Mr. Yuriy Rodin	57	Chairman of the Supervisory Council
Mr. Mark Bekker	62	Vice-Chairman of the Supervisory Council
Mr. Vitaliy Oplachko	69	Member of the Supervisory Council
Mrs. Alla Vanetsyants	29	Member of the Supervisory Council

Mr. Yuriy Rodin – General Director of the enterprise “Tekom” Ltd., major shareholder of the Bank

Mr. Mark Bekker – General Director of German-Ukrainian Joint Company “Vivien” GMBH LTD, major shareholder of the Bank

Mr. Vitaliy Oplachko – General Director of the Odessa Maritime Agency “Interbroker” LTD, minority shareholder of the Bank

Mrs. Alla Vanetsyants – Deputy-Head of Financial Politics Division of the Bank, major shareholder of the Bank

6.3. Management Board

The Management Board (the “Board”) is an executive body of the Bank and is responsible for the day-to-day management of the Bank. The Board is accountable to the General Meeting of Shareholders and to the Supervisory Council of the Bank. The number of the Board's members is determined by the Supervisory Council and may not be fewer than six persons. The Supervisory Council also appoints the members of the Board for a term of five years. Meetings of the Board are held at least once a month.



The powers of the Board include the following:

- managing day-to-day activity of the Bank, ensuring the implementation of decisions of the Supervisory Council and the General Meeting of Shareholders;
- carrying out preliminary consideration of the documents which should be further submitted for approval by the General Meeting of Shareholders and the Supervisory Council;
- determining the Bank's risk management policy and reporting to the Supervisory Council on the implementation thereof;
- establishing standing committees, including the Credit Committees and the Asset and Liability Management Committee, and approving regulations on standing committees;
- establishing and regulating interest rates on the operations of the Bank;
- determining the form and system of the remuneration of the Bank's employees;
- establishing the Bank's outlets, approving the regulations for such outlets and amendments thereto;
- approving the terms of issuance and redemption of the Bank's bonds and deposit certificates, as well as other investment matters; and
- establishing limits on debit operations of the Bank's branches.

The Chairman of the Board manages the work of the Board and is entitled, within the scope of his authority, to represent the Bank in relations with state authorities, legal entities and individuals, to enter into and sign agreements on behalf of the Bank, to issue powers of attorney on behalf of the Bank and to dispose of the Bank's assets and use the Bank's funds in accordance with the applicable legislation.

The name, position and certain other information relating to each member of the Management Board are set out below:

Name	Age	Position in the Management Board
Mr. Vadim Morokhovskiy	36	Chairman of the Management Board
Mrs. Lyudmila Khudiyash	46	Vice-Chairman of the Management Board
Mrs. Lyudmila Oliferchuk	53	Vice-Chairman of the Management Board
Mrs. Liya Morokhovskaya	32	Member of the Management Board
Mrs. Lyudmila Kovalyonok	40	Member of the Management Board (Chief Accountant)
Mrs. Valentina Grechko	50	Member of the Management Board (Head of Legal Division)
Mrs. Elena Tsvetkova	43	Member of the Management Board (Director for Regional Network and Reporting)
Mr. Vadim Mokin	41	Member of the Management Board (Director for Treasury and International Business)
Ms. Galina Chekeres	41	Member of the Management Board (Head of Lending Division)
Mrs. Anna Svoboda	37	Member of the Management Board (Head of Corporate Customers servicing Division)



Mr. Vadim Morokhovskiy has served as Chairman of the Board since 1999. Mr. Morokhovskiy has a total of 14 years of banking experience, of which 12 years have been with the Bank. Mr. Morokhovskiy is also a member of the Supervisory Council and Credit Committee of the Regional Investment Bank (Latvia). He holds a Master's Degree in banking from Odessa Institute of National Economy.

Mrs. Lyudmila Khudiyash has served as Vice-Chairman of the Board since 1999. Mrs. Khudiyash has 24 years of banking experience, of which eight years have been with the Bank. She graduated from Odessa Institute of National Economy with a Master's Degree in banking.

Mrs. Lyudmila Oliferchuk has served as Vice-Chairman of the Board since 1993. Mrs. Oliferchuk has 28 years of banking experience, of which 14 years have been with the Bank. She holds a Master's Degree in banking from Odessa Institute of National Economy.

Mrs. Liya Morokhovskaya has served as Vice-Chairman of the Board since 2002. Mrs. Morokhovskaya has a total of 11 years of banking experience, all with the Bank. She graduated from Odessa State Economic University with a Master's Degree in banking.

Mrs. Lyudmila Kovalyonok has served as member of the Board since 1999. Mrs. Kovalyonok has 17 years of experience in banking, of which nine years have been with the Bank. She graduated from Odessa Institute of National Economy with a Master's Degree in banking.

Mrs. Valentina Grechko has served as member of the Board since 1995. Mrs. Grechko has 32 years of banking experience, of which 12 years have been with the Bank. She holds a Master's Degree in law from Odessa State University.

Mrs. Elena Tsvetkova has served as member of the Board since 2002. Mrs. Tsvetkova has 16 years of banking experience, of which nine years have been with the Bank. She graduated from Odessa Institute of National Economy with a Master's Degree in finance.

Mr. Vadim Mokin has served as member of the Board since 2007. Mr. Mokin has 15 years of banking experience, of which eleven years have been with the Bank. He graduated from National Centre for training of banking specialists of Ukraine with a Master's Degree in banking.

Ms. Galina Chekeres has served as member of the Board since 2007. Ms. Chekeres has 21 year of banking experience, of which 12 years have been with the Bank. She holds a Master's Degree in accounting and analysis from Odessa Institute of National Economy.

Mrs. Anna Svoboda has served as member of the Board since 2007. Mrs. Svoboda has 12 years of banking experience, which have been with the Bank. She holds a Master's Degree in finance from Odessa Institute of National Economy.

The business address of the members of the Management Board is 6/1, Krasnova Street, Odessa 65059, Ukraine.



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Members of the Management Board receive bonuses payable quarterly and bonuses are payable annually to managerial staff depending on the overall annual performance of the Bank. Pension plans are subject to current Ukrainian legislation and are provided on the same terms as the plans made available to the other staff at the Bank. Share incentive plans are not available.

Conflict of Interest

The members of the Management Board of the Bank do not have any conflicts, or any potential conflicts, between their duties to the Bank and their private interests or other duties.



7. EMPLOYEES AND RELATED PARTY TRANSACTIONS

As at 31 December 2007, the Bank had 2,206 employees, including 1,112 employees working in the head office in Odessa as compared to 1,828 employees (head office: 956) at 31 December 2006 and 1,548 employees (head office: 841) at 31 December 2005. The employees are not party to collective bargaining agreements.

Employees are trained at branches and smaller outlets. The Bank is focused on providing standardised training to its staff in order to provide excellent customer service throughout its entire distribution network. The Bank requires that its employees have appropriate qualifications and substantial knowledge of the banking industry. In order to recruit qualified and experienced employees and to increase employee retention, the Bank is establishing a number of programmes with leading Ukrainian educational institutions and provides a competitive salary package which is also in compliance with Ukrainian legislation. The Bank also engages external training providers to provide training to its personnel. The Bank utilises the National Centre of Bank Employees Training of Ukraine, various private training companies and consulting companies. In 2004, the Bank established its own training centre.

The Bank spent approximately UAH 331,154 on employee recruitment and external training for the year ended 2007, as compared to UAH 125,000 for the year ended 31 December 2006. Salaries are paid to the Bank's employees in accordance with Ukrainian employment legislation and the regulation on employees' remuneration.

In addition, the Bank has an incentives programme for employees which provides for personal bonuses (or "premiums") (payable quarterly to non-managerial staff depending on their individual performance) and bonuses (payable quarterly and annually to managerial staff depending on the overall annual performance of the Bank). The Bank launched a medical insurance scheme in 2006 to cover all its personnel following evaluation of the management scheme. In addition, a life insurance scheme was implemented for all employees who have worked at the Bank one year.

As with other Ukrainian banks, the Bank faces certain difficulties in attracting qualified management personnel in regions other than Kiev. The Bank seeks to mitigate against this lack of qualified personnel by offering competitive remuneration packages and by focusing on training and employee development.

The Bank has developed a staff loan programme as part of its motivation programme. The programme includes the provision of secured mortgage loans, car purchase loans, consumer loans and overdrafts, depending on the employee's position and length of service within the Bank.

As of 31 December 2007, no material disputes have occurred between the Bank and the employees.



7.1. Related Party Transactions

As at 31 December 2007, the amount of loans outstanding to related parties was UAH 124,287 thousand, or 1.8 per cent. of the Bank's gross loan portfolio. As at 31 December 2007, UAH 297,241 thousand, or 5.0 per cent. of the Bank's deposits were due to related parties of the Bank. The Bank has an internal limit for related parties' exposures of 30 per cent. of equity (which equated to approximately UAH 253,278 at 31 December 2007).

It is the Bank's policy that transactions with related parties are priced predominantly at market rates and are subject to the same approval procedures and limits as are applied by the Bank to transactions with unrelated parties. The Bank has concluded insurance contracts with CJSC Insurance Company "Tekom", a related party company, with respect to the premises and motor vehicles owned by the Bank. The agreements were concluded at arm's length and at standard market rates.

In the normal course of its business, the Bank enters into transactions with its direct and indirect significant shareholders and companies with which the Bank has direct and indirect significant shareholders in common. These transactions include loans, deposits, trade finance and foreign currency transactions. The outstanding balances as at 31 December 2007 and 31 December 2006 and income and expenses for the year ended 31 December 2007 and 31 December 2006 respectively are as follows:

As at 31 December 2007 (unaudited)

	Ultimate shareholders	Other shareholders	Entities under control of ultimate shareholders	Other related parties
		(in thousands of Ukrainian Hryvnias)		
Assets				
Gross amount of loans and advances to customers (contractual interest rate: 5 – 16%)	59	12,215	110,505	1,508
Impairment provisions for loans and advances to customers at 31 December 2007	(1)	(244)	(2,210)	(30)
Investment securities available-for-sale				
– Shares of OJSC "Pharmacia" (8% of holding)	—	—	12,216	—
- Shares of OJSC "Kholodmash" (9,55% holding)	--	--	631	--
– Shares of JSC "Kotovskoe ZPP" (10% of holding)	—	—	865	—
Prepayment for premises	—	7,357	—	—
Other assets	—	14,791	—	—
Liabilities				
Customer accounts (contractual interest rate: 4 – 19%)	50,959	105,414	140,699	169
Credit related commitments				
Guarantees issued by the Group at the period end	—	—	3,882	—
Import letters of credit at the year	--	--	1,580	--



end

The income and expense items with related parties for the year ended 31 December 2007 were as follows:

	Ultimate shareholders	Other shareholders	Entities under control of ultimate shareholders	Other related parties
Interest income	258	1,299	13,037	131
Interest expense	(7,289)	(5,803)	(2,494)	(410)
Reversal of/(provision for) loan impairment	219	121	(963)	58
Gains less losses from trading in foreign currencies	—	--	109	—
Fee and commission income	—	52	569	2
Impairment of investment securities available for sale	--	--	1,694	--
Other operating income	--	328	19	-
Administrative and other operating expenses	(10,849)	(12,927)	(10,056)	(224)

As at 31 December 2006

	Ultimate shareholders	Other shareholders (in thousands of Ukrainian Hryvnias)	Entities under control of ultimate shareholders	Other related parties
Assets				
Gross amount of loans and advances to customers (contractual interest rate: 5 – 16%)	10,985	18,236	62,371	4,384
Impairment provisions for loans and advances to customers at 31 December 2006	(220)	(365)	(1,247)	(88)
Investment securities available-for-sale (contractual interest rate: 15%)	—	—	6,707	—
Prepayment for premises	11,989	—	—	—
Other assets	—	—	16,181	—
Liabilities				
Customer accounts (contractual interest rate: 2 – 19%)	166,541	195,991	79,914	9,610
Credit related commitments				
Guarantees issued by the Group at the year end	—	—	536	—



The income and expense items with related parties for the year ended 31 December 2006 were as follows:

	Ultimate shareholders	Other shareholders	Entities under control of ultimate shareholders	Associates	Other related parties
	(in thousands of Ukrainian Hryvnias)				
Interest income	596	24	10,916	52	84
Interest expense	(3,202)	(2,968)	(394)	(508)	(1,239)
Reversal of/(provision for) loan impairment	(214)	(120)	7,966	--	100
Gains less losses from trading securities	--	--	453	--	--
Gains less losses from trading in foreign currencies	—	--	85	4	—
Fee and commission income	—	--	258	63	—
Administrative and other operating expenses	—	(1,101)	(2,412)	(74)	(4,943)
Excess of interest in the associate's net assets acquired over cost of investment	5,409	--	--	--	--
Share of profit of associates	--	--	--	2,478	--

Aggregate amounts lent to and repaid by related parties during the year ended 31 December 2007 (unaudited) were:

	Ultimate shareholders	Other shareholders	Entities under control of ultimate shareholders	Other related parties
	(in thousands of Ukrainian Hryvnias)			
Amounts lent to related parties during the period	238	1,102	175,028	1,694
Amounts repaid by related parties during the period	11,163	7,123	152,595	1,134

Aggregate amounts lent to and repaid by related parties during the year ended 31 December 2006 were:

	Ultimate shareholders	Other shareholders	Entities under control of ultimate shareholders	Other related parties
	(in thousands of Ukrainian Hryvnias)			
Amounts lent to related parties during the period	11,237	6,087	119,427	4,966
Amounts repaid by related parties during the period	583	7	114,257	1,914



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Key management compensation is presented below:

	Year ended 31 December 2007 (unaudited)		Year ended 31 December 2006	
	Expense	Accrued liability	Expense	Accrued liability
Short-term benefits:				
– Salaries	5,398	164	4,741	229
- Short-term bonuses	910	143	--	--
Post-employment benefits:				
– State pension and social security costs	403	36	202	11
Total	6,712	180	4,943	240



8. SHARE CAPITAL AND PRINCIPAL SHAREHOLDERS

8.1. Increasing Share Capital

According to Ukrainian legislation, a bank may increase its share capital through additional cash subscriptions, upon all previously issued and subscribed shares having been paid in full by their holders. The general meeting of shareholders of a bank has the exclusive power to make decisions to increase a bank's share capital. This includes announcements of the subscription for new share capital setting out the main terms of an issuance, and upon completion of the subscription, decisions on making appropriate amendments to such bank's charter. Decisions on amendments to the charter (including the registration of increased share capital) are subject to registration by the NBU prior to becoming effective. The additional share issuance is to be registered with the SSMSC.

Any shareholder of a bank shall have a pre-emptive right to buy any additional shares to be issued by such bank. If, as a result of the acquisition of additional shares in a bank, a shareholder's aggregate direct and indirect holdings would increase over one or more thresholds at 10, 25, 50 or 75 per cent. of the Bank's total share capital, such shareholder must obtain prior written consent of the NBU for such acquisition.

8.2. Dividends

According to the provisions of the Bank's governing charter and Ukrainian law, dividends may be distributed and paid once a year from the Bank's statutory retained earnings, subject to the decision of the General Meeting of Shareholders.

The Bank's policy is to capitalise its profit and to refrain from declaring dividends. All the profits from the Bank's business have been retained by the Bank.

In April 2006, the shareholders decided to capitalise dividends in the amount of UAH 23,500 thousand (2005: UAH 16,498 thousand).

8.3. Principal Shareholders

As at 31 December 2007, the Bank's authorised, issued and fully paid but not registered share capital was UAH 555,000,000 (nominal amount) comprising of 555,000,000 ordinary shares with a nominal value of UAH 1 each and ranked equally. Each share carries one vote.



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The following table sets out the Bank's share capital structure as at 31 December 2007:

UAH	Nominal value of shares held	Number of shares held	% of total shares
CJSC Insurance company "Tekom"	43,982,988	43,982,988	7.9249%
"Tekom" Ltd	42,592,907	42,592,907	7.6744%
Investment fund "Strategichni investitsii"	28,000,000	28,000,000	5.0450%
"Techno-Inform" LTD	26,923,959	26,923,959	4.8512%
Ukrainian/German Joint Company "Vivien GMBH" LTD.	20,147,907	20,147,907	3.6303%
CJSC Insurance company "Tekom-Zhittya"	8,820,163	8,820,163	1.5892%
OJSC "Vtormet"	467,182	467,182	0.0842%
Odessa Maritime Agency "Interbroker" LTD	369,188	369,188	0.0665%
Production-commercial firm "Kometeks" LTD	140,124	140,124	0.0252%
"Mial" firm LTD	93,623	93,626	0.0169%
CJSC "BG Realty"	90,815	90,815	0.0164%
OJSC Odessa cable plant "Odeskabel"	70,217	70,217	0.0127%
Private enterprise trading house "Nachalo"	23,406	23,406	0.0042%
CJSC "Odessavinprom"	16,697	16,697	0.0030%
Subtotal for Legal Entities	171,739,176	171,739,176	30.9440%
Yuriy O. Rodin	125,853,355	125,853,355	22.6763%
Mark I. Bekker	82,444,442	82,444,442	14.8549%
Alla Yu. Vanetsiants	67,350,545	67,350,545	12.1352%
Vadim V. Morokhovskiy	41,338,756	41,338,756	7.4484%
Oleksandr G. Rodin	15,042,873	15,042,873	2.7104%
Liya S. Morokhovska	13,332,095	13,332,095	2.4022%
Tamara M. Rodina	9,274,442	9,274,442	1.6711%
Lyubov S. Bekker	8,237,426	8,237,426	1.4842%
Oleksandr M. Groysman	6,872,146	6,872,146	1.2382%
Ganna Yu. Rodina	4,711,264	4,711,264	0.8489%
Levon S. Vanetsiants	2,968,680	2,968,680	0.5349%
Velya A. Rodina	2,762,762	2,762,762	0.4978%
Oleksandr F. Kuperman	2,100,632	2,100,632	0.3785%
Eduard P. Stas	706,713	706,713	0.1273%
Volodimir P. Vugelman	93,623	93,623	0.0169%
Ilona V. Chornenka	70,217	70,217	0.0127%
Musiy G. Khazankin	26,167	26,167	0.0047%
Maria S. Svoboda	23,866	23,866	0.0043%
Katerina A. Morozenko	23,406	23,406	0.0042%
Igor G. Zhabokritskiy	11,859	11,859	0.0021%
Anatoliy P. Tapor	8,955	8,955	0.0016%
Other Private Shareholders	6,600	6,600	0.0012%
Subtotal for Private Shareholders	383,260,824	383,260,824	69.0560%
Total	555,000,000	555,000,000	100.0000%

The Bank is ultimately controlled by two families originally from Odessa, who own 67 per cent. and 22 per cent. stakes in the Bank, with another 10 per cent. belonging to the family of the Bank's Chairman.



APENDIX A. UKRAINIAN BANKING SYSTEM

The current institutional framework of the Ukrainian banking sector consists of the NBU and commercial banks. As at 31 December 2007, there were a total of 198 commercial banks registered in Ukraine, 175 of which have been granted licences by the NBU to perform banking transactions. The Ukrainian banking sector has a high level of concentration of capital. According to the NBU, as at 31 December 2007, approximately 50 per cent. of the banking sector's total assets were held by the ten largest Ukrainian banks. As at 31 December 2007, Ukraine's two state-owned banks (The State Export-Import Bank of Ukraine (Ukreximbank) and State Savings Bank of Ukraine (Oschadbank)) had approximately 8.0 per cent. of the Ukrainian banking sector's total assets, 7.3 per cent. of the total loan portfolio and 9.8 per cent. of total retail deposits in Ukraine. As at 31 December 2007, 47 banks in Ukraine had some foreign capital, of which 17 were fully owned by foreign owners.

According to the NBU, as at 31 December 2007, the total assets of Ukrainian banks licensed to perform banking transactions amounted to UAH 599.4 billion. The total loan portfolio of such banks as at 31 December 2007 constituted UAH 430.1 billion, including UAH 276.4 billion of corporate loans and UAH 153.6 billion of retail loans.

According to the NBU, during the year ended 31 December 2007, the statutory capital of Ukrainian banks that were licensed to perform banking transactions increased by 63.2 per cent., amounting to UAH 42.9 billion as at 31 December 2007 (compared to a 62.7 per cent. increase in statutory capital in 2006). During the year ended 31 December 2007, the total assets and total liabilities of all licensed Ukrainian banks increased by, respectively, 76.2 per cent. and 78.0 per cent. and amounted to UAH 599.4 billion and UAH 529.8 billion, respectively (compared to increases of 59.1 per cent. and 57.9 per cent., respectively, in 2006). The regulatory capital of Ukrainian banks increased by 75.6 per cent. during the year ended 31 December 2007 (compared to a 56.0 per cent. increase in 2006), amounting to UAH 72.3 billion as at 31 December 2007 (the NBU data does not specify whether this figure refers to all banks or only those licensed to perform banking transactions).

Commercial banks operating in Ukraine are divided by the NBU into four groups according to the size of assets of the banks as at 31 December 2007, the first group included 17 banks with total assets of more than UAH 11 billion; the second group included 17 banks with total assets ranging from UAH 3 billion to UAH 11 billion; the third group included 34 banks with total assets ranging from UAH 1 billion to UAH 3 billion; and the fourth group included 114 banks with total assets of less than UAH 1 billion.

Despite the NBU's rate-cutting policies, the average annual lending rate of Ukrainian commercial banks as at 31 December 2007 was 13.9 per cent. for loans in Hryvnia and 11.3 per cent. for loans in foreign currency, according to NBU statistics.



Evolution of the Ukrainian Banking Sector

During the last decade, the banking sector has been one of the fastest growing sectors of the Ukrainian economy. The Ukrainian banking sector is increasingly competitive and there have been a number of recent acquisitions of Ukrainian banks by foreign banks, which is likely to increase competition further.

Ukraine had 76 registered (commercial) banks in 1991. The total number of banks increased to 230 by 1995 and 193 by 2007. Since 1994, Ukreximbank and Oschadbank have been the only two wholly state-owned banks in Ukraine. No single bank currently has a dominant position in any banking business in Ukraine.

From 1991 to 1993, the Ukrainian banking industry underwent a period of reorganisation and rapid growth. Soviet-era banks were re-registered by the NBU and a number of the current leading Ukrainian banks were established or re-registered during this period. The total number of banks registered by the NBU almost doubled from 1991 to 1992 and again from 1992 to 1993. In 1994 and 1995, the NBU strengthened banking regulations and sought to bring domestic standards closer to international standards. As a result, twelve banks were liquidated after failing to comply with these more rigorous standards during this period. In response, the NBU introduced a number of mandatory financial ratios for banks. The NBU also implemented a national electronic payment system to facilitate electronic settlements within Ukraine. Further, the NBU tightened its monetary policy in order to address hyperinflation, which had reached 400 per cent. in 1994. This resulted in improved borrowing rates for Ukrainian businesses and consumers.

The period from 1996 to mid-1998 was a period of stabilisation in the Ukrainian banking system. The introduction of the Hryvnia in 1996, together with a further tightening of the NBU's monetary and budget deficit policy, led to a further reduction in inflation and interest rate spreads. The banking sector's profit in 1996 was twice that of the previous year. However, the rapid growth of the Ukrainian banking sector was halted by the Russian financial crisis in August 1998, which resulted in the depreciation of the Ukrainian Hryvnia (which fell from UAH 2.1 per U.S. Dollar to UAH 5.4 per U.S. Dollar over a 17 month period). Sixteen banks were liquidated during 1998.

From mid-1998 to mid-2001, the Ukrainian banking system underwent a period of modernisation. In 1998, the NBU promulgated international accounting standards for Ukrainian banks. Banks with foreign capital entered the market and introduced new banking services and products. In 2001, Ukraine was placed on the list of Non-Cooperative Countries and Territories of the FATF as a result of its non-cooperation with the FATF and its failure to enact anti-money laundering legislation that met international standards. Nevertheless, total loans and assets in the banking sector continued to grow. At the beginning of 2004, the FATF removed Ukraine from its list of Non-Cooperative Countries and Territories. In January 2006, it ended formal monitoring of Ukraine. During the period from 2004 to 2006, a number of foreign banks acquired majority stakes in leading Ukrainian banks, including Bank Aval (Raiffeisen International Bank-Holding AG) and UkrSibbank (BNP Paribas), Raiffeisenbank Ukraine (OTP Bank), as well as Mriya (Vneshtorgbank) and smaller banks including Index-Bank (Credit Agricole).



Legislative Framework for the Ukrainian Banking Sector

The NBU regulates the banking activities of Ukrainian banks in accordance with, among other laws, the Law of Ukraine On the National Bank of Ukraine of 20 May 1999 (the National Bank Law), the Law of Ukraine On Banks and Banking Activity of 7 December 2000 (the Banking Law), Ukrainian legislation on joint stock companies and other business entities, as well as various NBU regulations.

These laws and regulations set out the list of banking operations and other transactions that may be performed by banks and establish the framework for the registration and licensing of banks and the regulation of banking activities by the NBU.

Banking Operations

Banks provide a wide range of banking services. Banks are permitted to perform the operations specified in their banking licence and the written permit issued to them by the NBU. On the basis of their banking licence, banks may perform the following operations: (i) taking deposits from legal entities and individuals; (ii) opening and servicing current accounts of customers and correspondent banks, including transferring funds from these accounts by means of payment instruments and placing funds on these accounts; (iii) depositing funds on their own behalf, under their own terms and at their own risk; (iv) granting guarantees, bails and similar instruments; (v) factoring; (vi) leasing; (vii) safekeeping and renting safes for storing valuables and documents; (viii) issuing, purchasing, selling and servicing cheques, notes and other negotiable payment instruments; (ix) issuing bank payment cards and performing operations using these cards; and (x) providing consulting and informational services with respect to banking operations. On the basis of their written permit, banks may be authorised to perform the following operations: (i) foreign currency operations; (ii) issuing their own securities; (iii) purchasing and selling securities on behalf of their clients; (iv) operations on the securities market on their own behalf (including underwriting); (v) investing in the statutory capital and shares of other legal entities; (vi) issuing and making payments under state and other monetary lotteries; (vii) transporting cash and valuables; (viii) money market operations, exchange rate and interest rate swaps, and financial futures and options; (ix) trust management of funds and securities; and (x) depositary, custodianship and registrar services.

Under the Banking Law, banks may not engage in manufacturing, commodities trading (except for trading in precious metals and coins) or insurance activities (except for insurance brokerage).

Role of the NBU

The NBU is the central bank of Ukraine. Established in 1991 and governed in accordance with the Constitution of Ukraine and the National Bank Law, the NBU is a specialised state institution whose principal objective is to ensure the external and internal stability of the national currency. To carry out its main function, the NBU strives to maintain the stability of



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the banking system and, within its competence, price stability. The NBU sets the official exchange rate of the national currency against foreign currencies, the discount rate and other interest rates. The NBU is also responsible for the accumulation and custody of the state's gold and currency reserves. In addition, it registers commercial banks, issues licences, supervises the operations of Ukrainian banks and determines the procedures for providing emergency funds to commercial banks.

Monetary Policy

The NBU is responsible for implementing monetary policy. Currently, the NBU implements monetary policy through instruments such as mandatory reserve requirements for banks, setting interest rates, refinancing commercial banks, issuing debt instruments and carrying out reverse repo operations. The NBU reduced the discount rate from 45 per cent. at the beginning of 2000 to 12.5 per cent. by the end of 2001 (after the economy had begun to stabilise following the regional financial crisis of 1998), and to 7.0 per cent. in December 2002. The NBU subsequently increased the discount rate to 9.5 per cent. (effective 10 August 2005) and then decreased it to 8.5 per cent. (effective 10 June 2006). From 1 June 2007, the discount rate was further decreased to 8.0 per cent.

The NBU has stated that the main goal of its monetary policy in 2007 is to maintain the stability of the Hryvnia and macroeconomic balance, and to establish the prerequisites for the renewal of stable economic growth and the solution of current and longer-term social and economic problems in Ukraine.

Registration and Licensing

The NBU registers commercial banks and grants licences and written permits for the performance of banking activities. The NBU may suspend or revoke banking licences and written permits. The NBU maintains the State Register of Banks of Ukraine.

Supervision and Control

The NBU oversees banks' compliance with mandatory ratios, limits and reserve requirements, imposes sanctions for violations of such ratios, limits and requirements, establishes reporting requirements and accounting rules and procedures for banks, oversees banks' operations and transactions, appoints temporary administrators to banks undergoing financial difficulties and regulates the direct and indirect acquisition of shareholdings in banks exceeding 10, 25, 50 and 75 per cent. thresholds.

Transactions with Banks

The NBU lends to banks, maintains other banks' correspondent accounts, provides cash and settlement services to banks, issues guarantees to banks, carries out transactions with sovereign debt securities, trades bullion and precious stones, and purchases and sells foreign



currency. The NBU may not own capital in other banks and commercial entities, perform real estate transactions (except as necessary for its own operations), or engage in trading, manufacturing, insurance or other activities which do not directly relate to its functions.

Exchange Control

In accordance with Ukrainian foreign currency legislation, the NBU has substantial powers to regulate foreign currency operations. In accordance with the Decree of the Cabinet of Ministers of Ukraine On the System of Currency Regulation and Currency Control of 19 February 1993, the NBU is empowered, among other things, to implement the government's foreign currency policy, to determine the procedures for purchasing and carrying out transactions with foreign currency, to issue and revoke licences for foreign currency operations, to determine the methodology for setting and applying foreign currency exchange rates, and to stipulate uniform accounting and reporting procedures for banks.

Governing Bodies of the NBU

The principal governing bodies of the NBU are the Council and the Board. The Council, being the highest governing body of the NBU, consists of 15 members, seven of whom are appointed by Parliament and seven of whom are appointed by the President of Ukraine. The Governor of the NBU (nominated by the President of Ukraine and appointed by Parliament for a five-year term) acts *ex officio* as the fifteenth member of the Council. The Council is responsible, in particular, for formulating the principles of Ukraine's monetary policy and has the right to veto the Board's decisions if they contravene such principles. The Board, which is comprised of the Governor, his or her deputies and other members of the Board, is responsible for implementing Ukraine's monetary policy, the development and implementation of other NBU policies and the management of the NBU.

The NBU organisation includes its headquarters in Kyiv, branches (or territorial departments), clearing units, the Mint, a banknote paper factory, the State Treasury of Ukraine, the Central Depository, other specialised units, banking educational institutions and operational service units.

According to the National Bank Law, neither the state nor the NBU are liable for the other's obligations, unless either has accepted such liability under an agreement or such liability is imposed by Ukrainian legislation. The NBU is legally and financially independent of the Ukrainian Government. Under the National Bank Law, the NBU is generally not permitted to extend loans to the state budget for the purpose of covering the state budget deficits.

Banking Supervision

Under the National Bank Law and the Banking Law, the NBU is authorised to adopt binding regulations concerning banking and foreign currency operations. The NBU has actively used this power in recent years, creating a detailed and extensive body of regulations. The NBU adopted the Banking Regulation Directive which establishes capital adequacy, liquidity and



other ratios. The NBU also sets auditing and other requirements for commercial banks. Some of the principal features of the supervisory regime governing banks in Ukraine are set out below.

Mandatory Ratios

The NBU is authorised to introduce mandatory ratios for Ukrainian banks. The Banking Regulation Instruction envisages five different types of mandatory ratios/requirements: capital requirements, liquidity requirements, credit risk requirements, investment risk requirements and currency position requirements.

Capital Requirements

The NBU has established requirements for minimum regulatory capital, regulatory capital adequacy and core capital adequacy which are binding on banks in Ukraine.

A bank's regulatory capital (being the sum of its principal (or core) capital, which consist of, among other items, its statutory capital, share premium, general loan loss reserves retained earnings and certain reserve funds, and additional capital, which consists of, among other items, assets revaluation reserves and subordinated debt) cannot be less than the minimum regulatory capital requirements established by the NBU for each particular year. From 1 May 2004, the NBU calculates the minimum regulatory capital requirement in UAH in an amount equivalent to the Euro amounts set forth in the Banking Regulation Instruction. As at 1 January 2007, the minimum regulatory capital requirements for newly established banks (being those that have been in existence for less than one year) are EUR 5 million for nationwide banks, EUR 3 million for regional banks and EUR 1 million for cooperative banks. The minimum regulatory capital requirements for banks that have been in existence for a period from one to two years are EUR 5.5 million for nationwide banks, EUR 3.5 million for regional banks and EUR 1.1 million for cooperative banks; while the requirements for banks in existence for a period from two to three years are EUR 6 million, EUR 4 million and EUR 1.2 million, respectively; for those in existence for a period from three to four years: EUR 7 million, EUR 4.5 million and EUR 1.35 million, respectively; and for those in existence for more than four years: EUR 8 million, EUR 5 million and EUR 1.5 million, respectively. These regulatory capital requirements are subject to periodic increases.

The minimum regulatory capital adequacy requirement is intended to ensure that Ukrainian banks are able to discharge their liabilities when due and in full. The minimum regulatory capital adequacy requirement set by the NBU is 10 per cent. of a bank's risk-weighted assets (or 15 per cent. in the case of banks that have been operating for less than 12 months, and 12 per cent. for banks that have been operating for between 12 and 24 months). Risk-weighted assets are calculated by applying various risk weightings to the bank's assets and off-balance-sheet commitments according to the terms set by the NBU. The minimum core capital adequacy requirements are intended to ensure that the creditors and depositors of Ukrainian banks are protected from unexpected losses that banks may incur in the course of their operations. The core capital adequacy requirement is calculated as the ratio of the bank's core capital to its total assets and must be at least 4 per cent.



Liquidity Requirements

The NBU has also established three separate liquidity ratios: the instant liquidity ratio, the current liquidity ratio and the short-term liquidity ratio. The instant liquidity ratio is set by the NBU in order to ensure that a bank may meet its liabilities from highly liquid assets, and is calculated as the ratio of a bank's correspondent account funds and cash to its current liabilities. According to the Banking Regulation Instruction, a bank must have an instant liquidity ratio of at least 20 per cent. The current liquidity ratio is set in order to determine a bank's ability to match its liquid assets to liabilities of corresponding maturity. The current liquidity ratio is calculated with respect to the bank's liabilities with maturities of up to 31 days. A bank's current liquidity ratio (being the ratio of the bank's primary and secondary liquid assets, including cash, banking metals, cash held on correspondent accounts with the NBU and other banks and debt securities issued or refinanced by the NBU, to liabilities with maturities of up to 31 days) must be at least 40 per cent.

The short-term liquidity ratio is set in order to determine a bank's ability to meet its short-term liabilities from its liquid assets. A bank's short-term liquidity ratio (being the ratio of liquid assets to short-term liabilities with maturities of less than one year) must be at least 20 per cent. According to the NBU's definition, liquid assets include cash, banking metals, amounts in correspondent accounts, debt securities of state agencies in the bank's trading portfolio, available-for-sale and held-to-maturity securities, and short-term interbank deposits and loans. Short-term liabilities include on-demand liabilities, funds of the state budget of Ukraine, short-term loans from the NBU and other banks, short-term interbank and customer deposits, short-term debt instruments issued by the bank and liabilities under all types of guarantees and committed credit lines to banks and customers.

Credit Risk Requirements

The Banking Regulation Instruction provides for four types of maximum borrowing limits: (a) the maximum credit risk per borrower; (b) the maximum total amount of large credit risks; (c) the maximum total amount of loans, guarantees and sureties per insider; and (d) the maximum total amount of loans, guarantees and sureties granted to all insiders.

The maximum credit risk per borrower (or group of borrowers, if any one borrower owns more than ten per cent. of the shares of the other, or any third party owns more than ten per cent. of the shares of each such borrower, or the borrowers use the loan proceeds jointly or for providing a further loan to a third party which is a customer of the lending bank) is calculated as the ratio of all of the bank's financial claims outstanding with respect to a particular borrower to the bank's regulatory capital, and may not exceed 25 per cent. However, a bank's internal regulations may establish a more stringent limit on loans to a single borrower. Notwithstanding the above borrowing limit, Ukrainian banking regulations permit banks to advance a loan to a borrower which would result in the bank exceeding the maximum credit risk amount per borrower provided the bank fulfils the following conditions: (i) the bank is well capitalised (meaning that the bank complies with the minimum regulatory capital requirement, the bank's regulatory capital adequacy ratio is at least 17 per cent. and the bank's core capital adequacy ratio is not less than 8 per cent.) or sufficiently capitalized (meaning that the bank complies with the minimum regulatory capital requirement, the bank's regulatory capital adequacy ratio is higher than 8 per cent. but less than 17 per cent., and the bank's core



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capital adequacy ratio is higher than 4 per cent. but less than 8 per cent.); and (ii) the loan is secured either by a pledge of proprietary rights over the monies deposited with the lender bank or by the pledge of savings/deposit certificates issued by the lender bank for the term of the loan or by an unconditional commitment granted to the bank by the government or central bank of a class A state (which would include most European states, the USA, Canada, Switzerland, Japan and Australia), the International Bank for Reconstruction and Development or the European Bank for Reconstruction and Development, or, for loans with a maturity of up to one year, banks having an investment grade credit rating assigned by one of the major credit rating agencies.

Under the Banking Regulation Instruction, credit risks are considered to be large if the amount of all loans, including off-balance sheet commitments such as guarantees granted to a single borrower or a group of affiliated borrowers, equals or exceeds 10 per cent. of the bank's regulatory capital. The maximum total amount of large credit risks may not exceed 800 per cent. of the bank's regulatory capital. If the maximum total amount of large credit risks is exceeded, the regulatory capital adequacy ratio is required to be doubled, if such excess is less than 50 per cent., and tripled, if such excess is more than 50 per cent.

The maximum total amount of loans, guarantees and sureties per insider is required to be less than five per cent. of the statutory capital of a bank. Banks must also comply with the maximum total amount of loans, guarantees and sureties granted to all insiders ratio. This ratio is calculated as the ratio of total indebtedness of all of the bank's insiders and aggregate amount of the off-balance commitments granted by the bank to all its insiders to the amount of the bank's statutory capital and may not exceed 30 per cent. The bank's internal regulations may establish a more stringent limit on the maximum total amount of loans, guarantees and sureties granted to insiders.

Investment Risk Ratio

The Banking Regulation Instruction provides for two mandatory ratios related to investment risk: the aggregate investment risk ratio and the single issuer investment risk ratio. The single issuer investment risk ratio limits the risk connected with investments (whether direct or portfolio) in equity of a single issuer, is calculated as a ratio of the amount invested in the equity securities and/or statutory capital of such issuer to the amount of the bank's regulatory capital and may not exceed 15 per cent. The aggregate investment risk ratio limits the risk connected with total equity investments (whether direct or portfolio) of a bank. The aggregate investment risk ratio is calculated as a ratio of the total equity investments to the amount of the bank's regulatory capital and may not exceed 60 per cent.

Open Currency Position Risk

The currency position of Ukrainian banks is determined on a daily basis and in respect of each particular foreign currency. The general open currency position is determined as the sum of such individual positions. The general open position of a bank may not exceed 30 per cent. of the bank's regulatory capital, while the general long open position may not exceed 20 per cent. of the bank's regulatory capital and the general short open position may not exceed



10 per cent. of the bank's regulatory capital. In addition, a bank's long open position in freely convertible currencies may not exceed 15 per cent. of the bank's regulatory capital, the open position in non-convertible currencies and banking metals may not exceed five per cent. of the bank's regulatory capital (at the bank's discretion) and the open currency position under forward contracts may not exceed 10 per cent. of the bank's regulatory capital.

Compulsory Reserve Requirements

Reserve Requirements

In 2001, the NBU adopted regulations relating to the mandatory reserves of commercial banks which provide that the NBU will impose sanctions for the failure to maintain the prescribed amounts of mandatory reserves. Such sanctions are payable from a bank's profits. Currently, commercial banks are required annually to transfer to their reserves not less than five per cent. of their profit, unless and until such reserves are equal to 25 per cent. of their regulatory capital. The NBU may require commercial banks to increase their mandatory reserve amounts.

The NBU established these mandatory reserve requirements in order to maintain the liquidity of the banking system and the stability of the Ukrainian Hryvnia. Banks are required to maintain certain reserves in current accounts with the NBU. There are no restrictions on the withdrawal of funds from the NBU. However, if the minimum average reserve requirements are not met, a bank may be subject to penalties. Reserve requirements are calculated as a percentage of certain of the bank's liabilities. In particular, since 1 October 2006, reserves are required to be not less than the sum of one per cent. of the amount of demand deposits and current accounts of customers in Hryvnia, five per cent. of demand deposits and current accounts of customers in foreign currency, 0.5 per cent. of term deposits of customers in Hryvnia and four per cent. of term deposits of customers in foreign currency.

Banks are required to file information regarding their reserves with the NBU and its regional units promptly after the end of each reporting period. In the event of non-compliance by a bank with the compulsory reserve requirements, the NBU may impose relevant penalties in accordance with applicable regulations.

Amounts deposited with the NBU in compliance with the compulsory reserve requirements may not be subject to attachment. In the event of the revocation of a bank's banking licence, such amounts are included in the pool of assets generally available for distribution amongst the bank's creditors in the order established by applicable Ukrainian legislation.

Provisioning and Loss Allowances

Banks must comply with mandatory requirements to cover net loan risks and review those provisions on a monthly basis. Some loan products, such as, among others, real estate backed leasing transactions, subordinated loans, uncommitted off-balance sheet credit lines (other than commitments extended to banks) and funds in foreign currency transferred to the



NBU, do not require any provisions. With effect from 10 April 2007, Ukrainian legislation sets forth separate provisioning requirements for loans in national and foreign currencies as well as for certain consumer loans. Each of the above groups of loans is classified into five categories, subject to varying provisioning requirements. The following provisioning requirements are set forth for loans in national currency: 1 per cent. for standard loans, 5 per cent. for loans on watch, 20 per cent. for substandard loans, 50 per cent. for doubtful loans and 100 per cent. for bad loans. Provisioning requirements applicable to loans in foreign currency are higher than for loans in national currency in line with an NBU policy aimed at reducing credit risks, especially under loans in foreign currencies and are as follows: 2 per cent. for standard loans, 7 per cent. (10 per cent. for loans to borrowers who have no foreign currency earnings) for loans on watch, 25 per cent. (40 per cent. for loans to borrowers who have no foreign currency earnings) for substandard loans, 60 per cent. (80 per cent. for loans to borrowers who have no foreign currency earnings) for doubtful loans and 100 per cent. for bad loans.

Provisioning requirements applicable to consumer loans are: 2 per cent. for standard loans, 10 per cent. for loans on watch, 40 per cent. for substandard loans, 80 per cent. for doubtful loans and 100 per cent. for bad loans. Banks are required to complete implementation of the newly established provisioning requirements by 1 October 2007.

Protection of Depositors

The Law of Ukraine on the Fund for Guaranteeing Deposits of Individuals of 20 September 2001 (the “Deposits Securing Law”) introduced the current system of securing deposits held by individuals in Ukrainian banks. It modified the previously existing arrangements for the protection of depositors that were established in 1998 by the Presidential Decree On Measures for the Protection of the Rights of Individual Depositors of Commercial Banks of Ukraine of 10 September 1998 (the “Decree”).

Pursuant to the Deposits Securing Law, Ukrainian commercial banks must be members of the Individual Deposits Guarantee Fund (the “Deposit Guarantee Fund”), established under the Decree and operating according to the Deposits Securing Law, and are obliged to transfer to the Deposit Guarantee Fund an initial contribution in the amount of one per cent. of their registered statutory capital (payable once after obtaining a banking licence). The amount of the regular contribution payable to the Deposit Guarantee Fund by Ukrainian banks is determined twice per year, on 31 December and 30 June, at a rate of 0.25 per cent. of the aggregate amount of deposits, including interest accrued, and is payable quarterly in equal instalments. The Deposit Guarantee Fund may also require Ukrainian banks to make a special contribution if the revenues of the Deposit Guarantee Fund are not sufficient to repay and service loans borrowed by the Deposit Guarantee Fund in order to meet compensation claims following the collapse of one or more banks. The Deposit Guarantee Fund guarantees deposits with commercial banks, including interest, to a maximum of UAH 25,000 per depositor with each such bank (since 26 February 2007). Deposits are recognised as unavailable, meaning eligible for compensation from the funds held by the Deposit Guarantee Fund, on the date of appointment of a bank’s liquidator. As of 7 June 2007, the Deposit Guarantee Fund had 169 member banks and three temporary member banks. As at 31



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December 2007, the total amount of funds accumulated by the Deposit Guarantee Fund was equal to UAH 1,335 million.

Reporting Requirements

Banks are required to submit annual reports that contain audited financial statements or consolidated financial statements, if they have affiliates under their control, as well as a general description of the bank's business. Financial statements must include a balance sheet, an income statement, a cash flow statement and a shareholders' equity statement. The general description section describes the basic features of a bank's business and its organisation and management. Interim financial statements are submitted by banks on a quarterly basis and consist of a balance sheet, an income statement, an offbalance sheet liabilities statement, trust management accounts and a cover letter. The purpose of the cover letter is to describe and explain events and operations that are important for a fair presentation of the financial position of a bank and are material. Banks are also required to submit to the NBU statistical data on a daily, weekly and monthly basis to enable the ongoing review and monitoring by the NBU of their performance and financial position.

The NBU may at any time conduct full or selective audits of any bank filings and may inspect any of the banks' books and records.

Accounting Practices

The NBU has established a standard format for the presentation of financial and statistical data and recording of banking transactions. The Banking Law requires the annual balance sheet and other financial statements of banks to be certified by an independent licensed auditor.



Insolvency Regime

The Ukrainian Parliament has not yet adopted any laws specifically regulating insolvency and bankruptcy proceedings in respect of Ukrainian banks. In Ukraine, solvency restoration and bankruptcy proceedings in respect of Ukrainian legal entities are generally governed by the Law of Ukraine On the Restoration of a Debtor's Solvency or Declaration of its Bankruptcy of 14 May 1992 (the "Insolvency Law"). However, the application of the Insolvency Law to Ukrainian banks is limited and modified by the provisions of the Banking Law. A Ukrainian bank may be restored to solvency by means of a temporary administration procedure directed and supervised by the NBU.

Restoration of Solvency

Under Ukrainian law, the NBU would be required to impose temporary administration on a Ukrainian bank if the NBU were to determine that there exists a significant threat to the solvency of the bank. In addition, the NBU would have discretion to impose temporary administration on a Ukrainian bank if (i) a bank systematically fails to comply with any legitimate requests or demands of the NBU, (ii) the Ukrainian bank's regulatory capital decreases by 30 per cent. over a six month period and it is in breach of any of the mandatory ratios, (iii) a bank fails to meet ten per cent. or more of its aggregate overdue liabilities and such failure continues for at least 15 business days, (iv) any member of the bank's management is arrested for or convicted of a criminal offence, (v) a bank commits any act aimed at the concealment of any accounts, assets, registers, reports or other documents, (vi) a bank refuses to submit to authorised representatives of the NBU any documents or information specified in the Banking Law without a legitimate reason, (vii) there is a public conflict within the management, or (viii) a bank requests the NBU to institute temporary administration.

The temporary administrator appointed by the NBU would replace all of the bank's governing bodies for the entire term of the temporary administration (being a period of up to one year with a possible extension for another year if the bank's liabilities are equal to or exceed ten per cent. of the total liabilities of all Ukrainian banks at the time of such extension), and would be authorised to carry out any acts aimed at the bank's financial rehabilitation, including but not limited to (i) terminating any ongoing operation (including the discharge of any outstanding obligation) of the bank (without terminating or invalidating the agreement itself), and (ii) terminating, in accordance with Ukrainian legislation, any agreement to which the bank is party and which, in the opinion of the temporary administrator, is either loss-making or unnecessary. The latter applies only to an agreement which contains outstanding obligations of any party. The temporary administrator would have a broad discretion in determining whether a particular agreement is loss-making or unnecessary, given that Ukrainian legislation provides no criteria for making such determination. In each case, a dissatisfied counterparty would be entitled to challenge the temporary administrator's decision in court and, where applicable, to demand compensation by the Ukrainian bank for any damages resulting from such decision.



During the term of operation of the temporary administration of a Ukrainian bank, but not longer than for a period of six months during such term, the NBU may impose a moratorium on the satisfaction of claims of the bank's creditors which became due prior to the appointment of the temporary administrator or the introduction of the moratorium. Applicable legislation exempts the following payments from the moratorium: ongoing operations performed by the temporary administrator; payroll liabilities; alimonies; obligations in respect of personal injuries; copyright liabilities; and liabilities to other creditors incurred in connection with obligations assumed by the bank in the course of temporary administration. During the term of the moratorium, the accrual of any financial sanctions for the non-performance of the bank's payment obligations (including default interest, penalties and fines), as well as any enforcement action for the recovery of debts, would be suspended.

Additionally, the temporary administrator may apply to a Ukrainian court to declare invalid any agreement for the disposal of the bank's assets prior to his appointment on one of the grounds provided in the Banking Law, including any transaction (meaning transfer of assets or payment): (a) within a six month period before the appointment of the temporary administrator, if the purpose of the transaction was to grant a preference to a creditor of the bank as compared to the bank's other creditors (such as where the transaction was not carried out on an arm's-length basis and/or was carried out on preferential terms); or (b) within a three-year period before the appointment of the temporary administrator, if the value of the asset or services was significantly lower than the price paid by the bank; or (c) within a three-year period before the appointment, if the purpose of the transaction was to conceal the bank's assets from the other creditors or to violate the rights of such creditors; or (d) within a one-year period before the appointment of the temporary administrator, if the transaction with a related party of the bank threatened the interests of the bank's creditors or contravened the requirements of Ukrainian legislation; or (e) within a three-year period before the appointment of the temporary administrator, if the transfer of assets was made without consideration to the bank; or (f) if it was based on forged documents or if it was of a fraudulent nature. If an agreement providing for such transaction is declared invalid by a court, the bank and its counterparty will be required to make full restitution, meaning that each of the bank and its counterparty will be required to repay all amounts and return all assets (or, if such return is not possible, to pay the value of the assets at the prices effective at the date of such restitution) received from each other under such agreement.

Insolvency Liquidation Procedure

If the temporary administration procedures imposed by the NBU do not result in the restoration of the bank's solvency, the NBU may revoke the bank's license and order its liquidation. The NBU is also authorised to revoke the bank's licence and order its liquidation if, in the course of the temporary administration of the bank, the NBU considers that it is impracticable to bring the bank's activity into legal and financial conformity with the provisions of the Banking Law and NBU regulations within a one-year period (except that, for banks whose liabilities constitute ten per cent. or more of the aggregate liabilities of the banking system, such term may be extended up to two years), or if the bank is not in compliance with the provisions of the Banking Law or NBU regulations and such non-compliance has resulted in substantial loss of the bank's assets and there is an indication that the bank is insolvent. The NBU is obliged to institute bankruptcy proceedings against a Ukrainian bank if the bank is not able to discharge its obligations under a court judgment within a six-month period and no



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work-out agreement has been reached between the bank and its creditor within that period. Following a decision by the NBU to revoke a bank's license and commence liquidation proceedings, the NBU must apply to a court for approval of the liquidator appointed by the NBU and for confirmation that the liquidation procedure complies with the requirements set out in the Banking Law.

Creditors of a bank intending to initiate bankruptcy proceedings should, before submission of the bankruptcy petition to a Ukrainian court, request the NBU to liquidate the bank upon presentation to the NBU of evidence of the bank's inability to discharge its payment obligations on time and in full. If the NBU fails to respond within one month, the creditors would be entitled to submit a bankruptcy petition to a competent Ukrainian court. Upon receipt of the bankruptcy petition, a Ukrainian court must obtain either an opinion of the NBU on the feasibility and grounds for the liquidation of the bank, and may only proceed with the bankruptcy proceedings if the NBU provides an affirmative opinion or a resolution of the NBU on the revocation of its banking licence and the appointment of a liquidator. The court must dismiss the creditor's bankruptcy petition if the NBU issues a negative opinion. Bankruptcy proceedings against a Ukrainian bank may not start as long as its banking licence remains effective. Ukrainian law does not permit the financial rehabilitation (sanation) of a bank if its banking licence has been revoked. Upon revocation of the banking licence, the authority that instituted bankruptcy proceedings (either the NBU or a Ukrainian court) must appoint a liquidator. The court may reject the liquidator appointed by the NBU if it finds that there is a conflict of interest between such liquidator and the bank. The liquidator would assume his duties immediately upon revocation of the banking licence and would be responsible for, inter alia: (i) preserving the bank's assets; (ii) managing and disposing of the assets; (iii) creating an inventory and appraising the assets; (iv) exercising the powers of the bank's management bodies; (v) chairing the liquidation commission and forming the liquidation estate; and (vi) filing claims against third parties to recover debts owed to the bank.

In addition, a liquidator would be entitled to refuse to perform, and would be entitled unilaterally to terminate, in accordance with applicable law, any agreement entered into by a Ukrainian bank which had not been performed by such time.

Upon the revocation of a bank's banking licence and appointment of a liquidator: (i) all of the bank's payment obligations that existed prior to the revocation of the banking licence will become due and payable in accordance with the procedure and order of priority established by applicable Ukrainian legislation; (ii) no default-related penalties provided for in the agreements entered into with, and payable by, the Ukrainian bank, will further accrue; (iii) the bank will be precluded from making payments to third parties, except for certain limited categories of payments (such as maintenance and utility payments and salaries); and (iv) the bank will be precluded from accepting and making payments for the benefit (and at the instruction) of its clients.

Upon commencement of liquidation proceedings, the liquidator of a Ukrainian bank must publish in the official bulletins of Parliament and the Cabinet of Ministers of Ukraine a notice on the liquidation of the bank. Creditors are entitled to submit their claims against the bank to the liquidator within the one-month period after the date of publication of the notice. Creditors' claims filed after the expiry of the one-month period are deemed to have been settled.



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The liquidator must, within three months of the date of publication of the notice of liquidation, consider all claims filed by the bank's creditors, determine their amount and assign them to the respective priority category. Claims for the payment of fees and expenses incurred in connection with the liquidation and claims secured by pledge are satisfied outside of the order of priority established by the applicable legislation. The former are satisfied during the course of the liquidation proceedings and in accordance with the schedule approved by the NBU. Receipts from the sale of collateral are used solely for the satisfaction of claims secured by the collateral. The balance of the creditors' claims are satisfied upon the sale of the bank's assets in the following order of priority: first, liabilities resulting from death or personal injury; second, payroll liabilities incurred prior to the commencement of the liquidation proceedings; third, liabilities to individual depositors to the extent that such liabilities exceed the amount guaranteed by the Deposit Guarantee Fund, but not more than UAH 50,000; fourth, liabilities to individual depositors to the extent that such liabilities exceed UAH 50,000; fifth, liabilities to the Deposit Guarantee Fund; sixth, liabilities to individuals with respect to blocked payments (except liabilities to subjects of entrepreneurial activities); seventh, all other claims.

The liquidation of a bank must be completed within a three-year period from the date of revocation of the banking licence. However, such period may be extended by one or, in the case of banks whose liabilities are equal to or exceed ten per cent. of the aggregate liabilities of all Ukrainian banks, two years.

Anti-Money Laundering

In November 2002, the Ukrainian Parliament adopted the law On Combating the Legalisation (Laundering) of Income Obtained by Criminal Means (the "Anti-Money Laundering Law"). Banks are required to comply with the provisions of the Anti-Money Laundering Law relating to, among other things, the development of appropriate internal standards and procedures, client identification, monitoring of client operations and reporting of operations to the State Committee for Monitoring of Ukraine (the "SCFM"). The Anti-Money Laundering Law requires that banks monitor and report any transaction if the amount of such single transaction is equal to or exceeds UAH 80,000 (or its equivalent in foreign currencies) and the transaction has certain characteristics as set forth in the Anti-Money Laundering Law, including one or more of the following: the transaction involves a cross-border money transfer with a cash payment to the recipient; one or more of the parties is resident or has a bank account in a country that does not participate in international efforts to combat money-laundering (which generally corresponds to the list of Non-Cooperative Countries and Territories maintained by FATF); the transaction involves making bank deposits for a third party beneficiary; or the transaction involves the deposit of precious stones, precious metals and other property with a pawnbroker. In addition, banks are required to monitor any transaction involving any individual or organisation that is connected with terrorist activities (according to information provided by the SCFM) and any legal entity controlled by them or their agents. If bank officers suspect that a transaction is being conducted in order to legalise any funds received as a result of illegal activity or to finance terrorist activities, they are required to report such operations whether or not they qualify as monitored transactions.

**APPENDIX B. 2007 INTERIM FINANCIAL STATEMENTS****Consolidated balance sheet***In thousands of Ukrainian hryvnias*

	(Unaudited)*	
Assets	31.12.2007	31.12.2006
Cash and cash equivalents and mandatory reserve balances	1,037,975	554,628
Securities at fair value through profit or loss	199,288	114,799
Due from other banks	39,889	31,886
Loans and advances to customers	6,872,032	3,230,276
Investment securities available for sale	11,230	17,724
Current income tax prepayment	5,168	1,253
Intangible assets	4,511	2,332
Premises and equipment	532,934	433,375
Other assets	39,335	23,864
TOTAL ASSETS	8,662,362	4,410,137
Liabilities		
Due to the National Bank of Ukraine	90,000	82,000
Due to other banks	1,013,789	274,871
Customer accounts	5,966,514	3,289,492
Debt securities in issue	136,661	163,280
Loan participation notes	522,532	-
Other borrowed funds	-	15,718
Deferred income tax liability	40,581	25,843
Other liabilities	48,024	23,093
Subordinated debt	-	8,107
TOTAL LIABILITIES	7,818,101	3,882,404
EQUITY		
Share capital	563,896	362,396
Retained earnings	167,050	64,483
Currency translation reserve	7,434	-
Revaluation reserve for premises	91,331	48,117
Revaluation reserve for investment securities	1,099	-
Minority interest	13,451	52,737
TOTAL EQUITY	844,261	527,733
TOTAL LIABILITIES AND EQUITY	8,662,362	4,410,137

(*) Based on Pivdennyi Bank's IFRS management accounts. Please note that the final audited accounts are now available on Intralinks.

**Consolidated statement of income***In thousands of Ukrainian hryvnias*

	(Unaudited)*	
	2007	2006
Interest income	675,445	368,577
Interest expense	(389,817)	(187,486)
Net interest income	285,628	181,091
Provision for loan impairment	(34,182)	(15,147)
Net interest income after provision for loan impairment	251,446	165,944
Gains less losses from securities	1,705	7,534
Gains less losses from trading in foreign currencies	42,328	15,560
Foreign exchange translation (losses less gains)/gains less losses	115	3
Fee and commission income	128,941	80,833
Fee and commission expense	(30,539)	(7,375)
Recovery of/(provision for) impairment of investment securities available for sale	(1,682)	-
Recovery of/(provision) for losses on credit related commitments	3,798	(2,949)
Other operating income	1,896	2,077
Administrative and other operating expenses	(268,128)	(171,362)
Operating profit	129,880	90,265
Excess of interest in the associate's (subsidiary's) net assets acquired over cost of investment	12,607	5,409
Share of profit of associate	-	2,478
Profit before tax	142,487	95,458
Income tax expense	(35,355)	(23,565)
Profit for the period	107,132	71,893
Profit is attributable to		
Equity holders of the Bank	102,567	71,893
Minority interest	4,565	-
Profit for the period	107,132	71,893

(*) Based on Pivdennyi Bank's IFRS management accounts



Consolidated statement of cash flow

	For the year Ended 31 December	
	2007	2006
<i>In thousands of Ukrainian hryvnias</i>	(Unaudited)*	
Cash flows from operating activities		
Interest received	660,224	369,915
Interest paid	(327,334)	(175,614)
Income received from trading in trading securities	(382)	4,450
Income received from trading in foreign currencies	43,508	15,560
Fees and commissions received	135,096	80,833
Fees and commissions paid	(32,613)	(7,375)
Other operating income received	1,633	1,753
Staff costs paid	(138,496)	(88,955)
Administrative and other operating expenses paid	(99,918)	(61,584)
Income tax paid	(23,103)	(12,630)
Cash flows from operating activities before changes in operating assets and liabilities	218,615	126,353
Changes in operating assets and liabilities		
Net increase in mandatory cash balances with the National Bank of Ukraine	(76,475)	59,742
Net (increase)/ decrease in trading securities	-	8,346
Net decrease/(increase)/ in other securities at fair value through profit or loss	12,749	(23,755)
Net decrease/(increase) in due from other banks	(22,600)	32,031
Net increase in loans and advances to customers	(3,571,846)	(1,264,692)
Net increase in other assets	(2,541)	(621)
Net (decrease)/increase in due to the National Bank of Ukraine	8,000	82,000
Net increase in due to other banks	752,130	(26,657)
Net increase in customer accounts	2,419,411	1,181,543
Net decrease/(increase) in debt securities in issue	(28,754)	(24,296)
Net increase/(decrease) in other liabilities	22,142	636
Net cash from operating activities	(269,170)	150,630
Cash flows from investing activities		
Acquisition of investment securities available for sale	(20,074)	(14,224)
Proceeds from disposal of investment securities available for sale	26,568	62,171
Cash of subsidiary acquired, net of consideration paid	-	141,167
Investments in subsidiaries and affiliates	(64,170)	(16,446)
Acquisition of premises and equipment and intangible assets	(87,046)	(250,211)
Proceeds from disposal of premises and equipment	215	696
Net cash used in investing activities	(144,508)	(76,847)
Cash flows from financing activities		
Proceeds from loan participation loans	505,000	-
Proceeds from other borrowed funds	-	15,718
Proceeds from long-term debt securities in issue	-	130,384
Issue of ordinary shares	201,500	130,000
Issue of ordinary shares by subsidiary	28,112	-
Repayment of other borrowed funds	(15,718)	-
Repayment of subordinated debt	(8,037)	-
Net cash from financing activities	710,857	276,102
Effect of exchange rate changes on cash and cash equivalents	8,353	704
Net increase in cash and cash equivalents	305,533	350,589
Cash and cash equivalents at the beginning of the year	490,113	139,524
Cash and cash equivalents at the end of the year	795,646	490,113

(*) Based on Pivdennyi Bank's IFRS management accounts



Consolidated statement of changes in equity

	Attributable to equity holders or the Parent					Total	Minority interest	Total equity
	Share capital	Retained earnings	Revaluati on reserve for premises	Revaluati on reserve for securities	Currency translatio n reserve			
Balance at 31 December 2005	208,896	16,090	26,348	-		251,334		251,334
Available-for-sale securities:								
- Fair value gains less losses	--	--	--	3,082	--	3,082	--	3,082
- Derecognition	--	--	--	(3,082)	--	(3,082)	--	(3,082)
Premises and equipment:								
- Revaluation	--	--	29,025	--	--	29,025	--	29,025
Income tax recorded in equity	--	--	(7,256)	--	--	(7,256)	--	(7,256)
Net income recognised directly in equity	-	-	21,769	-	-	21,769	--	21,769
Profit for the year	-	71,893	-	-	-	71,893	-	71,893
Total recognised income for the period	-	71,893	21,769	-	-	93,662	-	93,662
Share issue	130,000	-	-	-	-	130,000	-	130,000
Dividends capitalised	23,500	(23,500)	-	-	-	-	-	-
Acquisition of subsidiary	-	-	-	-	-	-	52,737	52,737
Balance at 31 December 2006	362,396	64,483	48,117			474,996	52,737	527,733
Available-for-sale securities:								
-Revaluation	-	-	-	1,465	-	1,465	-	1,465
Income tax recorded in equity	-	-	-	(366)	-	(366)	-	(366)
Premises and equipment:								
- Revaluation	-	-	57,619	-	-	57,619	-	57,619
Income tax recorded in equity	-	-	(14,405)	-	-	(14,405)	-	(14,405)
Currency translation reserve	-	--	-	-	7,434	7,434	1,100	8,534
Net income recognised directly in equity	-	-	43,214	1,099	7,434	51,747	1,100	52,847
Profit for the year	-	102,567	-	-	-	102,567	4,565	107,132
Total recognized income for the period	-	102,567	43,214	1,099	7,434	154,314	5,665	159,979
Share issue	201,500	-	-	-	-	201,500	28,112	229,612
Decrease in minority interest after share proceeds	-	-	-	-	-	-	(73,063)	(73,063)
Balance at 31 December 2007 (Unaudited)*	563,896	167,050	91,331	1,099	7,434	830,810	13,451	844,261

(*) Based on Pivdennyi Bank's IFRS management accounts