

Annual Report
2011





The Babylonian Map of the World (end of 8th century – start of 7th century), a clay tablet, the British Museum, London
The map represents countries of Babylon, Armenia and Assyria.

ARMENIA

Geographic position

- Armenia (officially the Republic of Armenia) is a land-locked country in Transcaucasia. Geographically, it is located in North-East Asia but culturally and politically it is considered a European country.
- Length of state frontiers: 1400 km.
- Land area: 29743 square km, with land for agriculture accounting for 71.3 percent, forests 12.4 percent, special reserve land 7.7 percent and other land 8.6 percent.
- Minerals: ore and non-ore minerals, including coal, metal, bauxite, molybdenum, gold, silver, lead, zinc, pumice, marble, tufa, lime, perlite, basalt, salt.
- Water resources: Lake Sevan is one of the highest fresh water mountain lakes in the world, located 1916 m above sea level.

Population

- 3 million 274.3 thousand people as of January 1, 2012.
- Urban population: 2 million 096.0 thousand people.
- Rural population: 1 million 178.3 thousand.

Administrative structure

- 11 regions, including Yerevan.
- Capital: Yerevan (population 1 million 127.3 thousand)

Administration

- Republic.
- Legislative power: National Assembly.
- Executive power: Government of Armenia, headed by prime minister.

Currency

- Armenian dram (AMD).



THE CENTRAL BANK OF THE REPUBLIC OF ARMENIA

- History of the Central Bank of the Republic of Armenia dates back to October 25, 1893 when Yerevan branch of State Bank of the Russian Empire opened.
- In Soviet times the Central Bank was named a branch office of State Bank of the USSR.
- Following Independence, on April 27, 1993 the Supreme Council of the Republic of Armenia adopted the Law on the Central Bank of the Republic of Armenia which served a framework for the Central Bank to start.
- On November 22, 1993 the national currency, the Dram, was introduced.
- Since 1893 the Central Bank has had 21 governors.
- At present, the Central Bank implements monetary policy of the Republic of Armenia; is responsible for price stability; acts as megaregulator of the financial sector of Armenia by regulating and supervising activities and operations of all financial sector participants.



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Chairman's message

Dear Reader,

This is the Annual Report for the year 2011. It contains information on the reforms and our achievements which we had during the year as well as description of what we will need to do in 2012.

The year 2011 was prominent with high inflationary environment which was determined by abrupt international price increases of basic commodities and food products on the one hand and reported decline in agriculture in Armenia on the other. On the whole for the year, however, we saw success in terms of price stability and sustainable development of the financial sector.

Tightening of monetary conditions by the Central Bank and consistent reduction of budget deficit by the Government as well as increased supply of agricultural product and a policy designed to improve competition environment all contributed to the mitigation of inflation. As a result, as it was expected, the 12-month inflation became possible to reduce starting from the mid of the year. Moreover, in the third quarter our predictions were optimistic enough, permitting even to loosen monetary conditions to some extent. The inflation indicator came back to the confidence band as it reached 4.7 percent.

Participants of the financial sector saw positive results for the year. In particular, the banking system – the biggest player of the sector – posted profit (return on equity was 9.8 percent and return on assets, 1.8 percent) while assets and loan investments generated, respectively, 32 percent and 36 percent growth. Further increasing of financial intermediation in the economy was a key achievement. The value of assets of the banking system already hit the level of AMD 2 trillion which makes up approximately 54 percent of the year's GDP. A year before this figure was 45 percent and in 2008 it amounted merely to 28 percent. This points out to the expanded integration of real and financial sectors of the economy.

A mandatory car insurance scheme was introduced in 2011. This proved to be a process full of responsibility and risks. Yet it was carried out smoothly and, more importantly, it gives solution to the social aspect addressed by that scheme. Further work was done to create required infrastructures for the development and improvement of the scheme.

For the first time in Armenia in 2011 mortgage-backed corporate securities were issued by the National Mortgage Company through NASDAQ OMX-Armenia's primary placement facility, which was aimed to further stimulate the mortgage market in the country.

As part of pension reforms, work was done to introduce a voluntary funded pension contribution scheme in 2011 and a mandatory funded pension contribution scheme is intended to be functional since 2014, which is of paramount importance to Armenia.

The agricultural lending program launched this year was a social target, too.

In 2011 All-Armenian Bank began its operations with the purpose to shore up financial investments in areas strategically important to Armenia.

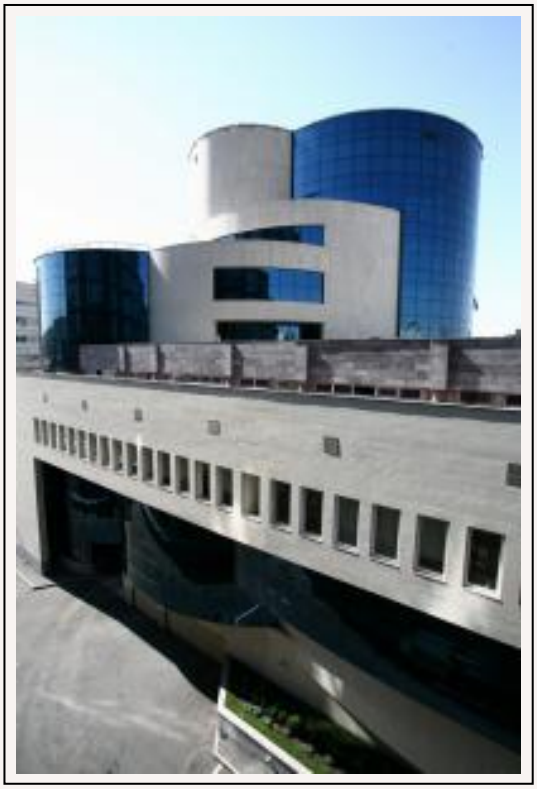
The encounters and achievements we had during the year make our responsibility more serious since forthcoming developments in global and domestic economies provide both challenges and vast opportunities.

On the path of fulfillment of goals and implementation of reforms, the Central Bank stays united and determined.



Chairman

ARTHUR JAVADYAN



GOVERNANCE AND ACCOUNTABILITY

MISSION AND OBJECTIVES OF THE CENTRAL BANK

According to the Republic of Armenia Law on the Central Bank, the primary goal of the Central Bank is price stability in Armenia. To achieve this goal, the Central Bank has a function of taking measures to attain price stability while developing, approving and implementing monetary policy programs. The Central Bank develops programs that are aimed to maintain financial stability of the country.

Mission of the Central Bank includes:

a) Be an internationally recognized institution that is independent, dynamic, prestigious, knowledge-based and onlooker of development trends in global financial system;

b) Maintain institutional ability to fast respond to the change in economic environment and effectively influence the economic processes;

c) Support on an ongoing basis the sustainable development of macroeconomic environment while being an important partner to the Government in facing economic challenges.

Objectives of the Central Bank include:

a) ensuring a stable and normal-functioning financial system, including creating conditions necessary for a stable, liquid, solvent and normal-functioning banking sector in Armenia;

b) creating and developing an efficient payment and settlement system;

c) issuing currency of the Republic of Armenia, and organizing and regulating money cycle;

d) organizing and regulating combat against legalization of criminal proceeds and terrorism funding;

e) creating conditions for protection of investors in securities and for building a framework for fair pricing of securities in the market, and for regulated activities of a sound, open, reliable and efficient securities market.

To achieve its objectives, the Central Bank:

a) takes up function to manage interest rates in dram markets and handle dram liquidity;

b) acts as a lender of last resort;

c) provides banking services to the Government and acts as financial agent and consultant to the Government;

d) licenses banks, payment and settlement organizations and other financial system participants, and regulates and oversees their activities for a unified supervision;

e) manages international reserves of the Republic of Armenia;

f) collects, compiles and publishes monetary and financial system statistics;

g) collects, surveys and analyzes information regarding legalization of criminal proceeds and terrorism financing; exchanges information and delivers that to local authorities and international organizations and, where provided for by international treaties of the Republic of Armenia, to competent authorities of other countries.

GOVERNANCE OF THE CENTRAL BANK

The Republic of Armenia Law on the Central Bank provides that the Board of the Central Bank is supreme management body of the Central Bank.

The Board consists of Chairman, Deputy Chairman of the Central Bank, and five Members. Chairman and Deputy Chairman are included in the Board *ex officio*.

Chairman of the Central Bank is the highest rank official of the Central Bank. Chairman of the Central Bank is appointed by the Armenian National Assembly upon recommendation of President of the Republic of Armenia, for a 6-year term. Chairman is responsible for fulfillment of the Central Bank objectives. Chairman coordinates and organizes the work and ensures the soundness of activities of the Central Bank; represents the Central Bank in the Republic of Armenia, other states

and international organizations; exercises authority not reserved to the competence of the Board. Where Chairman is absent or otherwise unable to act, such powers are to be vested with **Deputy Chairman of the Central Bank**, and where Deputy Chairman is absent or otherwise unable to act, such powers are to be vested with the eldest Board Member of the Central Bank. Deputy Chairman of the Central Bank is appointed by President of the Republic of Armenia, for a 6-year term. Chairman and Deputy Chairman as well as Board members cannot serve as a member of managing body of any party, be involved in activities other than scientific research, pedagogical and creative activities.

Board Members of the Central Bank shall be appointed by President of the Republic of Armenia for a 5-year term. Board Members cannot hold any other position in the Central Bank.

Board of the Central Bank

Regular meetings of the Board are held every two weeks, on Tuesday, pursuant to the schedule set by the Board at the opening meeting of the year. Extra meeting of the Board can be held at the request of Chairman, Deputy Chairman or at least three Board Members of the Central Bank. The Board approves Charter of the Central Bank, Monetary Policy Program of the Republic of Armenia, caps and interest rates on outright operations, loans provided and deposits attracted by the Central Bank, terms and procedure for reserve requirement with the Central Bank; enacts normative regulations of the Central Bank; issues, revokes or annuls banking licenses and other activity licenses; determines the procedure of licensing to banks and other entities; approves prudential standards for banking and calculation thereof; and exercises other authorities under law.



Board of the Central Bank *(left to right).*

Oleg Aghasyan
Aharon Chilingaryan
Nerses Yeritsyan
Arthur Javadyan
Vakhtang Abrahamyan
Ashot Mkrtchyan
Armenak Darbinyan

In 2011 the Board met 56 times and adopted 381 resolutions, of which 112 were normative resolutions and 269 were individual decisions. The normative resolutions and individual decisions covered such aspects of the Central Bank activity as approval of regulations supplements thereto, putting collector coins and notes into circulation, establishing normative acts for operations of the Central Depositary, insurance companies, credit organizations, reporting issuers, Bureau of Car Insurers of Armenia and All Armenian Banks; permitting the operations of money remittance organizations and their participation in the payment and settlement system, interest rates of the Central Bank operations in the financial market, approval of the design of collector coins issued by the Central Bank, issuing or revoking activity license to foreign exchange trades, issuing activity license to broker/dealer, pawnshop, credit organization, insurance and investment company operations and Bureau of Car Insurers of Armenia activities as well as decisions pertaining to Financial Monitoring Center and Audit Group of the Central Bank, and more decisions on various matters.

Commissions, committees and other consultative bodies are key pillars of the Central Bank governance, and their structure and competence are defined based on the scope of issues and area of activity. The commissions and committees of the Central Bank hold meetings and draw up minutes which are approved by Chairman of the Central Bank. Where appropriate, Chairman makes a decision and issues orders based on such minutes. There will be more useful information on commissions/committees of the Central Bank in appropriate sections of this Annual Report.

As a policy approver, the Board of the Central Bank has done much work in improving the legislative and regulatory framework aimed to the financial system stability and development. In particular, a handful of key reforming laws and legislative amendments proposed by the Board were endorsed by the National Assembly of the Republic of Armenia (see details in Section *Financial System Stability, Regulation and Development*).



The Executive Board addressing issues to be presented to the Board of the Central Bank

Executive Board of the Central Bank

The Executive Board is a consultative body adjunct to Chairman of the Central Bank, and conducts its proceedings through meetings. Normally, the Executive Board meets on a biweekly basis, on Tuesday following the day on which the Board's consecutive meeting was held.

Chairman of the Central Bank takes the chair of the Executive Board's meetings and, in his absence, Deputy Chairman does so.

Issues to be addressed by Executive Board Members in the meeting of the Board of the Central Bank are delivered to the Executive Board for consideration.

In 2011 the Executive Board met 18 times.



THE CENTRAL BANK ACCOUNTABILITY

In fulfilling its objectives, the Central Bank is independent from state authorities of the Republic of Armenia. The Central Bank maintains its accountability pursuant to the terms and procedure determined by the Republic of Armenia Law, the Central Bank strategy and internal rules and policies.

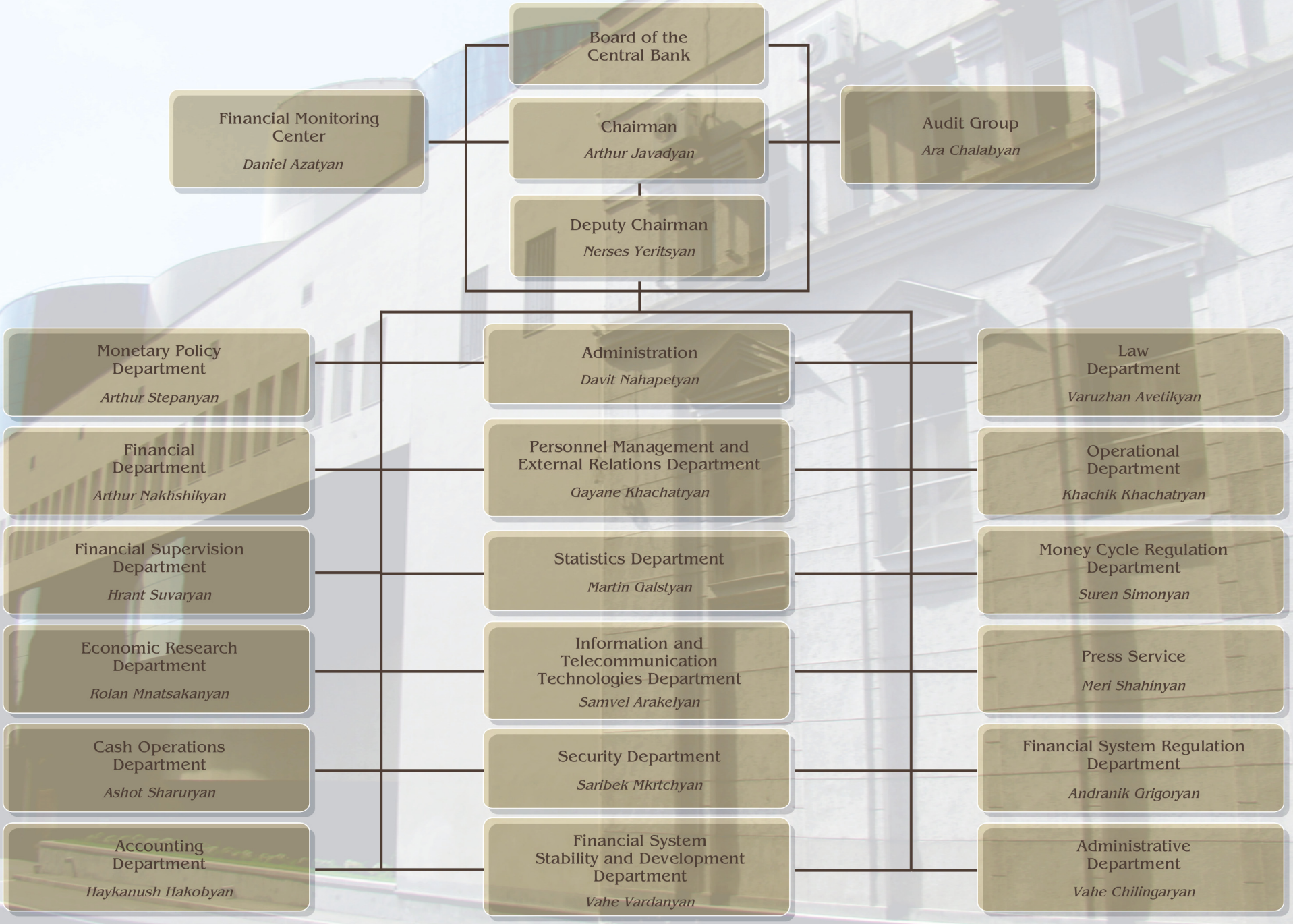
The Central Bank presents the *Monetary Policy Program* and *Status Report on Implementation of Monetary Policy (Inflation Report)* as well as *Expenditures Estimate and Capital Investment Program*, with performance papers, to the National Assembly of the Republic of Armenia.

In addition to the aforementioned papers, the Central Bank makes the following papers publicly available, such as: *Financial System of the Republic of Armenia: Development, Regulation and Supervision*, *Annual Report of the Central Bank*, *Financial Stability Report*, *Central Bank Bulletin*, *Central Bank Review*, *Central Bank Statistical Bulletin*, *Commemorative Coins of the Republic of Armenia*.

The Central Bank also ensures accountability through its official website (www.cba.am) which contains the Central Bank Development Vision, regular issues of periodical, the Board minutes and press releases on the refinancing rate, and other information relevant to the Central Bank operations and activity and the financial system as a whole.

Annual financial accounts of the Central Bank are another important component of accountability. Compliance of these accounts with International Financial Reporting Standards is verified each year by international recognized auditor.

THE CENTRAL BANK STRUCTURE





STRATEGIC DIRECTIONS

For 2011, the Central Bank prioritized the following objectives:

Developing and implementing monetary and foreign exchange policies and maintaining an increased level of transparency: the central priority was given to keeping the 12-month inflation within the confidence band and anchoring public expectations under intensified inflationary pressures in world commodity and food markets in the face of uncertainties transmitted from the external sector on the one hand and considerable easing of external and domestic inflation environments on the other.

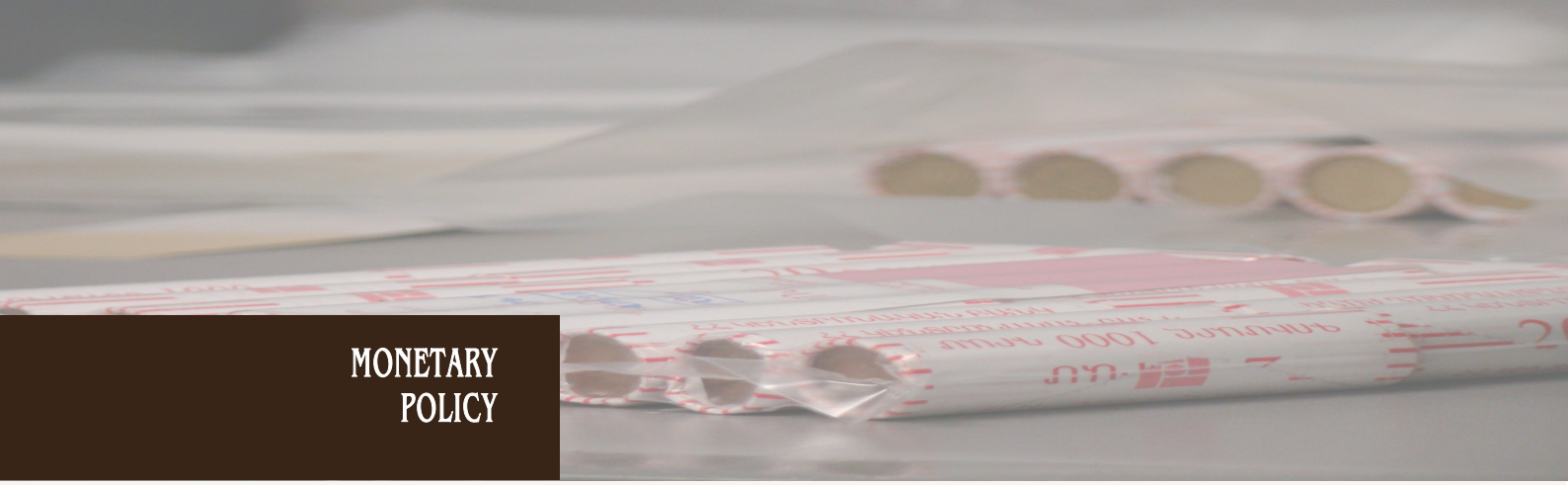
Improving the financial system stability and the regulatory and supervisory framework: increasing the level of financial intermediation in the economy, eliminating consequences of the crisis, enhancing the stability of the financial system by focusing on sustainable development of the financial market participants. One important achievement was considerable increase of the level of financial intermediation which, however, still lags behind the level reported for advanced countries and a number of East European countries. The banking system remains the largest player (holding as much as 91 percent of total assets) in overall financial sector in Armenia. The bank assets to GDP ratio has increased by 9.6 pp to 54.1 percent and the bank loans to GDP ratio has risen by 6.3 pp to 31.6 percent.

Improving measures to combat money laundering and terrorism financing: observing recommendations issued under the MONEYVAL Phase 3 Evaluation Report of Framework of the Fight against Money Laundering and Terrorism Financing in the Republic of Armenia, including adopting and elaborating relevant legal acts and presenting a status report; creating an administrative framework to raise effectiveness of collection and review of information based on reports and referrals on ML/TF.

Improving the payment and settlement system: the Central Bank did further work to improve non-cash instruments in response to increasing volumes of non-cash payments. A relevant legal framework was developed to sustain an accommodative monetary

policy and provide payment and settlement services by introducing new payment systems and improving the existing ones (the "repo and reverse repo" mechanism). Further efforts were directed to increase overall safety and reliability of Armenia's payment and settlement system.





MONETARY POLICY

According to the Republic of Armenia Law on the Central Bank, Article 4, the primary objective of the Central Bank is price stability, whereby the Central Bank contributes to the implementation of economic policy for a long-term stability and high economic growth. Price stability means a certain level of inflation which the Central Bank accepts as a target level of inflation or inflation target. In Armenia, the inflation target is set in medium-term expenditures frameworks of Armenian Government, the Republic of Armenia monetary policy programs as well as Sustainable Growth Program and the law on state budget. The Central Bank is independent in deciding on a strategy for conducting monetary policy and intermediate and operational targets as well as monetary instruments. Since January 1, 2006, the Central Bank has moved to an inflation targeting strategy, whereby a projected level of inflation serves an intermediate target and short-term interest rate serves an operational target. Interest rate (Refinancing Rate) of repurchase operations is the main instrument of monetary policy in the Republic of Armenia. The Board of the Central Bank determines the Refinancing Rate according to pre-announced annual timetable. For each upcoming year it is prepared in accordance with the reserve requirement calendar, while interest rates of the monetary policy instruments take effect on the first day after the refinancing rate has been determined[1].

The measures to attain the inflation target set for 2011 (4 ± 1.5%) were outlined in the monetary policy programs, and its implementation, in the quarterly inflation reports.

The monetary policy in 2011 was again implemented under high inflationary environment. The first quarter of the year saw intensification of the inflation environment, which had been high already since the second half of the previous year, due to *increased international prices of primary goods and food products* (in February the UN food price index hit a record 238), reduced supply in agriculture resulted from a reported downfall in this

[1] *Details on the monetary policy are presented in the quarterly paper Status Report on Implementation of Monetary Policy Program (Inflation Report), which is available at www.cba.am.*



Starting from January 2011 the Central Bank gradually tightened monetary conditions.

sector of economy of Armenia as well as second-round effects of high inflation and shaped high inflationary expectations. As a result, the 12-month inflation reached 11.5 percent in end-March, the highest level recorded in the last three years.

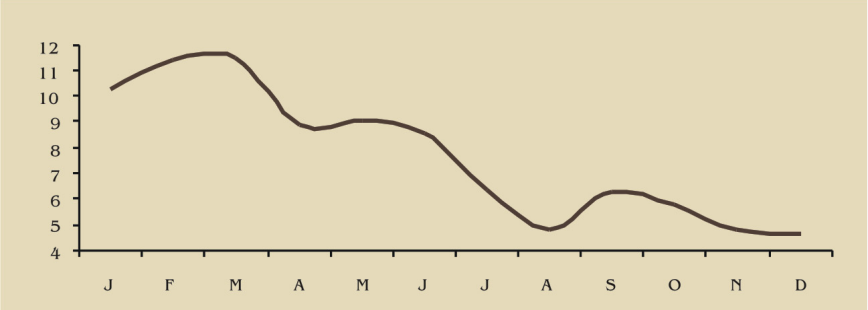
In early 2011, the Central Bank began gradually tightening monetary conditions by raising the refinancing rate in January-April a total of 1.25 pp to 8.5 percent with the aim to mitigate second-round effects of high inflation and expectations as well as get the inflation indicator closer to the target.

In the period April-May 2011 a seminar with the topic "Improving Monetary Policy: inflation targeting and implementation" was organized in Armenia in collaboration with IMF. A cooperation program derived from this arrangement was developed and now is carried out to improve the "Forecasting and Analysis System" and move to a full-fledged inflation targeting regime. The first phase of the program envisages training of some employees in the IMF (Washington D.C) while the next phases are expected to use knowledge and experience of these employees in formulating and implementing monetary policy of the Central Bank.

The program also boasts a far-looking objective, i.e. making monetary policy a model example among central banks of CIS countries.

In the course of the next three quarters the inflation environment gradually mitigated and the year ended with an annual inflation indicator of 4.7 percent (which is within the confidence band). Note that the downsloping trajectory of the 12-month inflation was mainly attributable to the lagged influence of monetary conditions tightened in early 2011, some stabilizing of prices of food products and primary goods in world markets, contractionary fiscal policy implementation and fallen prices of

domestic agricultural product as a result of increased output volumes reported in agriculture (in April-September 2011 a 4.4 percent of deflation was recorded versus 0.4 percent of inflation observed for the same period of time the year before).



In such a situation, starting from May 2011 the board of the Central Bank evaluated that the likelihood of inflation environment re-expanding was very low, and that curbing that environment through then applicable interest rates was possible. Based on this judgment, in the period May-August the Central Bank left the refinancing rate unchanged while in September the Board even lowered it by 0.5 pp to an 8 percent level. The Central Bank continued implementing a neutral monetary policy in the fourth quarter, too, while believing that the 12-month inflation would most likely rest within the confidence band of 4%+1.5 pp in the forecast horizon, which actually happened at the end of the year.

In 2011 the annual indicator of economic growth was estimated by the Central Bank to be in the 4.1 - 4.5 percent range. Increased output in industry (17.0 percent) and services (3.1 percent) again contributed to the economic growth, whereas construction and agriculture reported somewhat different development patterns compared to the trends observed in the year before.

The Monetary Policy Committee is responsible for reviewing and evaluating the previous week's monetary policy, the situation in banking sector and financial market, as well as the indicators of the Central Bank's operations and relations with State Budget.

The Monetary Policy Committee is set to review and evaluate the Central Bank Statistics Department's and the Republic of Armenia National Statistics Service's observations concerning inflation estimations of the previous 10 days. The Monetary Policy Committee's meetings are held each Friday at the Central Bank. In 2011 the Monetary Policy Committee met 50 times.

STATISTICS

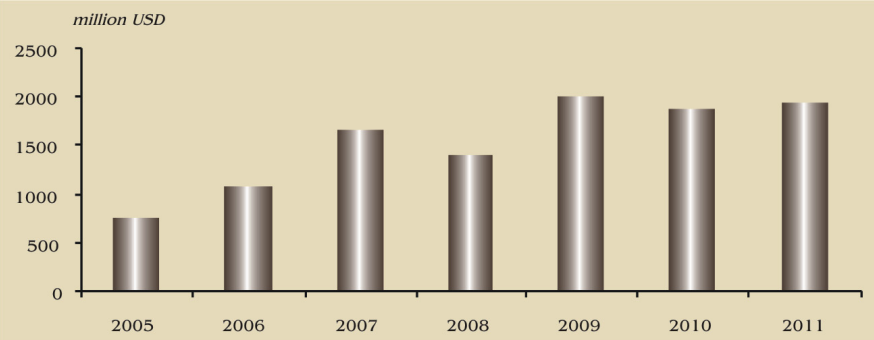
During 2011 the Central Bank revised and further improved the methodology of collection of data from banks and credit organizations. Classification of loan portfolio by sectors was aligned with the Manual on Statistical Classification of Economic Activities in the European Community, NACE rev.2, making the calculation of FISIM easier when measuring GDP by production method. The change in classifier was made in regard to reports filed to the Central Bank and the information bank at the Credit Registry. In 2011 an information system for the mandatory car insurance scheme was established.

Since 2011 the Central Bank is charged with preparation of the statistics of the Balance of Payments, International Investments Position and Foreign debt (external accounts). The Central Bank is responsible for drawing up of external accounts, development of data in compliance with a new BPM6 manual and revision of historical series of previous years.

During 2011 the Central Bank tested queries on assessment of inflation expectations, the results of which can be used to increase the effectiveness of monetary policy. The Central Bank developed a concept on making sectoral research and analysis and it improved the methodology of all sample research carried out by the Statistics Department.

INTERNATIONAL RESERVES MANAGEMENT

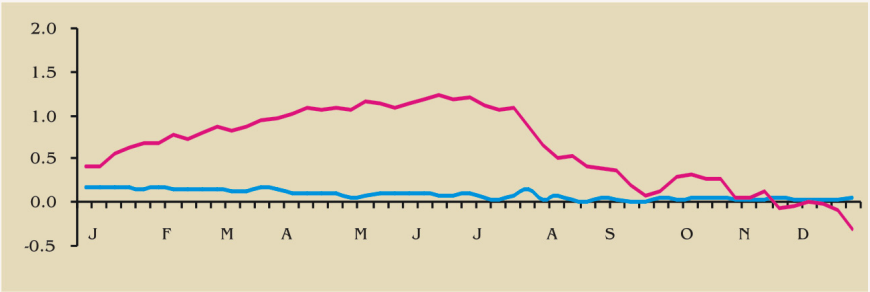
In 2011 Armenia's international reserves grew by roughly USD 67 million against the previous year and reached USD 1932.5 million at the end of the year.



Armenia's international reserves

During 2011 the Central Bank remained committed to a strategy of maximized yields under as low risk exposures as possible when managing Armenia's international reserves. The results of ex-post analysis suggest that the decision on benchmark allocation of reserves for the period under review has been fully justified in terms of the risk to yield ratio, in comparison with relevant indicators of possible benchmarks.

Attributable to the measures taken by governments and central banks in the U.S.A. Japan and Euro-area countries to overcome financial and economic crisis as well as low inflation expectations, interest rates in 2011 remained at record low, which in its turn reflected the level of profitability on international reserves of Armenia.



US and German treasury bill yields

US 6-month treasury bill yield

German 6-month treasury bill yield

Yields on Euro-area and U.S. treasury bills even posted decreases as a result of proactive public expenditure cut policies implemented in advanced countries. Even more so, in December 2011 yields on treasury bills of Germany and Netherlands, which traditionally boasted as 'safe haven' territories, plunged beyond the zero level and reported negative yields, accordingly.

The reporting year was characterized by high interest rate volatility in a number of European countries and profound downgrades of the U.S.A. and many European countries by major credit agencies, driven by sovereign debt issues in the U.S.A. and some South European countries. These events have not affected Armenia's international reserves negatively as investments were only made in instruments highly reliable and less sensitive to such risks.

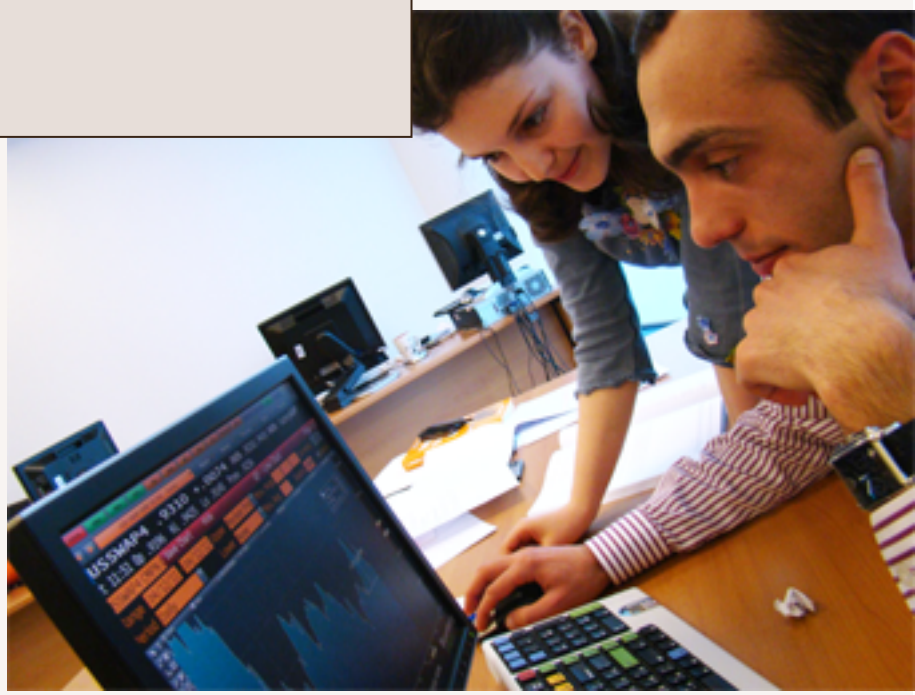
Investment Committee

The Investment Committee is an authorized decision-making body within the Central Bank structure. The Committee supervises and coordinates investment activities, evaluates the results of financial analyses in compliance with investment guidelines approved by the Board of the Central Bank.

The Committee is set to address issues of strategic and tactical management of international reserves as well as to perform monitoring of ongoing investment activities.

Normally, the Committee's meetings are held once a month.

In 2011 the Investment Committee met 10 times and adopted 8 decisions.

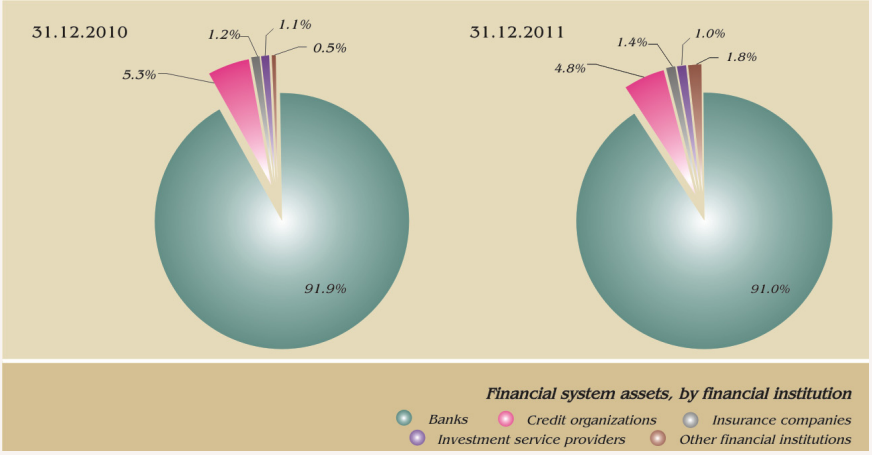




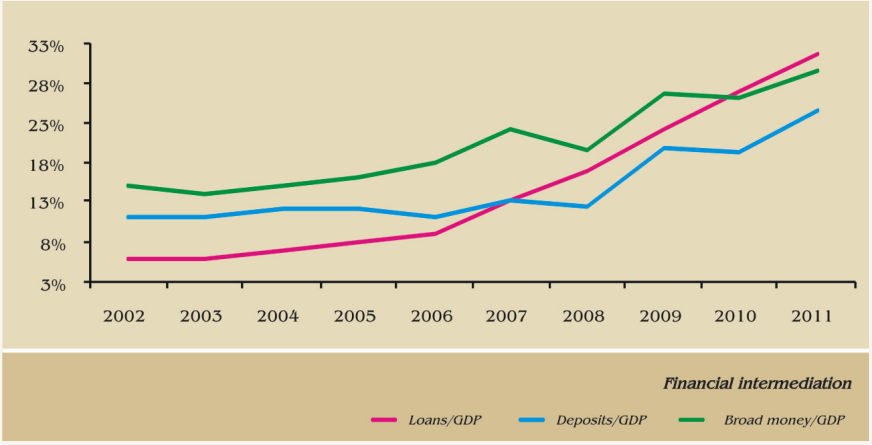
FINANCIAL STABILITY, REGULATION, SUPERVISION

Rather active during 2011, Armenia's financial sector maintained the area-specific risks within a comfortable territory of manageability while demonstrating high flexibility.

The banking system is the largest player in the financial sector as it holds 91 percent of assets of overall financial sector.



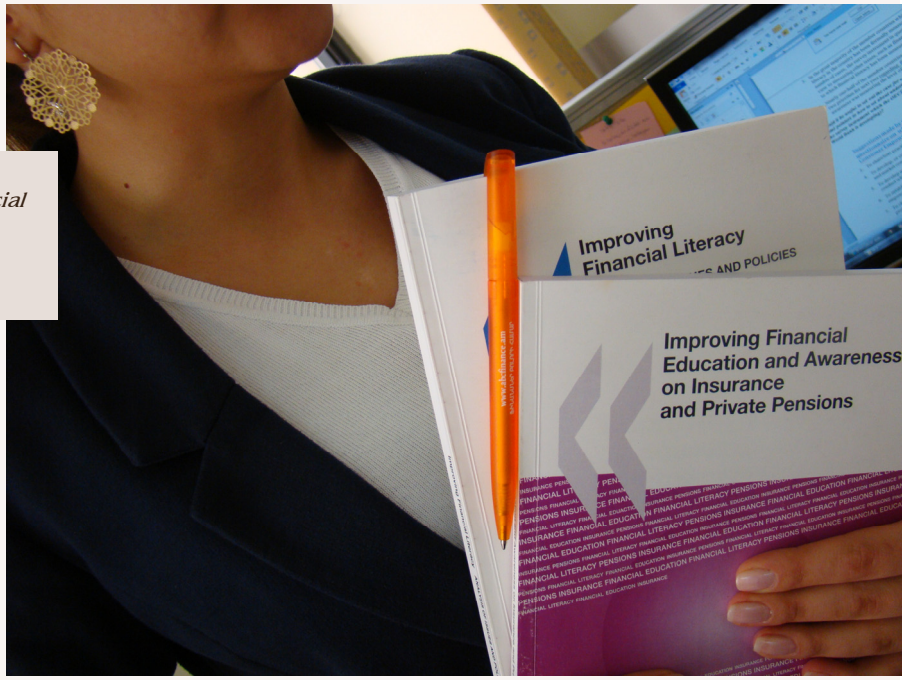
In 2011 the banking system posted 32.4 percent growth of assets and 11.6 percent increase of capital. Profitability indicators of the banking system were as follows: return on assets (ROA) posted 1.8 percent increase and return on equity (ROE), 9.8 percent increase.



Financial intermediation of the banking system has risen significantly. It however lags behind the level of financial intermediation reported in East European countries. In 2011 the bank assets to GDP ratio rose by 9.6 pp to 54.1 percent, and the bank loans to GDP ratio grew by 6.3 pp to 31.6 percent.

Other participants of the financial sector posted increases of main prudentials as well. Specifically, credit organizations have reported increases of total capital by 30.2 percent; liabilities, by 50.3 percent; assets, by 42.0 percent. The growth of respective indicators reported by insurance companies was 12.8 percent, 32.7 percent and 23.0 percent. Capital of investment companies has increased by 1.1 percent and liabilities and assets have grown by 13.7 percent and 11.6 percent, respectively[2].

The regulatory framework of the financial system is revised and improved on an ongoing basis.



[2] *See details on the financial system in the Armenian Financial System: Development, Regulation and Development, 2011, and the Financial Stability Report, 2011, published by the Central Bank (www.cba.am).*

Financial System Stability and Development Priorities in 2011 included:

- *Developing a concept paper on crisis management*

The paper was further amended to contain main actions pertaining to crisis management, in reference to the concept paper "Maintaining The Financial System Stability" which was developed back in 2005 and which considered both non-crisis and crisis conditions. It specifically contained amendment with regard to prevention and management of crises and essential policy components.

- *Efforts to prepare for the introduction of the Basle III*

Work on introducing the Basle III will continue over 2012.

- *Further work on designing a hybrid payment system*

The Central Bank continued working on the design of a hybrid payment system (see in subsection Payment Systems).

- *Further commitment to the creating a sub-legislative framework for pension and investment funds*

Once the pension reforms package took effect, the Central Bank of Armenia launched and now has mainly completed the developing of necessary sub-legislative acts within the scope of its competence. Since the voluntary component of a cumulative pension system was in effect from January of 2011, the Central Bank first developed regulatory papers containing procedures and requirements for investment companies, including for creation and activity of pension funds. Specifically, the Central Bank established a procedure for registration (operational rules) of an investment fund, which is vital to creation of such funds and their further functioning. Further procedures were adopted for granting permission for investment fund manager activity, including a simplified procedure for re-registration and re-licensing of investment companies. Aspects of qualification and professional integrity required for the management of investment fund managers as well as individual fund managers have been regularized under those procedures. Minimum statutory capital and total capital requirements, the calculation of these prudentials as well as the manager's share in any of its funds under management

have been established. Unified rules for measuring of assets of investment and pension funds have been established in order to reduce risks associated with the abuse in measuring assets. Regulations further set investment limits in order to make sure diversified investments are in place. A procedure for determining the value of net assets of investment funds has been established for the calculation of profit tax due. Further changes and supplements were made to the Central Bank Regulation 8/03 to make sure information on investment funds is accessible to the participants of these funds and to use unified principles for yields matching. Another regulation (the Central Bank Regulation 10/17) has been developed to provide criteria for calculation of the yield of assets of the pension fund and dissemination of information about yields. Also, the Central Bank of Armenia has established the minimum total value of shares purchased by non-qualified investors which invest with qualified investment funds.

In its capacity as regulator and supervisor of financial institutions being the participants of the Armenian cumulative pension market, the Central Bank joined, since September 2011, the International Organization of Pension Supervisors. As a managing member to IOPS, the Central Bank has an access to all thematic debates addressed within the organization, and enjoys the opportunity to exchange field information with counterparts, hold dialog with relevant authorities of other countries on financial policy issues of private pension fund system and benefit from best international experience in that field.

- *Taking further measures in order to explicate the benefits of mandatory insurance and pension reforms, in the context of protection of consumer interest.*

As part of explication of mandatory car insurance scheme, the Central Bank:

- ✓ designed a Bureau website and put it into operation;
- ✓ developed a booklet and ticket describing the mandatory car insurance scheme and distributed them nationwide;
- ✓ aired television and radio broadcasts about the benefits of mandatory car insurance scheme;

- ✓ created a dedicated page in the website "Finance for Everyone" (www.abcfinance.am) and explicated the scheme and use of mandatory motor liability insurance contracts;
- ✓ arranged seminars for reporters dedicated to mandatory motor liability insurance contracts.

As part of explication of pension system reforms, the Central Bank:

- ✓ designed booklets describing the need for pension system reforms;
- ✓ created a dedicated page in the website "Finance for Everyone" (www.abcfinance.am) and furnished the site with description material as appropriate;
- ✓ called for cooperation with the Pension System Information Center;
- ✓ launched awareness campaigns in regions of Armenia in collaboration with PSIC and the project of Pension System and Labor Market Reforms, including written materials and seminars.

In 2011 the Central Bank further worked on revising and improving the regulatory framework of the financial sector. In pursuit of consistent development of the banking, insurance and securities markets, a number of reform laws were passed at the National Assembly of the Republic of Armenia during 2011:

1. "Law on Supplement to the Republic of Armenia Law on Income Tax" and "Law on Amendment to the Republic of Armenia Civil Code"

These laws are aimed to deal with tax and legal aspects in connection with confiscation of the item of pledge. Before, under the applicable tax legislation, the pledged property, when transferred onto the ownership of the bank for its further marketing, was seen as sale of that property by the pledger, which was supposed to entail an obligation to pay income tax. As a tax agent, the bank then had to pay the income tax at its own expense. Furthermore, it was unclear as to when the amount of

difference between the value of confiscated property and covered liability would be handed back to the pledger.

The law has established a new mechanism with which to tax income of the individual received as a result of confiscation of the pledged property extrajudicially and sale-off of the one.

As provided for by the law, income from the sale-off of the pledge by the pledger involves the amount of positive difference between the marketed price of and covered liability for the pledged property.

So, three possible options were developed for determining marketing price of the pledge:

1) **Option 1** – the property pledged shall be sold off to a third party within 6 months after it has been transferred onto the ownership of the bank. In this case the price at which the property is sold off will be the marketing price of that property, and where the sell-off price is unreasonable below the market value of that property, the market price of the property will be the one at which that property can be sold off.
2) **Option 2** – the bank has not sold off the property pledged within 6 months after it has been transferred onto the ownership of the bank. In this case the market price of the last day of a specified 6-month period will be the sell-off price of that property.
3) **Option 3** – there is a preliminary signed written agreement in place between the bank and the pledger. The two parties can reach an agreement that where the property pledged is transferred onto the ownership of the bank, the market price determined as of the day that property has been transferred onto the ownership of the bank will be the sell-off price of that property.

The calculation of the above said 6-month period does not include the period to which extent the bank has introduced attachment to the property transferred into the bank's ownership as part of a civil, criminal, bankruptcy or administrative procedure.

2. "Law on Supplement and Amendment to the Republic of Armenia Law on Bankruptcy" and "Law on Supplement to the Republic of Armenia Law on Execution of Legal Acts"

- The laws, accordingly, contain provisions on satisfying creditor claims, backed by pledge, surety and guaranty, in the bankruptcy process, without the moratorium in effect. This means that the financial organization or person in question has the right to satisfying its claim without having to wait for the completion of the bankruptcy process.

- In the meantime, two possible options have been established for protecting interests of other creditors involved with the case of bankruptcy the debtor is in, as follows:

  - where creditor is to use his right to benefit the marketed pledge prematurely (without having to wait for the accomplishment of moratorium), he is not allowed (nor will be allowed in future) to get satisfaction of his claim in respect of other property of the debtor if the claim is in excess of the value of the pledge;

  - where creditor is not using his right to benefit the marketed pledge prematurely, he will get satisfaction of his claim after the moratorium, in this case benefiting from both the marketed pledge and other property of the debtor.

3. "Law on Amendment to the Republic of Armenia Law on E-Communications" and "Law on Supplement to the Republic of Armenia Law on Circulation of Credit Information and Operations of Credit Bureaus"

The amendment to the Republic of Armenia Law on E-Communications provides that making credit information on their client (as such, this information involves data on the client indebtedness for phone calls) available with credit bureau by telecommunication operators does not mean public disclosure of personal information.

The amendment will enable telecommunication operators to provide information on their client's debt to credit bureaus.

Once the draft to the Republic of Armenia Law on Circulation of Credit Information and Operations of Credit Bureaus is endorsed, the credit bureau must include in its credit report information on which data were used to compile information that is available with the credit bureau, taking also into account that the credit bureau will, from now on, collect information not only about clients of financial organizations but also about other clients involved.

The amendment to the Republic of Armenia Law on Circulation of Credit Information and Operations of Credit Bureaus was necessity for prevention of problems that might arise in connection with preparing complete credit report by credit bureaus as well as for compilation and development of credit information of persons not having credit history. Where needed, the Central Bank will define a list of data to be included in the credit report, to make sure these reports are uniform.



4. "Law on Supplement to the Republic of Armenia Law on Payment and Settlement Systems and Payment and Settlement Organizations"

The amendment to the said Law established a minimum total capital prudential for payment and settlement organizations, introduced clearer terms and conditions for creation of payment and settlement organizations, their admission to memberships, creation of payment and settlement unions, as well as outsourcing and licensing procedures. Organizations can now deal with money remittance without having to establish branch office. Furthermore, types of services are now more clearly defined and best aligned with the EU legislative requirements, taking into consideration peculiarities of the domestic financial sector. Aspects of sanction with regard to payment and settlement organizations have been regularized.

In 2011 the Central Bank also made some sub-legislative amendments.



Licensing and Supervision Committee

The Licensing and Supervision Committee is set to address such aspects as:

a) granting preliminary consent to creation of banks and branch offices of foreign banks; registration and/or licensing of banks and branch offices of foreign banks;

b) registration of branch offices, representations of banks, representations of foreign banks;

c) registration of operational rules of regulated market operator and Central Depositary;

d) licensing of other participants;

e) registration of changes as required under the Law on Banks and Banking and the Central Bank Regulation 1;

f) certification and professional integrity of bank managers (excluding heads of structural units) and other participants eligible for the Central Bank licensing;

g) qualification of investment service providers, regulated market operator, Central Depositary managers and natural persons as investment service providers;

h) registration of prospectus of securities;

i) legislative infringements by banks, and explanations/objections by the bank, if any;

j) sanction, whether or not applied to the bank and/or bank manager;

k) legislative infringements by other parties registered or licensed or otherwise controlled by the Central Bank; and their explanations/objections, if any; and sanction, whether or not applied thereto;

l) issues pertaining to aspects contained in points a) to k) above;

m) issued derived from other aspects under the Central Bank competence.

The Licensing and Supervision Committee has its proceedings through meetings which are convened as per necessity but not less than once a week.

In 2001 the LSE met 62 times.

The Central Bank continued carrying out both off-site and on-site inspections of financial sector participants, aimed at preventing unjustified risks, combatting money laundering and terrorism financing, protecting consumer interests and further aligning the participants' operational activity with legislative requirements. During 2011 the Central Bank carried out 235 on-site inspections, of which:

- 7 all-purpose inspections and 13 targeted inspections at banks,
- 6 all-purpose inspections and 1 targeted inspection at a credit organization
- 3 all-purpose inspections at insurance companies
- 38 inspections at insurance brokers
- 4 inspections at investment service providers
- 163 inspections at other financial system participants (exchange offices, pawnshops, payment and settlement organizations and etc.).

Infringements revealed through supervision were remedied. The combating money laundering and terrorism financing, the protection of consumer interest and market conduct requirement has been in the focus of the examinations, along with risks to financial organizations.

Large-scale awareness campaigns on protection of consumer interest and financial education of target audience continued during 2011. Work was further done to develop a dedicated website "Finance for Everyone" (www.abcfinance.am). Cooperation with the "Civil Education Center" addressed problems specific to the financial sector. Other educational projects were also implemented.

RATING OF COMMERCIAL ORGANIZATIONS

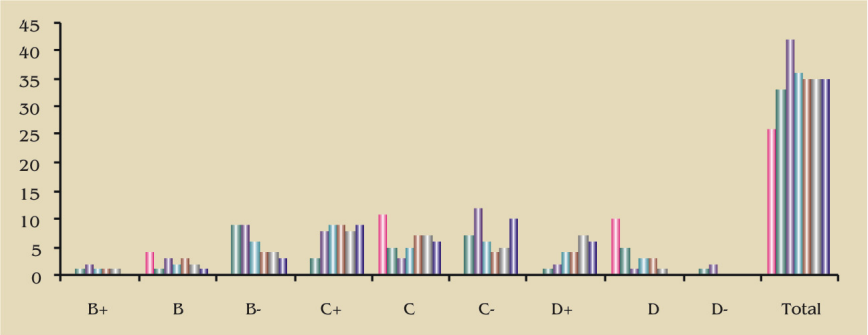
Since 2004 the Central Bank has embarked on granting credit rating to commercial organizations in Armenia. As early as September of 2005, credit ratings to the first 16 organizations were released.

In early 2011 there were 35 rated organizations; this number stayed the same at the completion of the proc3ss. As a result, the rating of 19 organizations remained unchanged, 13 organizations were downgraded and 3 upgraded.

The Central Bank grants credit rating to commercial organizations in order to demonstrate their ability to service (repay) attracted liabilities in a timely manner and in full to provide objective and impartial evaluation of their credibility.

Ratings are granted by use of letters of Armenian alphabet, with the letter + (A+) being the highest rating and the letter (F) being the lowest rating. Ratings from A+ to C - (+ to Գ -) are considered investment ratings, and ratings from D+ to F (Դ+ to) are considered non-investment ratings, according to Procedure on Commercial Organizations Rating by the Central Bank. Rating is applied to enterprises and companies from various sectors.

In 2011 the Rating Committee met 4 times and adopted decisions on introducing changes to the methodology of granting rating to individual organizations.



Commercial organizations rated in the period 2005-2011, by rating

As of yearend 2011, no organization was granted rating from category A. Four organizations received rating from category B (7 in the previous year); twenty-five organizations received rating from category C (20 in the previous year); and the number of organizations which received rating from category D was 6 (8 in the previous year).



PAYMENT AND SETTLEMENT SYSTEM

In 2011 the Armenian payment and settlement system developed in consideration of a number of circumstances. Work in the payment and settlement area was done in two main directions, pursuant to the Central Bank Development Vision.

1. Maintaining a sustainable and reliable payment and settlement system and increasing the volume of non-cash payments

The Central Bank established minimum requirements to automated self-service devices to make sure non-cash payments are executed in a safe and reliable manner.

The payment of pension on a non-cash basis started in 2011, and to this effect the Central Bank introduced changes and supplements to relevant regulation and policies.

In 2011 there were 21 commercial banks and 10 payment and settlement organizations in Armenia that offered their services.

At the end of 2011 the accounts opened in the banking sector numbered 2.2 million. The number of payment cards has increased by 34.02 percent, relative to end-2010, and amounted to 978 thousand cards. The value of operations executed with cards has increased by 32.3 percent and make up AMD 739 million and the number of transactions has increased by 29.8 percent and reached a total of 14.6 million transactions. The growth of these indicators was mainly driven by the increased demand for financial services.

2. Improved quality service and broader spectrum of reliable service offered by payment and settlement organizations

In the period under review the Central Bank introduced more payment systems and improved the existing ones, so that they are able to accommodate flexible monetary policy instruments and provide payment and settlement services on the whole.

The system "Repo/Reverse Repo" is set to announce auctions, conclude, execute and redeem transactions between the Central Bank and the system participants. In 2011 the system was tested and input, and it is expected to put into operation in 2012.

In 2011 the Central Bank worked on getting deposit operations automated in the electronic payments system.

More banks and payment and settlement organizations were granted permission to join international payment systems.

The Central Bank supported the Central Depositary of Armenia to start working on inputting the system "Depend". The system is intended for running registries of securities, custody transactions, clearing and final settlement procedures at the Depositary. The system will enable to expand the spectrum of services.

The Central Bank and NASDAQ OMX-Armenia JSC worked together to design procedures for placement, circulation and final settlement of corporate bonds issued by the National Mortgage Company CJSC. Procedures for over-the-counter transactions executed on the DVP (delivery versus payment) principle were agreed upon.

In 2011 the Armenian Card CJSC carried out work to re-furnish the system aimed at increasing the system's information security and strengthening payment facilities in the Internet environment. This will result in increased system capacity which is to foster e-commerce[3].

[3] Detailed report on the payment and settlement system is provided in the quarterly publication "The Central Bank Review", in the annual report "Armenia's Financial System: Development, Regulation, Supervision" and in the "Financial Stability Report". See the Central Bank's website at www.cba.am.

CASH MONEY CYCLE

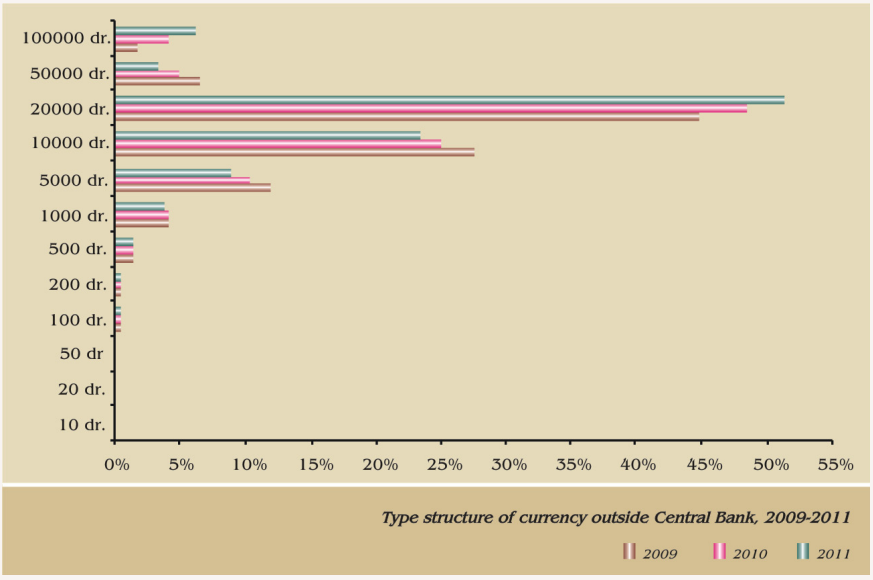
In 2011 the cash cycle of the Central Bank grew by 14.5 percent. The demand for cash by nominal value behaved differently.

Like in the previous year, the volumes of banknotes with nominal value 20000 and 100000 drams in cash cycle trended upward. Particularly, the volume of banknotes with nominal value 20000 has increased by 21.4 percent and at the end of the year it reached 51.3 percent of currency outside the Central Bank.

Since introduction, the volume of banknote with nominal value 100000 drams has increased and made up 6.2 percent of currency outside the Central Bank, at the end of 2011.

The shares of other nominal values have decreased in the structure of currency outside the Central Bank, as was the case in the previous year.

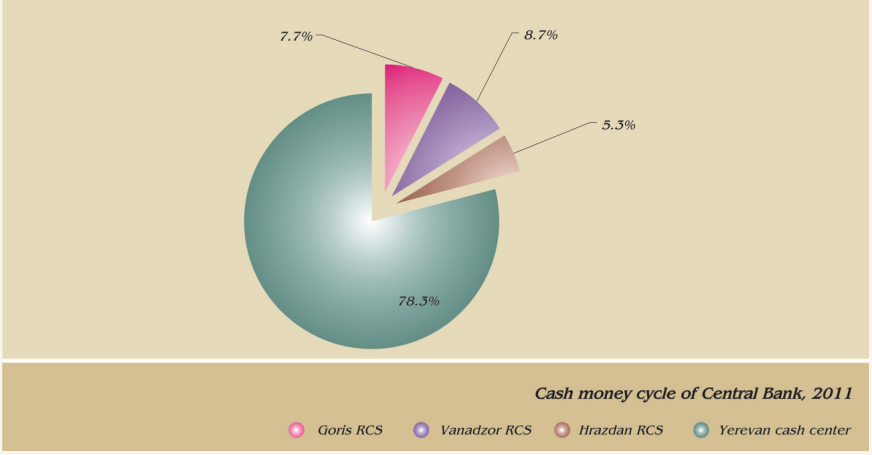
The total volume of coins with nominal value 10 to 500 drams grew during the year by 12.5 percent. The volumes of coins with nominal value 10 and 20 drams reported highest growth rates.



Type structure of currency outside Central Bank, 2009-2011

As a result of the above change in the type structure of currency outside the Central Bank, *average conventional note*[4] amounted to 2687 drams. Furthermore, average banknote amounted to 9047 drams and average coin, 103 drams.

During the year the Central Bank provided cash services to the clients through its central office as well as regional cash centers.



In 2011, like in previous years, cash outflow remained the main operation carried out by regional cash centers: cash outflow made up 93.0 percent of total RCC cash cycle.

To improve cash service of its clients, the Central Bank further had its operations automated.

In 2011 worked was in progress to develop a unified information system for cash management within the Central Bank. The system is intended to incorporate all existing electronic systems and will have more processes and functions automated. Collection organizations, commercial banks, the Ministry of Finance and other Central Bank clients will be expected to join this system. The system is designed to facilitate electronic circulation of documents, process management, cash flow monitoring as well as creation, survey and review of database. The work for the introduction of the system will continue the next year.

[4] *The calculation of the average conventional note includes nominal values in the range of 10 drams to 100000 drams.*

Work was done to identify banknote series to make sure banknotes with different nominal values, design patterns and security features, placement and numbering are classified. The identification of banknote series will help people to check up banknotes easily and will enhance awareness of security features.

In 2011 a new series of banknote with nominal value 1000 drams was put into circulation, and banknotes with nominal values 5000, 10000 and 20000 drams with an improved design are expected to put into circulation in 2012. Old banknotes with these nominal values will remain a legal tender.



Financial Sector Stability and Development Priorities in 2012

- *The Central Bank will carry out work to introduce Basle III aimed to enhance the financial system stability and curb risks to the banking system. Basle III is the integrity of recommendations to make changes to internationally accepted requirements pertaining to capital, liquidity and other fields of banking supervision. The main goal of this arrangement is to ensure the stability of the global financial system by establishing stricter requirements to bank capital and liquidity standards.*
- *The Central Bank will continue working on a new bank risk assessment framework which is designed to produce an aggregate measure of bank risks. The framework is expected to make a particular focus on key business processes within banks.*
- *Main provisions pertaining to unified supervision are expected to be regularized during the year.*
- *The Central Bank is expected to develop a methodology that determines the market boundaries (segments by service, geography) and to develop a procedure that defines market abuse.*
- *Plans include determining main economic prudentials for All-Armenian Bank' operations and a procedure for filing financial reports to the Central Bank.*
- *The Central Bank will remain proactive in the work on developing a regulatory framework for pension and investment fund activities.*

The Central Bank will collaborate with NASDAQ Group companies to design software that registers participants of the mandatory cumulative pension component in Armenia. Work will include developing relevant regulations and policies as well as testing of individual system modules.



Work was further carried out to achieve goals set forth in the 2010-2013 national strategy of combating ML/TF in the Republic of Armenia, aimed at introduction of regulations and policies broadly in compliance with FATF recommendations, implementing risk-based principles of the mechanism for combating ML/TF providing equal compliance with the requirements of anti-money laundering and combating terrorism financing legislation by all reporting entities, the strengthening and expansion of cooperation at domestic and international level, training of staff of Financial Monitoring Center of the Central Bank and other bodies engaged in combating ML/TF.

As national compiler, analyzer and disseminator of information relating the combating of ML/TF, to exercise its authorities the FMC is authorized to receive reports from reporting entities and to collect information from supervisory and other relevant bodies. The received information is analyzed and when necessary disseminated to law enforcement agencies or supervisory bodies in the manner defined by law.

In particular, reporting entities, domestic and foreign counterparts as well as mass media and other bodies concerned are a source of information. The analysis by the FMC includes additional inquiries made to and receive information from national law enforcement and supervisory authorities. The results of analysis are provided to law enforcement and supervisory authorities and foreign counterparts as appropriate, so that they are able to rake measures when required.

For the purpose of improving the mechanisms of combating ML/TF and further aligning anti-money laundering legislation to international standards, the FMC, in collaboration with other competent parties, drafted a package of amendments to the Republic of Armenia Law on Combating Money Laundering and Terrorism Financing and other AML/CTF legislation (a total of 14 laws) back in 2011. After remarks and recommendations with regard to the draft package were taken into consideration along

with evaluation from small and medium size enterprises, competition, budgetary, environmental, healthcare, social security and anti-corruption authorities, the package was submitted to the Government of Armenia.

There were 5 cases instigated during 2011 resulting in 7 persons convicted of legalization of criminal proceeds. Other cases were instigated for fake loans, appropriation and legalization of funds, production of forged bank cards which were used to withdraw money, a major case of appropriation of money from a legal entity, forged documents and appropriation of money as a result.

	2006	2007	2008	2009	2010	2011	Total
FMC referrals to law enforcement bodies	2	11	11	9	23	17	73
Criminal cases instigated upon FMC referrals	2	2	2	1	5	1	13
Information which the FMC requested from law enforcement bodies	-	12	23	13	15	33	96
Information which law enforcement bodies requested from the FMC	-	13	19	39	53	58	182
Criminal cases instigated at the initiative of law enforcement bodies	2	2	5	9	8	9	35
Criminal cases instigated, total	4	4	7	10	13	10	48
Sentences rendered	1	0	0	7	3	5	16
Funds suspended upon the Central Bank Board decision	0	0	USD 802.000	USD 1.100.000	AMD 345.000, USD 290.000	0	
Funds subject to confiscation (AMD)[5]	388.000	0	0	AMD 53.824.860, EUR 25.200	514.026.500	415.517.535	

[5] *In addition to the funds subject to confiscation to the budget as shown in the table, in 2011 a claim of AMD 83535019 was satisfied to the benefit of a third party by a conviction rendered on a money laundering case.*



International Cooperation

In the period under review international cooperation of the FMC remained strong as it further enhanced links with international/foreign counterparts.

The FMC was requested to make amendment to a number of papers, including FATF recommendations developed by international institutions (FATF, MONEYVAL, the Eurasia Group) and further work on certain international projects as part of international cooperation. In 2011 the FMC continued its efforts towards increasing effectiveness of information exchange between financial intelligence units worldwide.

Actions were taken to observe restriction requirements as applied by international institutions. As part of such actions, the FATF declarations were published on the FMC website regarding countries which were reported to have been strategically incomplete in combatting ML/TF as well as countries which have already developed plans for joint action to remove the said weaknesses.

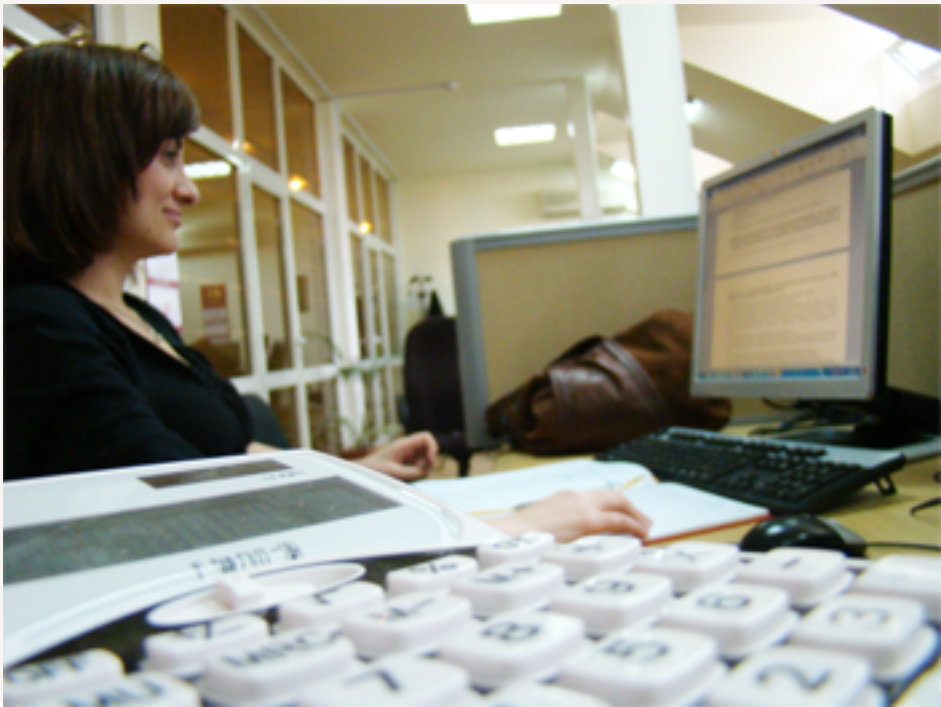
In the period under review the FMC signed memoranda of understanding with financial intelligence units of Tajikistan, China, Taiwan, Serbia, Montenegro, Saudi Arabia, Macedonia and Israel.

Work was further done by the FMC to deliver technical support to foreign intelligence units.

Training and consultancy remain central pillars in effective combatting ML/TF. In 2011 training programs and meetings were organized for FMC staff, other Central Bank people, public authorities and reporting entities to gain more knowledge of prevention of and fight against ML/TF. Courses and seminars arranged by the IMF, World Bank, Egmont Group, Basle

Management Institute, and European Bank for Reconstruction and Development should be mentioned. Also, the FMC organized seminars in Yerevan for specialists of the Central Banks of Eurasian Economic Community (EurAsEC) Member States; meetings and discussion with participation of internal monitoring centers of commercial domestic commercial banks were organized, as initiated by the FMC.

Programs tailored to increase professional knowledge of staff of non-financial institution reporting entities and individuals and bodies which oversee their activities are very important components in training and consultancy. To this effect, the FMC organized seminars during the year for representatives from the Ministry of Finance, agency of state registry of legal persons, gambling houses, audit and accountancy firms, and barristers.





MANAGEMENT AND ORGANIZATIONAL DEVELOPMENT

IMPROVING MANAGEMENT SYSTEMS

In 2011, as part of input of Information Security Management System (ISO 27001:2005), the Central Bank continued its cooperation with internationally reputable organization *Bureau Veritas* and further benefited the advice received from Armenia Representation of the organization.

Work done in 2011 according to the schedule of ISMS input under ISO 27001:2005 requirements included writing policies for the system operation, an appropriate software package was obtained and a relevant staff was trained. The work in all these areas will continue during 2012, too. In 2011 a Manual for Organizing Work to Maintain Business Continuity of the Central Bank was developed along with some other papers on individual business continuity processes and testing within the Central Bank.

The preparatory ISMS input and certification phase was successfully completed at the end of 2011 and audited accordingly. The next phase of audit by Bureau Veritas is planned in January 2012.

Seeking to further improve the electronic document circulation system within the Central Bank, certain source data document and document life cycle registration modules were developed.

To further meet ISO 27001:2005requirements, a Manual for Document Management and Registration was developed and actual documents circulation modalities were brought in compliance with the requirements laid down in the manual.

The year 2011 was profound in that the Central Bank did huge work connected with the construction of Dilijan Research Center in town Dilijan, Armenia. The center will be commissioned operational in 2012.

PERSONNEL MANAGEMENT

In 2011 the personnel policy of the Central Bank was aimed at fulfilling the main tasks and implementing the strategic program set before the Bank. This year too, appropriate resources were used to support professional development and lifelong training of the staff of the Central Bank. As of the end of 2010, the average number of staff of the Central Bank was 771 of which 445 women and 326 men. The average age of employees reached 38.

Vacancies in the Central Bank were filled primarily by competition. During the year 39 persons joined and 48 left the Central Bank. Staff turnover rate was 6.23 percent.

The Central Bank remained committed to recruiting young specialists, improving qualification and making the best use of their potential. As before, young specialists were selected mostly out of those who had attended a curriculum titled *Central Bank of Armenia: Introductory Course*, which is organized by the "Finance and Banking College" Foundation. In 2011 functional units of the Central Bank employed 61 young specialists on terminal contracts, 31 of who joined the Central Bank.

Students of establishments of higher education are allowed to take their academic and pre-diploma internship in the Central Bank so as to enhance their field knowledge and gain more professional skills. During the year 75 students from Armenia and 2 students from higher academic institutions abroad took their internship in the Central Bank.

Young Specialists Professional Knowledge Evaluation Committee of the Central Bank

The Committee for evaluation of professional knowledge of young specialists holds meetings to test and assess professional knowledge and talent of persons who work in the Central Bank as young specialists. The Committee's decisions on the status of young specialists are consultative only and can be used by heads of structural units for judgment and recommendation to chairman of the Central Bank for consideration.

In 2011 the Committee met 12 times and evaluated a total of 55 young specialists.

During 2011 the Central Bank further encouraged best students selected out of higher educational establishment of the Republic of Armenia and NKR by awarding 3 of them the Isahak Isahakyan Stipend.

Job Evaluation Committee of the Central Bank

The committee is designed to assess professional capacities of employees and applicants through both interview and tests in writing.

Chairman of the Central Bank heads the committee and has a decision-making power based on the conclusion issued by the committee, regarding:

- professional capacities and integrity of the employee for the job position he/she takes;
- signing an employment contract with the applicant;
- promoting a job position.

Staff Assessment Committee of the Central Bank

The Committee's meetings are held to evaluate professional capacities of employees of the Central bank or knowledge and skills of applicants for job at the Central Bank.

In 2011 the Committee met 27 times.

Improving Professional Qualification

In the period under review 58 staff members of the Central Bank have successfully taken exams for international professional qualification in finance, accounting, audit, insurance, and information technologies. Some already hold appropriate certificates.

An English Knowledge Test was developed by the Central Bank in collaboration with American University of Armenia which is aimed to check knowledge of the language and help the staff of the Central Bank for their active participation in training courses and trips abroad. In 2011 a total of 191 employees of the Central Bank passed the test successfully.

Job Evaluation Committee of the Central Bank

The task of the Committee for evaluation of jobs of the Central Bank is to evaluate and categorize new jobs or changed job positions. The Committee is set to discuss issues on evaluation and categorization of jobs for new or changed positions and make recommendations to chairman of the Central Bank for consideration. The Committee addresses the issues that are disputable with regard to performance of individual work programs of employees of the Central Bank.

The Committee's meetings are held as and when needed, before October 15 of the year.

In 2010 the Committee met 2 times.

INTERNATIONAL COOPERATION

In 2011 the Central Bank sustained its multilateral and bilateral cooperation with international organizations and institutions of other countries.

In the period under review, as part of the IMF/WB technical assistance, the Central Bank internalized the latest IMF approaches in banking supervision and financial operations, monetary policy and statistics.



Guests visiting the Central Bank during 2011 included an independent group of evaluators from the World Bank, experts of Agency Fitch Ratings, the EBRD delegation headed by vice-president Jan Fischer, an OECD expert Winfried Blaschke, with her mission to make studies in the area of financial services, a delegation from China Development Bank to explore cooperation possibilities and discuss mutual investment projects, the BSTDB delegation headed by chairman Andrei Kondakov, to present the Bank's medium-term strategy 2011-2014 and business plan, a delegation headed by Pascal Grangereau, a South Caucasia Coordinator of Agence Francaise du Developpement.

Events taken place in Yerevan as part of international cooperation during 2011 included:

- Visit of De Nederlandsche Bank's chairman Nout Wellink who lectured a topic "New Trends of Supervision Architecture: In and Outside Central Banks".
- Visit of ex minister of Labor and Social Security of Chile Jose Piñera who made a lecture with the following topic "Chile's experience in Social Security and Pension Reforms".
- 19th Plenary Session of Egmont Group of financial intelligence units representing 290 delegates from 99 countries.

During 2011 the Central Bank held bilateral contacts with international institutions and signed agreements with central banks and memoranda of understating within the framework of intergovernmental commissions, as follows:

- Memorandum of Understanding between the Central Bank and Financial Services Authority of Federal Republic of Germany regarding bank supervision.
- Agreement on Basic Currency Regulation and Currency Policy Principles in CIS Countries, signed in St. Petersburg, Russia.
- Memorandum of Understanding due for signing by and between the Central Bank and Financial Supervision Authority of the Republic of Poland.

Training programs

Staff members of the Central Bank participated in a great variety of events – training courses, seminars, workshops in Armenia and abroad; visited central banks of many countries to exchange experience. During 2011 a total of 236 employees of the Central Bank participated in 161 seminars abroad (EurAsEC Member States, CCBC in England, Joint Vienna Institute, central banks of Germany, France, Netherlands, Switzerland, Poland, Czech Republic, the Financial Stability Institute).

During the year a total of 27 specially tailored programs were organized by donor banks, at the initiation of the Central Bank.

A total of 10 seminars were organized by the Central Bank in cooperation with the US Federal Reserve System, central banks of Netherlands, Germany, the Toronto Center of Canada, National Bank of Poland, and EurAsEC Member States, including 6 regional seminars.

The Central Bank continued cooperation with the States of the Eurasia Economic Community in the form of the following four workshops: "Credit Rating of Organizations and the Central Bank Credit Registry", "Accounting Policy of Capital Investments and Fixed Assets Repair Operations", "Studying Framework for Combatting Criminally Obtained Proceeds and Terrorism Financing" and "Internal Audit and Control within Central Bank". A seminar titled "Consolidated Supervision" was organized by the U.S. Federal Reserve System, with participation of 13 experts from abroad and 19 employees of the Central Bank.

The Toronto Center of Canada organized a seminar "Leading" with participation of 15 employees of the Central Bank.

A total of 171 employees from the Central Bank and 35 specialists from abroad participated in 10 tailor-made seminars organized in Armenia.

In the period under review 35 staff members of the Central Bank participated in distant training course in a real-time regime on bank and insurance supervision, organized by the Financial Stability Institute.

There were more training activities (a total of 44) organized in Armenia to which 452 employees of the Central Bank participated.



PUBLIC RELATIONS

In the area of public relations in 2011 the Central Bank continued its efforts in explaining and commenting on its activities and organized educational and public awareness programs.

In the period under review the Central Bank launched a large-scale campaign to increase public awareness of the mandatory car insurance scheme which was introduced in 2011. There were 8 video clips produced and televised as part of the campaign.

Following its policy of keeping the public informed and aware, the Central Bank continued cooperating with non-governmental organizations, such as Union of Armenian Banks, Union of Mortgage Market Participants of Armenia, Association of Insurers and Consumer Interest Protection Organization.

The Central Bank regularly organized meetings with heads of organizations functioning in the financial sector; appeared with explanation of its actions, projects and legislative initiatives in the area of monetary policy, financial supervision and maintenance of financial stability.

The 19th Plenary Session of the Egmont Group was broadly featured by both local and foreign mass media.

A number of seminars/workshops were organized for representatives of mass media in which issues relating to monetary policy and financial stability as well as certain aspects of financial education were addressed.

The Central Bank published, on a monthly basis, Board resolutions on interest rates of Repo (Refinancing) Operations. A brief communication about the decision comes out shortly after any such resolution while the Board Minutes is publicly disclosed within 10 days.

In the period under review the Press Service of the Central Bank organized 10 press-conferences and arranged 10 interviews; responded comprehensively to 52 written and verbal queries; issued 152 press-releases explaining the Central Bank's activities, 38 press-releases about meetings of the Board, and 24 press-releases about interest rate of Repo Operations.



VISITOR CENTER [6]

The Visitor Center of the Central Bank opened in autumn of 2011. The Center is aimed to increase public awareness of the activities and operations of the Central Bank through various educational instruments (static, thematic and interactive displays).

The construction and design works of the Center took nearly 4 years. In the period from September to December 2011 the Center accepted 1657 pupils and students and 166 teachers.

In town Gavar, Armenia, the Central Bank organized an exhibition titled 'History of Money Circulation in Armenia'. The exhibition gathered 685 spectators.

Possibilities, structure

- Main visitors include high-grader schoolchildren and students. Other visitors are general public interested in the history of money, Central Bank activities, monetary policies.
- There are 24 static displays in exhibition with two interactive zones, including, among others, a note-checking laboratory, an automated teller machine, multimedia facilities, video films on the history of national currency, history of the Central Bank, cartoons on the financial system and how it functions.
- The exhibition is delivered in there languages – Armenian, English and Russian.
- The Center hosts training sessions for teachers of schools of general education; there are thematic lectures delivered for target audience.

[6] *See details on www. visitorscenter.cba.am.*



RISK MANAGEMENT AND AUDIT

INTERNAL AUDIT

Audit Group is a structural unit of the Central Bank and has been created by the Board of the Central Bank. It is responsible for the internal audit of the Central Bank. Group performs its functions in compliance with International Professional Practices Framework and The Code of Ethics issued by the Institute of Internal Auditors (IIA), as well as CobIT, VolIT, Risk IT framework.

Staff members of Audit Group are members to the IIA, Information System Audit and Control Association, Association of Chartered Certified Accountants, and take international qualification exams (CIA, CISA, ACCA).

In 2011 Audit Group carried out examinations, target and regular, pursuant to the annual audit plan approved by the Board of the Central Bank, to evaluate the effectiveness of risk management, control, and governance processes within the Central Bank as well as to provide possible solution to increased effectiveness. Evaluation has been issued as a result of an adequate assurance that:

- possible risks of processes are identified, and the mechanisms designed to manage them are efficient,
- information is reliable, sufficient and relevant for decision-making in terms of accountability and governance,
- processes are organized in an effective fashion, and control mechanisms in place are adequate and reliable,
- procedures comply with the governing law and regulations.

For each objective assurance, Audit Group made a respective report to the Board and Audit Committee of the Central Bank, with recommendations as appropriate.

In the period under review Audit Group continued actively cooperating with its counterparts at central banks and other organizations (European central Bank, the U.S. Federal Reserve System, German Bundesbank, Bank of Lithuania, De Nederlandsche Bank, Bank of Italy, Czech National Bank, and the IMF, Institute of Internal Auditors, ACCA, ISACA).



The following activities were continued during 2011:

- The auditing methodology was revised thoroughly, which resulted in creation of the *Risks Manual* designed for the annual planning of works, the *Internal Audit Guideline* designed for audit examination; the charter of Audit Group was simplified consistent with best international experience.
- The examinations schedule for 2012 was prepared and approved; the schedule now contains somewhat a broader scope of examinations; the schedule is part of the entire audit cycle for 2012-2014.
- Audit Group saw staff change; 4 specialists representing the area of external audit and IT audit joined the group.
- The staff training program changed to include more professional knowledge and such topics so as to respond to the processes included in the Audit Plan for 2012-2014.

A workshop titled "Internal Audit and Control in Central Banks" was organized in Tsaghkadzor, Armenia, in the framework of the Eurasia Economic Community.

In the period under review, owing to joint efforts by Audit Group and Personnel Management Department, the Central Bank was granted an ACCA Platinum Employer Level Audit Group, which enhanced the Central Bank's reputation as an institution that encourages its employees to earn international qualification.

Audit Group negotiated arrangements with Internal Audit of De Nederlandsche Bank to plan a visit for external evaluation of the Central Bank expected in July of 2012.

Audit Committee

The Audit Committee of the Central Bank is one of key components of the Bank's governance. Responsibilities of the Committee include issues and tasks pertinent to financial accounts of the Bank, internal control, external and internal audit. The Committee consists of three members, including chairman of the Committee. Members of the Committee are board members of the Central Bank. During the year the Committee met 6 times and discussed and adopted decisions in respect of 30 issues. The discussion of issues covered examinations of Audit Group, external audit, internal control and risk management system as well as day-to-day activities of the Group and area-specific issues.

Republic of Armenia

Central Bank

Annual Financial Statements

2011

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CENTRAL BANK
OF THE REPUBLIC OF ARMENIA

Consolidated financial statements and Independent auditor's report

31 December 2011

INDEPENDENT AUDITOR'S REPORT

To the sole founder and Board of the Central Bank of the Republic of Armenia

We have audited the accompanying consolidated financial statements of the Central Bank of the Republic of Armenia and its subsidiaries, which comprise the consolidated statement of financial position as at 31 December 2011, and the consolidated income statement, consolidated statements of comprehensive income, of changes in equity and of cash flows for the year then ended, and a summary of significant accounting policies and other explanatory information.

Management's responsibility for the consolidated financial statements

Management is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with International Financial Reporting Standards, and for such internal control as management determines is necessary to enable the preparation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's responsibility

Our responsibility is to express an opinion on these consolidated financial statements based on our audit. We conducted our audit in accordance with International Standards of Auditing. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance whether the consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditors' judgment, including the assessment of the risks of material misstatement of consolidated financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the consolidated financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the consolidated financial statements present fairy, in all material respects, the financial position of the Central Bank of the Republic of Armenia and its subsidiaries as at 31 December 2011, and their financial performance and its cash flows for the year ended in accordance with International Financial Reporting Standards.

Ernst and Young CJSC

Partner (Audit department)  ***Dmitry Weinstein***

On behalf of the General director M. Alexandarian
(by power of authority dated 1 September 2011)  ***Eric Hayrapetyan***

30 March 2012

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Consolidated statement of comprehensive income

(in thousand Armenian drams)

	Note	Year ended 31 December, 2011	Year ended 31 December, 2010 *(restated)*
Interest income	4	11,880,230	9,534,614
Interest expense	5	(10,144,881)	(16,652,276)
Net interest income (expense)		**1,735,349**	**(7,117,662)**
Fee and commission income		70,910	61,399
Fee and commission expense		(350,914)	(438,138)
Net fee and commission expense		**(280,004)**	**(376,739)**
Net foreign exchange gain/(loss)	6	19,181,238	(12,637,826)
Net realized gain/(loss) on available-for-sale assets		60,729	(21,168)
Net gain on financial instruments at fair value through profit or loss	7	1,997,356	2,943,175
Other income	8	2,804,325	1,901,653
Impairment losses	11,13	(11,564,863)	-
Costs of production of banknotes, coins and numismatics	9	(2,383,348)	(226,802)
Other expenses	10	(10,987,815)	(13,061,942)
Income tax		(99,043)	-
Profit/ (loss) for the year		**463,924**	**(28,597,311)**
Other comprehensive income			
Net unrealized loss from changes in fair value		470,530	(235,829)
Net (gains)/losses reclassified to profit or loss on disposal of available-for-sales assets		(60,729)	21,168
Total comprehensive income for the year		**873,725**	**(28,811,972)**

These consolidated financial statements were approved by the Board of the Central Bank of the Republic of Armenia on March 27, 2012 and were signed on its behalf by:

Arthur JAVADYAN
Chairman of the Central Bank
of the Republic of Armenia



Haykanush HAKOBYAN
Chief Accountant of the Central Bank
of the Republic of Armenia



The accompanying notes from 1 to 29 are an integral part of these consolidated financial statements.

Consolidated statement of financial position

(in thousand Armenian drams)

	Note	As of 31 December, 2011	As of 31 December, 2010 *(restated)*	As of 31 December, 2009 *(restated)*
ASSETS				
Foreign currency assets				
Cash		5,013,113	7,552,047	7,776,292
Placements with banks and other financial institutions	11	236,415,264	158,102,101	221,678,070
Financial instruments at fair value through profit or loss	12	344,720,503	404,632,917	459,234,675
Available-for-sale assets	13	1,646	917	917
Held to maturity assets	13	137,340,298	95,678,521	25,171,087
Placements with the IMF	14	76,489,346	63,670,237	101,621,324
Other assets		1,228,086	874,492	666,956
		801,208,256	**730,511,232**	**816,149,321**
Domestic currency assets				
Loans and reverse repurchase agreements	15	149,245,576	70,615,499	70,735,139
Available-for-sale assets	13	106,922,985	88,705,765	121,204,193
Held to maturity assets	13	3,265,916	4,132,916	3,862,867
Property and equipment	16	38,369,456	26,312,189	15,762,787
Intangible assets	17	640,389	583,179	427,907
Other assets	18	6,253,627	3,752,261	2,451,325
		304,697,949	**194,101,809**	**214,444,218**
Total assets		**1,105,906,205**	**924,613,041**	**1,030,593,539**
LIABILITIES AND EQUITY				
Foreign currency liabilities				
Deposits and accounts of financial and other institutions	19	104,346,523	99,650,034	150,616,174
Due to the Government of the Republic of Armenia	22	3,974,934	3,989,112	1,329,188
Financial liabilities at fair value through profit or loss	12	1,771,245	694,841	36,588
Due to the IMF	14	306,460,839	278,087,230	267,820,110
Other borrowed funds	20	38,846,294	27,599,809	28,309,397
Other liabilities		153,901	146,096	206,504
		455,553,736	**410,167,122**	**448,317,961**

The accompanying notes from 1 to 29 are an integral part of these consolidated financial statements.

	Note	As of 31 December, 2011	As of 31 December, 2010 *(restated)*	As of 31 December, 2009 *(restated)*
Domestic currency liabilities				
Notes and coins in circulation		398,777,362	348,164,734	320,669,631
Deposits and accounts of financial and other institutions	19	166,827,933	80,825,771	53,204,221
Due to the Government of the Republic of Armenia	22	80,229,419	106,545,573	177,194,796
Debt securities issued		963,593	-	-
Other liabilities	21	3,255,800	1,353,894	853,302
		650,054,107	**536,889,972**	**551,921,950**
Total liabilities		**1,105,607,843**	**947,057,094**	**1,000,239,911**
Equity				
Issued capital	23	100,000	100,000	100,000
General reserve	23	17,389,049	17,389,049	11,392,622
Additional paid in capital	13	107,531,884	85,663,194	85,663,194
Revaluation reserve for available-for-sale assets		(1,218,959)	(1,628,760)	(1,414,100)
Accumulated losses		(123,503,612)	(123,967,536)	(65,388,088)
Total equity		**298,362**	**(22,444,053)**	**30,353,628**
Total liabilities and equity		**1,105,906,205**	**924,613,041**	**1,030,593,539**

The accompanying notes from 1 to 29 are an integral part of these consolidated financial statements.

Consolidated statement of changes in equity

(in thousand Armenian drams)

	Issued capital	General reserve	Additional paid in capital	Revaluation reserve for available-for-sale assets	Accumulated loss (restated)	Total equity
Balance as of 1 January, 2010	**100,000**	**11,392,622**	**85,663,194**	**(1,414,100)**	**(65,388,088)**	**30,353,628**
Distribution to general reserve	-	5,996,427	-	-	(5,996,427)	-
Distribution to the Government of the Republic of Armenia	-	-	-	-	(23,985,710)	(23,985,710)
Loss for the year (restated)	-	-	-	-	(28,597,311)	(28,597,311)
Other comprehensive income	-	-	-	(214,661)	-	(214,661)
Balance as of 31 December, 2010 (restated)	**100,000**	**17,389,049**	**85,663,194**	**(1,628,760)**	**(123,967,536)**	**(22,444,053)**
Extension of the promissory note by the Government of the Republic of Armenia	-	-	21,868,690	-	-	21,868,690
Profit for the year	-	-	-	-	463,924	463,924
Other comprehensive income	-	-	-	409,801	-	409,801
Balance as of 31 December, 2011	**100,000**	**17,389,049**	**107,531,884**	**(1,218,959)**	**(123,503,612)**	**298,362**

The accompanying notes from 1 to 29 are an integral part of these consolidated financial statements.

Consolidated statement of cash flows

(in thousand Armenian drams)

	Note	Year ended 31 December, 2011	Year ended 31 December, 2010
CASH FLOWS FROM OPERATING ACTIVITIES			
Profit/(loss) for the year		463,924	(28,597,311)
Depreciation and amortization		1,223,482	731,035
Impairment losses		11,564,863	-
Loss from disposal of property and equipment		367,180	5,302
Interests receivable		661,507	577,853
Interests payable		103,910	657,448
Net (gains)/losses from revaluation of monetary assets and liabilities		(19,326,197)	12,099,588
Net loss from remeasurement of financial instruments at fair value		1,450,482	1,939,306
Other		238	(32)
Cash flows from operating activities before changes in operating assets and liabilities		**(3,490,611)**	**(12,586,811)**
(Increase)/decrease in operating assets			
Placements with banks and other financial institutions		(65,998,845)	882,671
Financial instruments at fair value through profit or loss		80,622,949	26,861,008
Placements with the IMF		12,099	23,797
Available-for-sale assets		4,060,543	8,298,058
Held-to-maturity assets		(33,289,368)	(67,685,078)
Loans and reverse repurchase agreements		(78,951,506)	(30,946)
Other assets		(1,845,736)	(1,421,373)
Increase/(decrease) in operating liabilities			
Notes and coins in circulation		50,612,628	27,495,103
Deposits and accounts of financial and other institutions		84,090,265	(16,270,879)
Due to the IMF		(8,199,434)	6,923,690
Due to the Government of the Republic of Armenia		(26,489,725)	(68,085,395)
Debt securities issued		963,593	-
Other liabilities		1,283,912	190,940
Net cash from/(used in) operating activities		**3,380,764**	**(95,405,215)**
CASH FLOWS FROM INVESTING ACTIVITIES			
Purchase of property, equipment and intangible assets		(13,729,298)	(11,446,498)
Proceeds from sale of property and equipment		24,160	5,487
Net cash used in investing activities		**(13,705,138)**	**(11,441,011)**
CASH FLOWS FROM FINANCING ACTIVITIES			
Loans received		70,340,555	64,703,960
Loans redeemed		(39,530,684)	(44,426,131)
Net cash from/(used in) financing activities		**30,809,871**	**20,277,829**
Net increase/(decrease) in cash and cash equivalents		**20,485,497**	**(86,568,397)**
Cash and cash equivalents at the beginning of the year		139,497,528	236,032,987
Exchange differences on cash and cash equivalents		7,761,602	(9,967,062)
Cash and cash equivalents at the end of the year	26	**167,744,627**	**139,497,528**
Supplementary information			
Interest received		11,218,722	8,956,761
Interest paid		(10,248,791)	(17,309,724)

The accompanying notes from 1 to 29 are an integral part of these consolidated financial statements.

Notes to 2011 consolidated financial statements

1. Background

Principal activities

The Central Bank of the Republic of Armenia or the Central Bank of Armenia (the "Bank") is the parent entity in the Group. It is a legal entity the sole founder of which is the Republic of Armenia.

The registered address of the Bank is 6 Vazgen Sargsyan Street, Yerevan 0010, Republic of Armenia. The average number of employees of the Bank during 2011 was 765 (2010: 728).

The basic objective of the Bank is ensuring stability of prices in the Republic of Armenia. It is achieved through elaboration and implementation of monetary policy. In addition to its basic objective, the Bank is also responsible for:

- ensuring the stability, liquidity, solvency and other necessary conditions for sound operation of the financial system in the Republic of Armenia; and,
- creation and development of an effective payment and settlement system.

The Bank also:

- issues the national currency of the Republic of Armenia and regulates its circulation;
- organizes and regulates anti money laundering and terrorism financing activities;
- is the financial agent and advisor of the Government of the Republic of Armenia;
- licenses commercial banks and, cases envisaged by the legislation, other entities, supervises and regulates their activities;
- is the lender of last resort to commercial banks; and,
- owns, uses and manages international reserves of the Republic of Armenia.

The Bank's subsidiaries are as follows:

Name	Country of incorporation	Principal activity	Controlled %		Date of establishment
			2011	2010	
"Armenian Card" CJSC	Republic of Armenia	Payment and settlement services	59	66	March 2000
"ArmCollection" CJSC	Republic of Armenia	Transportation/delivery of cash	100	100	April 1998
"Panarmenian bank" OJSC	Republic of Armenia	Banking	100	100	December 2009
"National Mortgage Company" RCO CJSC	Republic of Armenia	Mortgage refinancing	100	100	June 2009
"Home for Youth" UCO CJSC	Republic of Armenia	Mortgage refinancing	100	100	February 2010
"Small and medium business credit support" CJSC	Republic of Armenia	Lending support	100	100	December 2010

2. Basis of preparation

2.1. Statement of compliance

These consolidated financial statements have been prepared in accordance with International Financial Reporting Standards ("IFRS").

2.2. Basis of measurement

The consolidated financial statements have been prepared under the historical cost convention except as disclosed in the accounting policies below. For example, trading and available-for-sale securities, derivative financial instruments have been measured at fair value.

2.3. Functional and presentation currency

The national currency of the Republic of Armenia is the Armenian Dram ("AMD"), which is the Bank's functional currency and the currency in which these consolidated financial statements are presented. All financial information presented in AMD has been rounded to the nearest thousand unless otherwise indicated.

2.4 Use of estimates and judgments

In the process of applying the Group's accounting policies, management has used its judgments and made estimates in

determining the amounts recognised in the consolidated financial statements. The most significant use of judgments and estimates are as follows:

- Where the fair values of financial assets and financial liabilities recorded in the consolidated statement of financial position cannot be derived from active markets, they are determined using a variety of valuation techniques that include the use of mathematical models. The input to these models is taken from observable markets where possible, but where this is not feasible, a degree of judgment is required in establishing fair values.
- The Group regularly reviews its loans and receivables to assess impairment. The Group uses its experienced judgment to estimate the amount of any impairment loss in cases where a borrower is in financial difficulties and there are few available sources of historical data relating to similar borrowers. Similarly, the Group estimates changes in future cash flows based on the observable data indicating that there has been an adverse change in the payment status of borrowers in a group, or national or local economic conditions that correlate with defaults on assets in the group. Management uses estimates based on historical loss experience for assets with credit risk characteristics and objective evidence of impairment similar to those in the group of loans and receivables. The Group uses its experienced judgment to adjust observable data for a group of loans or receivables to reflect current circumstances.

2.5 Restatement of corresponding figures

In the process of preparation of the 2011 financial statements Management of the Group has restated the corresponding figures as at 31 December 2010 and for the year then ended for the following:

- Foreign currency denominated liabilities due to IMF
  - In 2009 due to an arithmetical mistake the Group reported foreign currency liability due to IMF in the amount of AMD 92,263,527 thousand instead of AMD 95,263,527 thousand;
  - In 2010 and 2009 the Group has incorrectly classified its SDR-denominated liabilities due to IMF as domestic currency (Armenian dram) liabilities due to IMF;
- Currency forward with the Government of Armenia
  - In 2010 the Group didn't recognize a currency forward agreement with the Government of Armenia. According to the agreement, the Government should exchange with the Bank main foreign currency denominated budget inflows and outflows at a rate fixed in the state budget.

The corresponding figures for the year ended 31 December 2010 have been restated as follows:

(in thousand Armenian drams)

	As previously reported	Restatement	As restated
Consolidated statement of financial position			
Foreign currency liabilities			
Financial liabilities at fair value through profit or loss	19,478	675,363	694,841
Due to the IMF	82,284,509	195,802,721	278,087,230
Domestic currency liabilities			
Due to the IMF	195,802,721	(195,802,721)	-
Accumulated losses	(123,292,173)	(675,363)	(123,967,536)
Consolidated statement of comprehensive income			
Net foreign exchange gain/(loss)	(11,962,463)	(675,363)	(12,637,826)
Profit/(loss) for the year	(27,921,948)	(675,363)	(28,597,311)
Total comprehensive income for the year	(28,136,609)	(675,363)	(28,811,972)

The consolidated statement of financial position as at 31 December 2009 has been restated as follows:

	As previously reported	Restatement	As restated
Consolidated statement of financial position			
Foreign currency liabilities			
Due to the IMF	92,263,527	175,556,583	267,820,110
Domestic currency liabilities			
Due to the IMF	172,556,583	(172,556,583)	-

3. Significant accounting policies

3.1. Changes in accounting policies

The Group has adopted the following amended IFRS and new IFRIC Interpretations during the year. The principal effects of these changes are as follows:

IAS 24 Related Party Disclosures (Revised)

The revised IAS 24, issued in November 2009 and effective for annual periods beginning on or after 1 January 2011, simplifies the disclosure requirements for government-related

entities and clarifies the definition of a related party. Previously, an entity controlled or significantly influenced by a government was required to disclose information about all transactions with other entities controlled or significantly influenced by the same government. The revised standard requires disclosure about these transactions only if they are individually or collectively significant. The revised standard had no impact on the Group's consolidated financial statements.

Amendments to IAS 32 Financial Instruments: Presentation: Classification of Rights Issues

In October 2009, the IASB issued amendment to IAS 32. Entities shall apply that amendment for annual periods beginning on or after 1 February 2010. The amendment alters the definition of a financial liability in IAS 32 to classify rights issues and certain options or warrants as equity instruments. This is applicable if the rights are given pro rata to all of the existing owners of the same class of an entity's non-derivative equity instruments, in order to acquire a fixed number of the entity's own equity instruments for a fixed amount in any currency. The amendment had no impact on the Group's consolidated financial statements.

IFRIC 19 Extinguishing Financial Liabilities with Equity Instruments

IFRIC Interpretation 19 was issued in November 2009 and is effective for annual periods beginning on or after 1 July 2010. The interpretation clarifies the accounting when the terms of a financial liability are renegotiated and result in the entity issuing equity instruments to a creditor to extinguish all or part of the financial liability. This Interpretation had no impact on the Group's consolidated financial statements.

Improvements to IFRSs

In May 2010 the IASB issued the third omnibus of amendments to its standards, primarily with a view to removing inconsistencies and clarifying wording. Most of the amendments are effective for annual periods beginning on or after 1 January 2011. There are separate transitional provisions for each standard. Amendments included in May 2010 "Improvements to IFRS" had impact on the accounting policies, financial position or performance of the Group, as described below.

- *IFRS 3 Business Combinations*: limits the scope of the measurement choices that only the components of NCI that are present ownership interests that entitle their holders to a proportionate share of the entity's net assets, in the event of liquidation, shall be measured either at fair value or at the present ownership instruments' proportionate share of the acquiree's identifiable net assets.
- *IFRS 7 Financial Instruments: Disclosures*; introduces the amendments to quantitative and credit risk disclosures. The additional requirements had minor impact as information is readily available.

- Other amendments to IFRS 1, IFRS 3, IAS 1, IAS 27, IAS 34 and IFRIC 13 will have no impact on the accounting policies, financial position or performance of the Group.

The following amendments to standards and interpretations did not have any impact on the accounting policies, financial position or performance of the Group:

- IFRS 1 *First-time Adoption of International Financial Reporting Standards – Limited Exemption from Comparative*;
- IFRS 7 *Disclosures for First-time Adopters;*
- IFRIC 14 *Prepayments of a Minimum Funding Requirement.*

3.2. Basis of consolidation

Subsidiaries, which are those entities in which the Group has an interest of more than one half of the voting rights, or otherwise has power to exercise control over their operations, are consolidated. Subsidiaries are consolidated from the date on which control is transferred to the Group and are no longer consolidated from the date that control ceases. All intra-group transactions, balances and unrealised gains on transactions between group companies are eliminated in full; unrealised losses are also eliminated unless the transaction provides evidence of an impairment of the asset transferred. Where necessary, accounting policies for subsidiaries have been changed to ensure consistency with the policies adopted by the Group.

A change in the ownership interest of a subsidiary, without a change of control, is accounted for as an equity transaction. Losses are attributed to the non-controlling interests even if that results in a deficit balance.

If the Group loses control over a subsidiary, it derecognises the assets (including goodwill) and liabilities of the subsidiary, the carrying amount of any non-controlling interests, the cumulative translation differences, recorded in equity; recognises the fair value of the consideration received, the fair value of any investment retained and any surplus or deficit in profit or loss and reclassifies the parent's share of components previously recognised in other comprehensive income to profit or loss.

3.3. Foreign currency translation and presentation of foreign currency items

Transactions in foreign currencies are initially recorded in the functional currency, converted at the rate of exchange ruling at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies at the reporting date are retranslated at the rate of exchange ruling at the reporting date.

Gains and losses resulting from the translation of foreign currency transactions are recognised in profit or loss as net foreign exchange gain/(loss). Non-monetary assets and liabilities denominated in foreign currencies that are measured in terms of historical cost in a foreign currency are translated using the exchange rates ruling as at the dates of the initial transaction. Non-monetary items measured at fair value in a foreign currency are translated using the exchange rates at the date when the fair value was determined.

Differences between the contractual exchange rate of a transaction in a foreign currency and the exchange rate ruling at the date of the transaction are included in profit or loss.

The exchange rates at the reporting dates used by the Bank in the preparation of the consolidated financial statements are as follows:

	31 December, 2011	31 December, 2010
AMD/1 US Dollar	385.77	363.44
AMD/1 Euro	498.72	481.16
AMD/1 SDR	592.26	559.71

3.4. Cash and cash equivalents

The Group considers cash, nostro accounts with banks and SDR holdings in the IMF to be cash and cash equivalents.

3.5. Financial instruments

Initial recognition

Financial assets in the scope of IAS 39 are classified as either financial instruments at fair value through profit or loss, loans and receivables, held-to-maturity assets, or available-for-sale assets, as appropriate. When financial assets are recognised initially, they are measured at fair value, plus, in the case of investments not at fair value through profit or loss, directly attributable transaction costs. The Group determines the classification of its financial assets upon initial recognition, and subsequently can reclassify financial assets in certain cases as described below.

Date of recognition

All regular way purchases and sales of financial assets are recognised on the settlement date. Regular way purchases or sales are purchases or sales of financial assets that require delivery of assets within the period generally established by regulation or convention in the marketplace.

Financial assets at fair value through profit or loss

Financial assets classified as held for trading are included in the category "financial instruments at fair value through profit or loss". Financial assets are classified as held for trading if they are acquired for the purpose of selling in the near term. Derivatives are also classified as held for trading unless they are designated and effective hedging instruments. Gains or losses on financial assets held for trading are recognised in profit or loss.

In the normal course of business, the Group enters into various derivative financial instruments including futures, forwards, swaps and options in the foreign exchange and capital markets. Such financial instruments are held for trading and are recorded at fair value. The fair values are estimated based on quoted market prices or pricing models that take into account the current market and contractual prices of the underlying instruments and other factors. Derivatives are carried as assets when their fair value is positive and as liabilities when it is negative. Gains and losses resulting from these instruments are included in profit or loss as net gain on financial instruments at fair value through profit or loss or net foreign exchange gain/(loss), depending on the nature of the instrument.

Derivatives embedded in other financial instruments are treated as separate derivatives and recorded at fair value if their economic characteristics and risks are not closely related to those of the host contract, and the host contract is not itself held for trading or designated at fair value through profit or loss. The embedded derivatives separated from the host are carried at fair on the trading portfolio with changes in fair value recognised in profit or loss.

Held-to-maturity assets

Non-derivative assets with fixed or determinable payments and fixed maturity are classified as held-to-maturity when the Group has the positive intention and ability to hold them to maturity. Investments intended to be held for an undefined period are not included in this classification. Held-to-maturity assets are subsequently measured at amortised cost. Gains and losses are recognised in profit or loss when the assets are impaired, as well as through the amortisation process.

Loans and receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. They are not entered into with the intention of immediate or short-term resale and are not classified as trading securities or designated as investment securities available-for-sale. Such assets include placements with banks and other

financial institutions, placements with the IMF, loans and reverse repurchase agreements. Such assets are carried at amortised cost using the effective interest method. Gains and losses are recognised in profit or loss when the loans and receivables are derecognised or impaired, as well as through the amortisation process.

Available-for-sale assets

Available-for-sale assets are those non-derivative financial assets that are designated as available-for-sale or are not classified in any of the three preceding categories. After initial recognition available-for sale assets are measured at fair value with gains or losses being recognised in other comprehensive income until the investment is derecognised or until the investment is determined to be impaired at which time the cumulative gain or loss previously reported in other comprehensive income is reclassified to profit or loss. However, interest calculated using the effective interest method is recognised in profit or loss.

Reclassification of financial assets

If a non-derivative financial asset classified as held for trading is no longer held for the purpose of selling in the near term, it may be reclassified out of the fair value through profit or loss category in one of the following cases:

- a financial asset that would have met the definition of loans and receivables above may be reclassified to loans and receivables category if the Group has the intention and ability to hold it for the foreseeable future or until maturity;
- other financial assets may be reclassified to available for sale or held to maturity categories only in rare circumstances.

A financial asset classified as available for sale that would have met the definition of loans and receivables may be reclassified to loans and receivables category of the Group has the intention and ability to hold it for the foreseeable future or until maturity.

Financial assets are reclassified at their fair value on the date of reclassification. Any gain or loss already recognized in profit or loss is not reversed. The fair value of the financial asset on the date of reclassification becomes its new cost or amortised cost, as applicable.

Borrowings

Issued financial instruments or their components are classified as liabilities, where the substance of the contractual arrangement results in the Group having an obligation either to deliver cash or another financial asset to the holder, or to

satisfy the obligation other than by the exchange of a fixed amount of cash or another financial asset for a fixed number of own equity instruments. Such instruments include deposits and accounts of financial and other institutions, amounts due to the Government of the Republic of Armenia and the IMF, other borrowed funds and debt securities issued. After initial recognition, borrowings are subsequently measured at amortised cost using the effective interest method. Gains and losses are recognised in profit or loss when the borrowings are derecognised as well as through the amortisation process.

Determination of fair value

- The fair value of financial instruments traded in active market at the reporting date is based on their quoted market price or dealer price quotations (bid price for long positions and ask price for short positions) without any deduction for transaction costs.
- For all other financial instruments not listed in an active market, the fair value is determined by using appropriate valuation techniques.
- Valuation techniques include net present value techniques, comparison to similar instruments for which market observable prices exist, options pricing models and other relevant valuation models.

3.6. Derecognition of financial assets and liabilities

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

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

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

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

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

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

3.7. Offsetting of financial assets and liabilities

Financial assets and liabilities are offset and the net amount is reported in the consolidated statement of financial position when there is a legally enforceable right to set off the recognised amounts and there is an intention to settle on a net basis, or realise the asset and settle the liability simultaneously. This is not generally the case with master netting agreements, and the related assets and liabilities are presented gross in the consolidated statement of financial position.

3.8. Repurchase and reverse repurchase agreements

Sale and repurchase agreements ("repo") are treated as secured financial transactions. Securities sold under sale and repurchase agreements are retained in the consolidated statement of financial position and, in case the transferee has the right by contract or custom to sell or repledge them, reclassified as securities pledged under sale and repurchase agreements. The corresponding liability is presented within deposits and accounts of financial and other institutions. The difference between the sale and repurchase price is treated as interest and accrued over the life of the repo agreements using the effective yield method.

3.9. Securities lending and borrowing

Securities lent to counterparties are retained in the consolidated statement of financial position. Securities borrowed are not recorded in the consolidated statement of financial position, unless these are sold to third parties, in which case the purchase and sale are recorded within net gain

on financial instruments at fair value through profit or loss in profit or loss. The obligation to return them is recorded within financial liabilities at fair value through profit or loss.

3.10. Notes and coins in circulation

Notes and coins in circulation issued by the Bank are presented in the consolidated statement of financial position as a liability at nominal value. Printing and production costs of notes and coins are recognized in profit or loss as incurred.

3.11. Numismatic coins

Numismatic coins are measured at the lower of cost and net realisable value. The cost of numismatic coins is based on the first-in first-out principle, and includes expenses incurred in acquiring the numismatic coins and bringing them to their existing location. Net realisable value is the estimated selling price less the estimated costs necessary to make the sale. The difference between net disposal proceeds and the carrying value is recognised as a gain or loss included in profit or loss.

3.12. Property and equipment

Property and equipment are carried at cost, excluding the costs of day-to-day servicing, less accumulated depreciation and any accumulated impairment. Such cost includes the cost of replacing part of equipment when that cost is incurred if the recognition criteria are met. Likewise, when a major inspection is performed, its cost is recognised in the carrying amount of the plant and equipment as a replacement if the recognition criteria are satisfied.

Where significant parts of property and equipment are required to be replaced at intervals, the Group recognises such parts as individual assets with specific useful lives and depreciates them accordingly.

All other repair and maintenance costs are recognised in profit or loss as incurred.

An item of property, plant and equipment and any significant part initially recognised is derecognised upon disposal or when no future economic benefits are expected from its use or disposal. Any gain or loss arising on derecognition of the asset (calculated as the difference between the net disposal proceeds and the carrying amount of the asset) is included in profit or loss when the asset is derecognised.

Depreciation

Depreciation of an asset begins when it is available for use. Depreciation is calculated on a straight-line basis over the following estimated useful lives:

	2011	2010
Land and buildings	30-50 years	30-50 years
Networks, computer and other equipment	2-15 years	2-15 years
Vehicles	5 years	5 years

The asset's residual values, useful lives and methods are reviewed, and adjusted as appropriate, at each financial year-end.

3.13. Intangible assets

Intangible assets include computer software and licenses.

Intangible assets acquired separately are measured on initial recognition at cost. The cost of intangible assets acquired in a business combination is fair value as at the date of acquisition. Following initial recognition, intangible assets are carried at cost less any accumulated amortisation and any accumulated impairment losses. The useful lives of intangible assets are assessed to be either finite or indefinite. Intangible assets with finite lives are amortised over the useful economic lives of 1 to 7 years and assessed for impairment whenever there is an indication that the intangible asset may be impaired. Amortisation periods and methods for intangible assets with indefinite useful lives are reviewed at least at each financial year-end.

Computer software maintenance costs are recognized in profit or loss as incurred.

3.14. Operating leases – Group as lessee

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

3.15. Impairment

The Group assesses at each reporting date whether there is any objective evidence that a financial asset or a group of financial assets is impaired. A financial asset or a group of financial assets is deemed to be impaired if, and only if, there is objective evidence of impairment as a result of one or more events that has occurred after the initial recognition of the asset (an incurred "loss event") and that loss event (or events) has an impact on the estimated future cash flows of the financial asset or the group of financial assets that can be reliably estimated. Evidence of impairment may include indications that the borrower or a group of borrowers is experiencing significant

financial difficulty, default or delinquency in interest or principal payments, the probability that they will enter bankruptcy or other financial reorganisation and where observable data indicate that there is a measurable decrease in the estimated future cash flows, such as changes in arrears or economic conditions that correlate with defaults.

Placements with banks and other financial institutions and loans and reverse repurchase agreements

For amounts due from financial institutions carried at amortised cost, the Group first assesses individually whether objective evidence of impairment exists individually for financial assets that are individually significant, or collectively for financial assets that are not individually significant. If the Group determines that no objective evidence of impairment exists for an individually assessed financial asset, whether significant or not, it includes the asset in a group of financial assets with similar credit risks characteristics and collectively assesses them for impairment. Assets that are individually assessed for impairment and for which an impairment loss is, or continues to be, recognised are not included in a collective assessment of impairment.

If there is an objective evidence that an impairment loss has been incurred, the amount of the loss is measured as the difference between the assets' carrying amount and the present value of estimated future cash flows (excluding future expected credit losses that have not yet been incurred). The carrying amount of the asset is reduced through the use of an allowance account and the amount of the loss is recognised in profit or loss. Interest income continues to be accrued on the reduced carrying amount based on the original effective interest rate of the asset. Loans together with the associated allowance are written off when there is no realistic prospect of future recovery and all collateral has been realised or has been transferred to the Group. If, in a subsequent year, the amount of the estimated impairment loss increases or decreases because of an event occurring after the impairment was recognised, the previously recognised impairment loss is increased or reduced by adjusting the allowance account. If a future write-off is later recovered, the recovery is credited to profit or loss.

The present value of the estimated future cash flows is discounted at the financial asset's original effective interest rate. If a loan has a variable interest rate, the discount rate for measuring any impairment loss is the current effective interest rate. The calculation of the present value of the estimated future cash flows of a collateralised financial asset reflects the cash flows that may result from foreclosure less costs for obtaining and selling the collateral, whether or not foreclosure is probable.

For the purpose of a collective evaluation of impairment, financial assets are grouped on the basis of the Group's internal

credit grading system that considers credit risk characteristics such as asset type, industry, geographical location, collateral type, past-due status and other relevant factors.

Future cash flows on a group of financial assets that are collectively evaluated for impairment are estimated on the basis of historical loss experience for assets with credit risk characteristics similar to those in the group. Historical loss experience is adjusted on the basis of current observable data to reflect the effects of current conditions that did not affect the years on which the historical loss experience is based and to remove the effects of conditions in the historical period that do not exist currently. Estimates of changes in future cash flows reflect, and are directionally consistent with, changes in related observable data from year to year (such as changes in unemployment rates, property prices, commodity prices, payment status, or other factors that are indicative of incurred losses in the group or their magnitude). The methodology and assumptions used for estimating future cash flows are reviewed regularly to reduce any differences between loss estimates and actual loss experience.

Held-to-maturity assets

For held-to-maturity assets the Group assesses individually whether there is objective evidence of impairment. If there is objective evidence that an impairment loss has been incurred, the amount of the loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows. The carrying amount of the asset is reduced and the amount of the loss is recognised in profit or loss.

If, in a subsequent year, the amount of the estimated impairment loss decreases because of an event occurring after the impairment was recognised, any amounts formerly charged are credited to profit or loss.

Available-for-sale assets

For available-for-sale assets, the Group assesses at each reporting date whether there is objective evidence that an investment or a group of investments is impaired.

In the case of equity investments classified as available-for-sale, objective evidence would include a significant or prolonged decline in the fair value of the investment below its cost. Where there is evidence of impairment, the cumulative loss – measured as the difference between the acquisition coast and the current fair value, less any impairment loss on that investment previously recognised in profit or loss – is reclassified from other comprehensive income to profit or loss. Impairment losses on equity investments are not reversed through profit or loss; increases in their fair value after impairment are recognised in other comprehensive income.

In the case of debt instruments classified as available-for-sale, impairment is assessed based on the same criteria as financial assets carried at amortised cost. Future interest income is based on the reduced carrying amount and is accrued using the rate of interest used to discount the future cash flows for the purpose of measuring the impairment loss. The interest income is recorded in profit or loss. If, in a subsequent year, the fair value of a debt instrument increases and the increase can be objectively related to an event occurring after the impairment loss was recognised in profit or loss, the impairment loss is reversed through profit or loss.

Non financial assets

The Group assesses at each reporting date whether there is an indication that an asset may be impaired. If any indication exists, or when annual impairment testing for an asset is required, the Group estimates the asset's recoverable amount. An asset's recoverable amount is the higher of an asset's or cash-generating unit's (CGU) fair value less costs to sell and its value in use and is determined for an individual asset, unless the asset does not generate cash inflows that are largely independent of those from other assets or groups of assets. When the carrying amount of an asset or CGU exceeds its recoverable amount, the asset is considered impaired and is written down to its recoverable amount. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset.

All impairment losses are recognised in profit or loss and reversed only if there has been a change in the assumptions used to determine the asset's recoverable amount. The reversal is limited so that the asset's carrying amount does not exceed the carrying amount that would have been determined, net of depreciation, had no impairment loss been recognised.

3.16. Pensions

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

3.17. Provisions

Provisions are recognised when the Group has a present legal or constructive obligation as a result of past events, and it

is probable that an outflow of resources embodying economic benefits will be required to settle the obligation and a reliable estimate of the amount of obligation can be made.

3.18. Taxation

The Bank is not subject to any taxes except for import duties. At the same time the Bank acts as a tax agent according to the procedures envisaged by the laws of the Republic of Armenia. The Bank's subsidiaries are subject to income tax and other taxes on their operations in accordance with the laws of the Republic of Armenia.

3.19 Share capital

Share capital

Ordinary shares are classified as equity.

The promissory notes extended by the Government of the Republic of Armenia.

The promissory notes extended by the Government of the Republic of Armenia as envisaged by the article 11.4 of the Law of the Republic of Armenia on the Central Bank of Armenia to cover excess of the losses of the Bank over the general reserve is recognized as additional paid-in capital.

Dividends

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

3.20. Contingencies

Contingent liabilities are not recognised in the consolidated statement of financial position but are disclosed unless the possibility of any outflow in settlement is remote. A contingent asset is not recognised in the consolidated statement of financial position but disclosed when an inflow of economic benefits is probable.

3.21. Interest income and expense

For all financial instruments measured at amortised cost and interest bearing securities classified as available-for-sale, interest income or expense is recorded at the effective interest rate, which is the rate that exactly discounts estimated future cash payments or receipts through the expected life of the financial instrument or a shorter period, where appropriate, to

the net carrying amount of the financial asset or financial liability. The calculation takes into account all contractual terms of the financial instrument (for example, prepayment options) and includes any fees or incremental costs that are directly attributable to the instrument and are an integral part of the effective interest rate, but not future credit losses. The carrying amount of the financial asset or financial liability is adjusted if the Group revises its estimates of payments or receipts. The adjusted carrying amount is calculated based on the original effective interest rate and the change in carrying amount is recorded as interest income or expense.

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

3.22. Fee and commission income

Fees earned for the provision of services over a period of time are accrued over that period.

3.23. Future changes in accounting policies

Standards and interpretations issued but not yet effective

IFRS 9 Financial Instruments

In November 2009 and 2010 the IASB issued the first phase of IFRS 9 *Financial Instruments*. This Standard will eventually replace IAS 39 *Financial Instrument: Recognition and Measurement*. IFRS 9 becomes effective for financial years beginning on or after 1 January 2015. The first phase of IFRS 9 introduces new requirements on classification and measurement of financial instruments. In particular, for subsequent measurement all financial assets are to be classified at amortised cost or at fair value through profit or loss with the irrevocable option for equity instruments not held for trading to be measured at fair value through other comprehensive income. For financial liabilities designated at fair value through profit or loss using fair value option IFRS 9 requires the amount of change in fair value attributable to changes in credit risk to be presented in other comprehensive income. The Group now evaluates the impact of the adoption of new Standard and considers the initial application date.

IFRS 10 Consolidated Financial Statements

IFRS 10 establishes a single control model that applies to all entities including special purpose entities. The changes introduced by IFRS 10 will require management to exercise significant judgement to determine which entities are controlled, and therefore, are required to be consolidated by a

parent, compared with the requirements that were in IAS 27.In addition IFRS 10 introduces specific application guidance for agency relationships. IFRS 10 replaces the portion of IAS 27 *Consolidated and Separate Financial Statements* that addresses the accounting for consolidated financial statements. It also includes the issues raised in SIC-12 *Consolidation – Special Purpose Entities*. It is effective for annual periods beginning on or after 1 January 2013. Earlier application is permitted. Currently the Group evaluates possible effect of the adoption of IFRS 10 on its financial position and performance.

IFRS 11 Joint Arrangements

IFRS 11 removes the option to account for jointly controlled entities (JCEs) using proportionate consolidation. Instead, JCEs that meet the definition of a joint venture must be accounted for using the equity method. IFRS 11 supersedes IAS 31 *Interests in Joint Ventures* and SIC-13 *Jointly Controlled Entities-Non-monetary Contributions by Venturers* and is effective for annual periods beginning on or after 1 January 2013. Earlier application is permitted. The Group expects that adoption of IFRS 11 will have no effect on its financial position and performance.

IFRS 12 Disclosure of Interests in Other Entities

IFRS 12 includes all of the disclosures that were previously in IAS 27 related to consolidated financial statements, as well as all of the disclosures that were previously included in IAS 31 and IAS 28. These disclosures relate to an entity's interests in subsidiaries, joint arrangements, associates and structured entities. A number of new disclosures are also required. IFRS 12 is effective for annual periods beginning on or after 1 January 2013. Earlier application is permitted. Adoption of the standard will require new disclosures to be made in the financial statements of the Group but will have no impact on its financial position or performance.

IFRS 13 Fair Value Measurement

IFRS 13 establishes a single source of guidance under IFRS for all fair value measurements. IFRS 13 does not change when an entity is required to use fair value, but rather provides guidance on how to measure fair value under IFRS when fair value is required or permitted. IFRS 13 is effective for annual periods beginning on or after 1 January 2013. Earlier application is permitted. The adoption of the IFRS 13 may have effect on the measurement of the Bank's (Group's) assets and liabilities accounted for at fair value. Currently the Group evaluates possible effect of the adoption of IFRS 13 on its financial position and performance.

IAS 27 Separate Financial Statements (as revised in 2011)

As a consequence of the new IFRS 10 and IFRS 12, what remains of IAS 27 is limited to accounting for subsidiaries,

jointly controlled entities, and associates in separate financial statements. The amendment becomes effective for annual periods beginning on or after 1 January 2013.

IAS 28 Investments in Associates and Joint Ventures (as revised in 2011)

As a consequence of the new IFRS 11 and IFRS 12. IAS 28 has been renamed IAS 28 *Investments in Associates and Joint Ventures*, and describes the application of the equity method to investments in joint ventures in addition to associates. The amendment becomes effective for annual periods beginning on or after 1 January 2013.

Amendments to IFRS 7 Financial Instruments: Disclosures

The Amendments were issued in October 2010 and are effective for annual periods beginning on or after 1 July 2011. The amendment requires additional disclosure about financial assets that have been transferred but not derecognised to enable the user of the Group's financial statements to understand the relationship with those assets that have not been derecognised and their associated liabilities. In addition, the amendment requires disclosures about continuing involvement in derecognised assets to enable the user to evaluate the nature of, and risks associated with, the entity's continuing involvement in those derecognised assets. The amendment affects disclosure only and has no impact on the Group's financial position or performance.

Amendments to IAS 12 Income Taxes – Deferred tax: Recovery of Underlying Assets

In December 2010 the IASB issued amendments to IAS 12 effective for annual periods beginning on or after 1 January 2012. The amendment clarified the determination of deferred tax on investment property measured at fair value. The amendment introduces a rebuttable presumption that deferred tax on investment property measured using the fair value model in IAS 40 should be determined on the basis that its carrying amount will be recovered through sale. Furthermore, it introduces the requirement that deferred tax on non-depreciable assets that are measured using the revaluation model in IAS 16 always be measured on a sale basis of the asset. The Group now evaluates the impact of the adoption of these amendments.

Amendments to IAS 19 Employee Benefits

The IASB has published amendments to IAS 19 *Employee Benefits*, effective for annual periods beginning on or after 1 January 2013, which proposes major changes to the accounting for employee benefits, including the removal of the option for deferred recognition of changes in pension plan assets and liabilities (known as the "corridor approach"). In addition, these

amendments will limit the changes in the net pension asset (liability) recognised in profit or loss to net interest income (expense) and service costs. The Group expects that these amendments will have no impact on the Group's financial position.

Amendments to IAS 1 Changes to the Presentation of Other Comprehensive Income

The amendments to IAS 1 *Presentation of Financial Statements*, effective for annual periods beginning on or after 1 July 2012, change the grouping of items presented in other comprehensive income. Items that could be reclassified (or "recycled") to profit or loss at a future point in time (for example, upon derecognition or settlement) would be presented separately from items that will never be reclassified. These amendments will change presentation in the statement of comprehensive income but will have no effect on its financial position and performance.

Amendment to IFRS 1 Severe Hyperinflation and Removal of Fixed Dates for First-time Adopters

These amendments to IFRS 1, effective for annual periods beginning on or after 1 July 2011, introduce a new deemed cost exemption for entities that have been subject to severe hyperinflation. The Group expects that these amendments will have no impact on the Group's financial position.

Amendments to IAS 32

In December 2011, the IASB issued amendments to its current guidance in IAS 32 on offsetting financial assets and liabilities and has introduced new disclosure requirements in IFRS 7. The amendments to IFRS 7 are to be retrospectively applied for annual periods beginning on or after 1 January 2013 and the amendments to IAS 32 are to be retrospectively applied for annual periods beginning on or after 1 January 2014. Earlier application is permitted. The amendments to IAS 32 now clarify that rights to set-off must not only be legally enforceable in the normal course of business, but must also be enforceable in the event of default, bankruptcy or insolvency of all the counterparties to the contract. The amendments to IAS 32 also clarify that rights of set-off must not be contingent on a future event. The amendments to IAS 32 also clarify the offsetting criteria that the reporting entity is required to intend either to settle on a net basis, or to realize the asset and settle the liability simultaneously. The amendments to IFRS 7 require the reporting entity to disclose information about rights of set-off and related arrangements for all recognized financial instruments that are set off in accordance with IAS 32. The Group now evaluates the impact of the adoption of new amendments and considers the initial application date.

4. Interest income

(in thousand Armenian drams)

	2011	2010
Interest income from foreign currency assets		
Term deposits	1,485,131	1,834,407
Held to maturity assets	778,609	138,829
Nostro accounts	180,383	248,843
Placements with the IMF	33,309	60,756
Other	352	-
	2,477,784	**2,282,835**
Interest income from domestic currency assets		
Loans and reverse repurchase agreements	7,359,989	4,676,307
Available-for-sale assets	1,760,350	2,305,423
Held to maturity assets	282,082	270,049
Other	25	-
	9,402,446	**7,251,779**
	11,880,230	**9,534,614**

5. Interest expense

(in thousand Armenian drams)

	2011	2010
Interest expense on foreign currency liabilities		
Due to the IMF	3,383,675	2,571,362
Other borrowings	263,492	204,348
Other	26,994	17,320
	3,674,161	**2,793,030**
Interest expense from domestic currency assets		
Due to the Government of the Republic of Armenia	5,613,007	13,487,074
Deposits and accounts of financial and other institutions	770,412	313,078
Debt securities issued	8,930	-
Other	78,371	59,094
	6,470,720	**13,859,246**
	10,144,881	**16,652,276**

6. Net foreign exchange gain/(loss)

(in thousand Armenian drams)

	2011	2010 *(restated)*
Net gain/(loss) from revaluation of monetary assets and monetary liabilities	19,326,197	(12,099,588)
Net gain on spot transactions	593,752	137,125
Net loss on currency derivatives	(738,711)	(675,363)
	19,181,238	**(12,637,826)**

Included in the net gain/ (loss) loss from revaluation of monetary assets and liabilities is a foreign exchange revaluation gain of AMD 21,040,517 thousand on financial instruments at fair value through profit or loss (2010: loss in amount AMD 24,501,164 thousand).

7. Net gain on financial instruments at fair value through profit or loss

(in thousand Armenian drams)

	2011	2010
Net gain on assets under trust management (excluding foreign exchange revaluation*)	166,294	236,469
Net gain/(loss) on foreign securities under own management (excluding foreign exchange revaluation*)	2,492,809	6,599,921
Net gain/(loss) on money market instruments under own management	(3,577)	11,126
Net loss on futures under own management (excluding foreign exchange revaluation*)	(525,985)	(3,772,380)
Trust management fees (excluding foreign exchange revaluation*)	(132,185)	(131,961)
	1,997,356	**2,943,175**

** The foreign exchange revaluation of assets is included in "Net foreign exchange gain (loss). See Note 6.*

8. Other income

(in thousand Armenian drams)

	2011	2010
Financial agency fee of the Government of the Republic of Armenia	1,637,706	1,189,996
Numismatic coins	686,002	434,022
Credit registry	61,929	58,248
Other	418,688	219,387
	2,804,325	**1,901,653**

9. Costs of production of banknotes, coins and numismatics

(in thousand Armenian drams)

	2011	2010
Production of banknotes and coins	1,982,853	1,366
Production of numismatic coins	400,495	225,436
	2,383,348	**226,802**

10. Other expenses

(in thousand Armenian drams)

	2011	2010
Employee compensation, staff training and related payments	4,674,578	4,139,441
Promotion of economic education and research	2,000,000	500,000
Depreciation and amortization	1,223,482	731,035
Security	803,473	729,718
Repairs and maintenance	323,924	569,417
Professional services	183,542	240,330
Contribution to Deposit Guarantee Fund	-	5,000,000
Other	1,778,816	1,152,001
	10,987,815	**13,061,942**

11. Placements with banks and other financial institutions

(in thousand Armenian drams)

	2011	2010
Placements with banks and other financial institutions in foreign currency		
Nostro accounts	140,731,605	119,776,198
Term deposits	105,856,548	37,385,870
Cash included in assets under trust management	76,449	89,668
Accrued interest on deposits and nostro accounts	76,314	36,169
Margin requirement of interest rate futures	71,710	814,196
Other	18,420	-
	246,831,046	**158,102,101**
Allowance for impairment	(10,415,782)	-
	236,415,264	**158,102,101**
Allowance for impairment		
Opening balance	-	-
Increase in provision	(10,415,782)	-
Closing balance	**(10,415,782)**	**-**

Concentration of placements with banks and other financial institutions

As at 31 December 2011 and 2010 the Group had placements in 3 banks with individual balances exceeding 10% of total placements. The gross value of these balances as of 31 December 2011 and 2010 amounted to AMD 170,902,429 thousand and AMD 135,152,491 thousand, respectively.

The term deposits have up to 3 months remaining maturity with interest rates ranging from 0.15% to 3.6% (2010: up to one year, 0.69-4.5%).

12. Financial instruments at fair value through profit or loss

(in thousand Armenian drams)

	2011	2010
Assets		
Debt and other fixed-income instruments		
Foreign bonds	344,720,503	400,925,859
Money market instruments under own management	-	3,645,519
	344,720,503	**404,571,378**
Derivative financial instruments		
Interest rate futures contracts under own management	-	61,539
	344,720,503	**404,632,917**

Debt and other fixed-income instruments were, upon initial recognition, designated by the Group as financial assets at fair value through profit or loss.

As at 31 December 2011 foreign securities at fair value under own management include:

(in thousand Armenian drams)

	2011	2010
Government bonds	224,738,574	249,225,131
State agency bonds	33,517,440	40,569,775
Other securities	41,216,144	68,665,899
Total	299,472,158	358,460,805

As at 31 December 2011 the foreign bonds under trust management include:

(in thousand Armenian drams)

	2011	2010
Governments bonds	37,133,087	32,032,674
Corporate bonds	8,115,258	10,432,380
Total	**45,248,345**	**42,465,054**

Securities and derivative financial instruments under trust management represent financial instruments under discretionary asset management at IBRD. The risk exposure limits and investment guidance are set by the Group.

Derivative financial instruments

(in thousand Armenian drams)

	2011	2010 *(restated)*	2009	2011		2010 *(restated)*		2009	
	Nominal value			Asset	Liability	Asset	Liability	Asset	Liability
Commodity futures	1,624,742	1,350,189	-	-	2,961	-	4,629	-	-
Interest rate futures	2,445,368	10,913,063	14,806,747	-	535	-	14,849	-	36,588
Total foreign exchange futures contracts under trust management	**4,070,110**	**12,263,252**	**14,806,747**	**-**	**3,496**	**-**	**19,478**	**-**	**36,588**
Interest rate futures contracts under own management	192,268,980	467,176,740	1,136,105,882	-	-	61,539	-	-	-
Currency swap contracts	7,649,301	-	-	-	145,161	-	-	-	-
Currency forward contracts	47,925,837	27,293,893	-	-	1,622,588	-	675,363	-	-
Total	251,914,228	506,733,885	1,150,912,629	-	1,771,245	61,539	694,841	-	36,588

13. Investment securities

(in thousand Armenian drams)

	2011	2010
Available-for-sale investments in foreign currency		
Equity investments at cost		
SWIFT	1,646	917
	1,646	**917**
Available-for-sale investments in domestic currency		
Debt instruments		
Treasury bonds of the Government of the Republic of Armenia	12,952,668	12,124,141
Promissory note of the Government of the Republic of Armenia	77,512,700	55,644,010
	90,465,368	**67,768,151**
Equity investments at cost		
Other investments	16,457,617	20,937,614
	16,457,617	**20,937,614**
Total available-for-sale investments in domestic currency	**106,922,985**	**88,705,765**
Total available-for-sale investments	**106,924,631**	**88,706,682**
Held-to-maturity investments in foreign currency		
Foreign bonds	137,340,298	95,678,521
	137,340,298	**95,678,521**
Held-to-maturity investments in domestic currency		
Discount bond	4,414,997	4,132,916
Allowance for impairment	(1,149,081)	-
	3,265,916	**4,132,916**
Total held-to-maturity investments	**140,606,214**	**99,811,437**
Allowance for impairment of discount bond		
Opening balance	-	-
Increase in provision	(1,149,081)	-
Closing balance	**(1,149,081)**	**-**

In 2011 a non-interest on demand promissory note at par value of AMD 77,512,700 (2010: 55,644,010 thousand) thousand was issued by the Government of the Republic of Armenia as a gratis investment in the Bank. The promissory note was issued according to the Law on the Central Bank to cover the negative net assets of the Bank.

The management believes that the carrying amount of the bond approximates its fair value.

Available-for-sale debt investment securities of the Government of the Republic of Armenia are recorded at fair value determined using a valuation technique, which uses current market rates to discount future cash flows of the financial instruments.

14. International Monetary Fund

Assets due from the IMF

(in thousand Armenian drams)

	2011	2010
Placements with the IMF in foreign currency		
Membership quota in the IMF (subscription)	54,487,874	51,493,341
SDR holdings in the IMF	21,999,909	12,169,283
Accrued interest	1,563	7,613
	76,489,346	**63,670,237**

The Rupublic of Armenia is a member of the International Monetary Fund (the IMF). The Bank holds the quota for the Republic of Armenia membership in the IMF.

The Group maintains an SDR-denominated current account with the IMF used for processing and settlement of transactions with the IMF. This current account bears interest based on the SDR Interest Rate.

Liabilities due to the IMF

(in thousand Armenian drams)

	2011	2010 (restated)	2009 (restated)
Securities account	140,663,079	140,663,079	140,663,079
Adjustment account for AMD liabilities to the IMF	(2,916,354)	(6,677,555)	8,523,264
Account 1	90,168,906	61,814,443	23,367,610
Account 2	2,842	2,754	2,630
SDR allocation	52,112,119	49,248,152	52,125,764
ECF	25,906,615	32,565,060	42,837,498
Interest accrued	523,632	471,297	300,265
	306,460,839	**278,087,230**	**267,820,110**

For a part of its liabilities to the IMF and the membership quota the Group issued a promissory note.

The Securities account, Adjustment account and Accounts 1 represent the amounts of Stand-By Arrangement, Extended Fund Facility (the "ECF") and the quota. Accoun 2 is used by the IMF for administrative purposes.

The Group recieved the following loans from the IMF: Extended Credit Facility, Extended Fund Facility, and Stand-By Arrangement.

The Extended Credit Facility provides financial assistance to the countries with protracted balance of payments problems. The ECF was created under the newly established Poverty Reduction and Growth Trust (the PRGT) as part of a broader reform to make the IMF's financial support more flexible and

better tailored to the diverse needs of Low Income countries, including in times of crisis. As at 31 December 2011 the ECF bears no interest (2010: 0%, 2009: 0.5%). The loan matures in November, 2018. As at 31 December 2011 the amount witdrawn by the Group under these funds equaled to AMD 25,906,615 thousand (2010: AMD 32,565,060 thousand, 2009: AMD 42,837,498 thousand).

The Extended Fund Facility (the EFF) is provided to the countries to overcome medium-term payment problems. The EFF interest rate is floating and published by the IMF on weakly basis as Adjusted Rate of Charge. The loan matures in February, 2022. As at 31 December 2011 the amount witdrawn by the Group under these funds equaled to AMD 41,458,142 thousand (2010: AMD 19,589,845 thousand, 2009: AMD 0).

The Stand-By Arrangement (the SBA) is provided by the IMF to member countries to overcome their payment problems during crisis. The SBA interest rate is floating and published by the IMF on weakly basis as Adjusted Rate of Charge. The IMF accounts surcharge of 2% per annum on the part of the SBA and the EFF exceeding 300% of the membership quota. The SBA matures in March, 2015. As at 31 December 2011 amount witdrawn under these funds equaled to AMD 131,969,653 thousand (2010: AMD 124,716,781 thousand, 2009: AMD 118,051,813 thousand).

The IMF for the purpose of increasing the international reserves of the member countries makes SDR allocations in the member countries. The SDR allocation interest rate is floating and published by the IMF on weakly basis as SDR interest rate. The SDR allocation has no maturity date but can be cancelled by the IMF.

15. Loans and reverse repurchase agreements

(in thousand Armenian drams)

	2011	2010
Reverse repurchase agreements	46,345,414	8,022,812
Loans to resident financial institutions under arrangement with the KFW and World bank	42,439,125	29,643,307
Subordinated loans	30,285,580	24,536,382
Mortgage refinancing	21,477,990	-
Other loans	8,697,467	8,412,998
	149,245,576	**70,615,499**

Concentration of loans and reverse repurchase agreements

As at 31 December 2011, one counterparty bank had a balance individually exceeding 10% of total loans and reverse

repurchase agreements amount, which amounted to AMD 32,597,195 thousand (2010: 3 banks amounting to 26,618,171 thousand).

Loans to resident banks under the agreement with the KFW and World bank are provided to 14 domestic banks and 4 financial institutions at interest rates from 5.5% to 9% and having up to 12 years of maturity period. The Group has right to suspend amounts due from banks` correspondent accounts, otherwise all the rights and benefits of the colletoral is to be passed to the Group.

In consideration of Armenia's banking sector reliability and long-term stability, the Group has provided loans on subordinated terms to 10 banks at interest rate ranging from 7.5% to 8% and having 5 years of maturity, aimed to build sufficient capacity in the system to absorb potential crisis-derived risks.

Mortgage refinancing has been provided to financial institutions at interest rates ranging from 5.5% to 9.5% and up to 13 years of maturity period.

Included in the other loans is a single loan for mergers in the banking sector in amount of AMD 7,324,711 thousand (2010: AMD 7,325,216 thousand) at 7.5% percent interest rate and 2-year of maturity (2010: 7.5%, 3-year).

The Group accepted securities on reverse repurchase agreements as collateral for commercial loans, which the Group is permitted to sell or repledge. As of 31 December 2011 amounts receivable under reverse repurchase agreements are with 11 resident banks (2010: 5 banks) and are collateralised by the following securities.

(in thousand Armenian drams)

	2011 Fair value	2010 Fair value
Treasury bonds of The Government of the Republic of Armenia	46,289,474	8,131,931
	46,289,474	**8,131,931**

16. Property and equipment

(in thousand Armenian drams)

	Land and buildings	Networks, computer and other equipment	Vehicles	Construction in progress	Total
Cost					
Balance at 1 January 2010	4,398,993	6,351,261	306,793	10,762,869	21,819,916
Additions	195,408	719,514	10,268	10,366,036	11,291,226
Disposals	-	(569,592)	-	-	(569,592)
Transfer	2,543,324	1,476,546	-	(4,019,870)	-
Balance at 31 December 2010	**7,137,725**	**7,977,729**	**317,061**	**17,109,035**	**32,541,550**
Additions	53,914	455,080	43,140	13,021,550	13,573,684
Disposals	(719,280)	(649,450)	(29,503)	-	(1,398,233)
Transfer	9,887,781	77,911	-	(9,965,692)	-
Balance at 31 December 2011	**16,360,140**	**7,861,270**	**330,698**	**20,164,893**	**44,717,001**
Depreciation					
Balance at 1 January 2010	2,178,974	3,711,563	166,592	-	6,057,129
Charge for the period	116,632	573,990	40,413	-	731,035
Disposals	-	(558,803)	-	-	(558,803)
Transfer	-	-	-	-	-
Balance at 31 December 2010	**2,295,606**	**3,726,750**	**207,005**	-	**6,229,361**
Charge for the period	238,984	837,200	43,403	-	1,119,587
Disposals	(331,269)	(642,106)	(28,028)	-	(1,001,403)
Balance at 31 December 2011	**2,203,321**	**3,921,844**	**222,380**	-	**6,347,545**
Carrying amount					
At 31 December 2011	14,156,819	3,939,426	108,318	20,164,893	38,369,456
At 31 December 2010	4,842,119	4,250,979	110,056	17,109,035	26,312,189

17. Intangible assets

(in thousand Armenian drams)

	Computer software
Cost	
Balance at 1 January 2010	633,222
Additions	155,272
Disposals	-
Balance at 31 December 2010	**788,494**
Additions	172,455
Disposals	(97,971)
Balance at 31 December 2011	**862,978**
Amortization	
Balance at 1 January 2010	205,315
Charge for the period	-
Disposals	-
Balance at 31 December 2010	**205,315**
Charge for the period	103,895
Disposals	(86,621)
Balance at 31 December 2011	**222,589**
Carrying amount	
At 31 December 2011	640,389
At 31 December 2010	583,179

18. Other assets

(in thousand Armenian drams)

	2011	2010
Receivables and prepayments	5,117,579	2,836,231
Numismatic coins	960,172	739,624
Other	175,876	176,406
	6,253,627	**3,752,261**

Included in the receivables and prepayments is the prepayments connected with the construction in amount AMD 4,803,352 thousand (2010: AMD 2,209,974 thousand).

19. Deposits and accounts of financial and other institutions

(in thousand Armenian drams)

	2011	2010
Foreign currency liabilities		
Vostro accounts and deposits of domestic banks	102,512,913	88,236,533
Term deposit of Deposit Guarantee Fund	1,746,015	1,684,280
Current accounts of other legal entities	87,595	9,729,221
	104,346,523	**99,650,034**
Domestic currency liabilities		
Vostro accounts and deposits of domestic banks	166,362,507	77,124,832
Accounts of other legal entities	465,426	3,700,939
	166,827,933	**80,825,771**

Concentration of deposits and accounts of financial and other institutions

As of 31 December 2011 and 2010, two counterparty banks had balances individually exceeding 10% of total amount of deposits and accounts of financial and other institutions amounting to AMD 96,773,190 thousand and 38,596,273 thousand, respectively.

Term deposits due to Deposit Guarantee Fund mature in 2012 at floating rate based on 6m EURIBOR.

20. Other borrowed funds

(in thousand Armenian drams)

	2011	2010
Due to the KFW	23,338,090	16,610,289
Due to the World Bank	15,508,204	10,989,520
	38,846,294	**27,599,809**

The loans due to the KFW are provided under an intergovernmental agreement on financial cooperation between the Government of the Republic of Armenia and the Federal Republic of Germany to finance special loan programs placed through domestic commercial banks (Note 15). The loans mature from 2011 through 2048, and bear interest of 0.75-2.3% for the used part of the loan, and 0.25% for the unused part of the loan. The repayment of loans to the KFW is guaranteed by the Government of the Republic of Armenia.

The loan due to the World Bank is provided by the World Bank for financing small and medium enterprises through domestic commercial banks (Note 15). The loan matures in 2035, and bears interest of 0.5%.

During the periods presented the Bank did not have any defaults of principal, interest or other breaches with respect to its liabilities.

21. Other liabilities

(in thousand Armenian drams)

	2011	2010
Payables	2,500,577	822,826
Demand deposits of employees	755,223	531,068
	3,255,800	**1,353,894**

22. Due to the Government of the Republic of Armenia

(in thousand Armenian drams)

	2011	2010
Foreign currency liabilities		
Current accounts of the Government of the Republic of Armenia	3,964,955	1,187,537
Payables	9,979	2,801,575
	3,974,934	**3,989,112**
Domestic currency liabilities		
Current accounts of the Government of the Republic of Armenia	40,130,613	27,315,188
Term deposits	40,098,806	79,230,385
	80,229,419	**106,545,573**

As of 31 December 2011 term deposits of the Government of RA have remaining maturity up to 3 months at interest rate ranging from 10.67-11.67% (2010: 7.45%-8.29%).

23. Equity

Issued capital

The issued capital of the Bank is owned by the Republic of Armenia and cannot be pledged, sold or otherwise disposed.

Additional paid in capital

Additional paid in capital represents a contribution made by the Government of the Republic of Armenia in the form of a promissory note (Note 13).

General reserve

The general reserve is formed according to law on the Central Bank of the Republic of Armenia and cannot be distributed.

24. Commitments

Capital commitments

The capital commitments outstanding at 31 December 2011 related to the construction of the Group's premises is AMD 17,720,517 thousand (2010: AMD 14,541,725 thousand).

Litigation

The Group management is unaware of any actual, pending or threatened significant claims against the Bank.

Guarantees

As at 31 December 2011 and 2010 the Bank has given guarantees in the amount of AMD 658,000 thousand issued from 1994 to 1995 on behalf of construction companies and relates to earthquake zone construction. Guarantees represent irrevocable assurance that the bank will make payments in the event that a customer cannot meet its obligations to third parties and carry credit risk.

25. Related party transactions

Transactions with members of the key management

Total remuneration is included in employee compensation, staff training and related payments (Note 10).

(in thousand Armenian drams)

	2011	2010
Key management including the Bank's Board members	220,502	209,580
Social security costs	18,923	18,017

The outstanding balances and average effective interest rates as of 31 December 2011 with members of the key management are as follows:

(in thousand Armenian drams)

	2011	Average effective Interest rate	2010	Average effective Interest rate
Consolidated statement of financial position				
Assets				
Loans				
Balance at 1 January	**65,674**		**76,832**	
Additions	6,996		19,837	
Disposal	(35,284)		(30,973)	
Movement	(10)		(22)	
Balance at 31 December	**37,376**	**3-5%**	**65,674**	**3-5%**
Liabilities				
Deposits				
Balance at 1 January	**59,785**		**43,025**	
Additions	84,945		74,435	
Disposal	(23,525)		(57,568)	
Movement	30		(107)	
Balance at 31 December	121,235	13.5%	59,785	14%
Salary payable	7,660	-	-	-

Amounts included in the statement of comprehensive income in relation to transactions with the key management are as follows:

(in thousand Armenian drams)

	2011	2010
Statement of comprehensive income		
Interest expense	(9,574)	(6,142)
Interest income	2,520	3,294

Transactions with the Government of the Republic of Armenia

The outstanding balances and average effective interest rates as of 31 December 2011 with the Government of the Republic of Armenia are as follows:

(in thousand Armenian drams)

	2011	Average effective Interest rate	2010	Average effective Interest rate
Consolidated statement of financial position				
Assets				
The Government of Republic of Armenia treasury bonds (Note 13)	12,952,668	11.5%	12,124,141	11%
The Government of Republic of Armenia promissory note extended to the Bank as additional paid in capital (Note 13)				
Balance at 1 January	55,644,010		79,629,720	
Additions	21,868,690		0	
Disposal	-		(23,985,710)	
Balance at 31 December	77,512,700	0.00%	55,644,010	0.00%
Liabilities				
Due to the Government of the Republic of Armenia (domestic currency, Note 22)	80,229,419	10%	106,545,573	10%
Due to the Government of the Republic of Armenia (foreign currency, Note 22)	3,974,934	0.00%	3,989,112	0.00%

The movement of deposits included in liabilities due to the Government of the Republic of Armenia, in domestic currency:

(in thousand Armenian drams)

	2011	2010
Balance at 1 January	79,230,385	131,051,654
Additions	630,269,499	688,363,583
Disposal	(669,401,078)	(740,184,852)
Balance at 31 December	40,098,806	79,230,385

Amounts included in the statement of comprehensive income in relation to transactions with the Government of the Republic of Armenia are as follows:

(in thousand Armenian drams)

	2011	2010
Consolidated statement of comprehensive income		
Interest income	1,760,350	2,305,423
Net foreign exchange gain	2,194,298	782,980
Interest expense	(5,613,007)	(13,487,074)

In 2011 the building with carrying value of AMD 371,656 thousand was granted to the Government of the Republic of Armenia.

According to the agreement with the Government of the Republic of Armenia in 2012 the Group is obliged to exchange main foreign currency denominated state budget inflows and outflows at 378.96 AMD per one US dollar (357.98 in 2011) and as at 31 December 2011 the Government of the Republic of Armenia has a right to purchase US dollars at 370.17 AMD per one US dollar from the Group in amounts required to service 39.98% (2010: 35.40%) of the debt amounting to 500 million US dollars of the Government of the Republic of Armenia to Russian Federation in accordance with the loan agreement dated 20 May 2009.

Transactions with the Deposit Guarantee Fund

(in thousand Armenian drams)

	2011	Average effective Interest rate	2010	Average effective Interest rate
Consolidated statement of financial position				
Liabilities				
Due to the Deposit Guarantee Fund (domestic currency, Note 19)	6,102	0.00%	119,710	0.00%
Due to the Deposit Guarantee Fund (foreign currency, Note 19)	1,746,015	1.73%	1,684,280	1.13%

(in thousand Armenian drams)

	2011	2010
Consolidated statement of comprehensive income		
Interest expense	26,994	17,320
Other expense	-	5,000,000

26. Cash and cash equivalents

Cash and cash equivalents at the end of the financial year as shown in the statement of cash flows is composed of the following items:

(in thousand Armenian drams)

	2011	2010
Cash	5,013,113	7,552,047
Nostro accounts (Note 11)	140,731,605	119,776,198
SDR holdings in the IMF (Note 14)	21,999,909	12,169,283
	167,744,627	**139,497,528**

27. Fair value of financial instruments

The Bank estimates the fair value of most financial assets and liabilities not to be materially different from their carrying values. The estimated fair values of its financial assets and liabilities, except for available-for-sale assets held in unquoted equity securities, is calculated using discounted cash flow techniques based on estimated future cash flows and discount rates for a similar instruments at the reporting date.

(in thousand Armenian drams)

	Carrying value 2011	Fair value 2011	Unrecognised gain/(loss) 2011	Carrying value 2010	Fair value 2010	Unrecognised gain/(loss) 2010
Financial assets						
Cash	5,013,113	5,013,113	-	7,552,047	7,552,047	-
Placements with banks and other financial institutions	236,415,264	236,415,264	-	158,102,101	158,102,101	-
Loans and reverse repurchase agreements	149,245,576	146,152,233	(3,093,343)	70,615,499	69,409,942	(1,205,557)
Placements with the IMF	76,489,346	76,489,346	-	63,670,237	63,670,237	-
Financial instruments at fair value through profit or loss	344,720,503	344,720,503	-	404,632,917	404,632,917	-
Investment securities:						
- available-for-sale assets	106,924,631	106,924,631	-	88,706,682	88,706,682	-
- held-to-maturity	140,606,214	140,505,420	(100,794)	99,811,437	99,804,546	(6,891)
Financial liabilities						
Deposits and accounts of financial and other institutions	271,174,456	271,174,456	-	180,475,805	180,475,805	-
Due to the Government of the Republic of Armenia	84,204,353	84,204,353	-	110,534,685	110,534,685	-
Financial liabilities at fair value through profit or loss	1,771,245	1,771,245	-	694,841	694,841	-
Due to the IMF	306,460,839	306,460,839	-	278,087,230	278,087,230	-
Debt securities issued	963,593	963,593	-	-	-	-
Other borrowed funds	38,846,294	38,846,294	-	27,599,809	27,599,809	-
Total unrecognised change in unrealised fair value			**(3,194,137)**			**(1,212,448)**

The estimates of fair value are intended to approximate the amount for which a financial instrument could be exchanged between knowledgeable, willing parties in an arm's length transaction. However given the uncertainties and the use of subjective judgment, the fair value should not be interpreted as being realisable in an immediate sale of the assets or settlement of liabilities.

Fair value hierarchy

Financial assets and liabilities measured at fair value in the statement of financial position are presented according to the

fair value hierarchy. The hierarchy divides the financial assets and liabilities into three levels based on the materiality of instruments used when measuring their fair value. The fair value hierarchy has the following three levels:

- Level 1: quoted prices on active markets for the same assets and liabilities (non-adjusted);
- Level 2: inputs, other than quoted prices specified in Level 1, which are observable for the asset and liability directly (i.e. as prices) and indirectly (i.e. available based on prices);
- Level 3: inputs which are not based on observable market data (non-observable inputs).

(in thousand Armenian drams)

	2011			
	Level 1	Level 2	Level 3	Total
Financial assets				
Financial instruments at fair value through profit or loss	325,964,611	18,755,892	-	344,720,503
Available-for-sale assets	-	12,952,668	-	12,952,668
Total	325,964,611	31,708,560	-	357,673,171
Financial liabilities				
Financial liabilities at fair value through profit or loss	3,496	-	1,767,749	1,771,245
Total	3,496	-	1,767,749	1,771,245
Net fair value	**325,961,115**	**31,708,560**	**(1,767,749)**	**355,901,926**

(in thousand Armenian drams)

	2010			
	Level 1	Level 2	Level 3	Total
Financial assets				
Financial instruments at fair value through profit or loss	393,650,370	10,921,008	-	404,571,378
Available-for-sale assets	-	12,124,141	-	12,124,141
Derivative financial assets	61,539	-	-	61,539
Total	393,711,909	23,045,149	-	416,757,058
Financial liabilities				
Financial liabilities at fair value through profit or loss	19,478	-	675,363	694,841
Total	19,478	-	675,363	694,841
Net fair value	**393,692,431**	**23,045,149**	**(675,363)**	**416,062,217**

Impact on fair value of level 3 financial instruments measured at fair value of changes to key assumptions

The following table shows the impact on the fair value of level 3 instruments of using reasonably possible alternative assumptions:

(in thousand Armenian drams)

	31 December 2011		31 December 2010	
	Carrying amount	Effect of reasonably possible alternative assumptions	Carrying amount	Effect of reasonably possible alternative assumptions
Financial liabilities				
Financial liabilities at fair value through profit or loss	1,767,749	(347,808)	675,363	(135,677)

In order to determine reasonably possible alternative assumptions the Group adjusted key unobservable model inputs as follows:

- For currency derivatives the Group adjusted the country credit spread assumptions by decreasing the assumptions by 1 per cent, which is considered by the Group to be within a range of reasonably possible alternatives based on credit spreads of countries with similar risk profiles.

28. Risk management

Introduction

Risk is inherent in the Group's activities but it is managed through a process of ongoing identification, measurement and monitoring, subject to risk limits and other controls. This process of risk management is critical to the Group's continuing profitability and each individual within the Group is accountable for the risk exposures relating to his or her responsibilities. The Group is exposed to credit risk, liquidity risk and market risk, the latter being subdivided into trading and non-trading risks. It is also subject to operating risks.

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

Risk management structure

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

Board

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

Audit Group

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

Institutional framework

International reserves of the Republic of Armenia are Central Bank claims on non-residents in freely convertible foreign currencies. The reserves are reflected in the consolidated statement of financial position of the Central Bank of Armenia (CBA). The CBA manages the reserves in accordance with the principles envisaged by the article 52 of the "LAW of Republic of Armenia on the Central Bank of Armenia", by investing the reserves within the Investment framework set by the Board of the CBA.

The reserves can be used to finance external payments/trade imbalances, to regulate indirectly the impact of such imbalances on the exchange rate, and to ensure the international obligations of Armenia are duly performed. The CBA uses reserves to provide foreign exchange services to the Government and state agencies of Armenia, e.g. foreign currency conversions or external debt servicing.

Starting from 2007 the Central Bank of Armenia has established a new reserve management framework in compliance with best international practices. First of all, strategic and tactical decision-making were separated and segregation of responsibilities for the decision-making at the levels of the Board, the Investment Committee and reserve management dealers (the Foreign Markets Operations unit of the Financial Department of the Bank) was adopted. In other words, the Group adopted a three level decision-making system, whereby the Bank's Board sets the Strategic Asset Allocation framework for the reserves management for a long-term time horizon (3 years), whereas the Investment Committee of the Bank was given executive power on short-term tactical benchmarks. Portfolio managers, in turn, have been delegated

authority to decide on current management issues within the framework of tactical benchmarks and active risk tolerance.

Administration and control

According to the Group's structure, the Financial Department is responsible for Armenia's international reserves management. The Foreign Markets Operations unit of the Financial Department is in charge of operations related day-to-day management of reserves. The International Risk Management unit is responsible for risks assessment, development of strategic asset allocation and benchmarking, compliance monitoring, performance evaluation and reporting.

Investment Committee as a rule meets once a month to discuss issues related to reserves management. The Committee includes heads of structural units involved in the entire process of reserves management, as well as the Bank's Chairman and Deputy Chairman. Formerly, the Committee was only a consultative body but, after the introduction of the three level system for management, it has been granted executive power. The Financial Department reports on the performance of reserves management to the Investment Committee on a quarterly basis and to the Bank's Board on a semi-annual basis. Each quarter the Bank presents information on condition and composition of international reserves to the Government and the National Assembly, and makes that information publicly available.

Reserve management process is under the control of the Bank's Audit Group, which reports directly to the Board.

Asset allocation and risk management

According to the principles set forth in article 52 of the Armenian Law on “The Central Bank”, Armenia's international reserves are managed based on with the principle of profit maximization while ensuring proper liquidity and security of reserves. For this purpose, the Financial Department develops drafts of strategic asset allocation and tactical benchmarks subject to approval by the Bank's Board and the Investment Committee, respectively. The investment benchmarks include all limits and rules governing the investment process as well as the structure of assets consistent with the reserves management principles set by the Board.

Credit risk

Credit risk is the risk that the Group will incur a loss because its customers, clients or counterparties failed to discharge their contractual obligations. The Group manages and controls credit risk by setting limits on the amount of risk it is willing to accept for individual counterparties and for geographical and industry concentrations, and by monitoring exposures in relation to such limits.

The Group has established a credit quality review process to provide early identification of possible changes in the credit-worthiness of counterparties. The Central Bank of the Republic of Armenia evaluates the counterparty creditworthiness based on the credit ratings assigned by leading internationally recognized credit rating agencies.

The Group sets minimum rating requirement for securities issued by governments, government agencies, other government authorities, and supranational organizations. These ratings cannot be lower than AA- (S&P)/Aa3 (Moody's) for long-term issues and A1+ (S&P)/P1 (Moody's) for short-term issues.

To monitor the credit risk the Group uses an in-house developed model, which allows assessing the issuer default probability based on stock prices and balance sheet data. It belongs to the class of structural models, providing an economically meaningful explanation of default based on the asset-liability structure and financial leverage. The model is based on the barrier option price equation which is one of components of implied rating issued by FITCH. Ratings and model results are used to build a matrix of investment limits for each rating group, maturity, individual counterparties, and asset classes. The matrix is the main tool for the credit risk management.

Derivative financial instruments

Credit risk arising from derivative financial instruments is, at any time, limited to those with positive fair values, as recorded in the consolidated statement of financial position.

Maximum credit risk without collateral or other credit enhancement

The table below presents the worst scenario of the Group's exposure to credit risk as of 31 December 2011, and 31 December 2010, without consideration of security.

(in thousand Armenian drams)

	Note	Gross maximum risk, as of 31 December 2011	Gross maximum risk, as of 31 December 2010
Placements with banks and other financial institutions	11	246,831,046	158,102,101
Financial instruments at fair value through profit or loss	12	344,720,503	404,632,917
Loans and reverse repurchase agreements	15	149,245,576	70,615,499
Available-for-sale assets	13	106,924,631	88,706,682
Held-to-maturity assets	13	141,755,295	99,811,437
Placements with the IMF	14	76,489,346	63,670,237
Total credit risk		1,065,966,397	885,538,873

Where financial instruments are recorded at fair value, the amounts above presented will denote the current risk but not the maximum one, which may arise in future as a result of changes in fair value.

Credit quality per class of financial assets

The credit quality of financial assets is managed by the Group internal credit ratings. The table below shows the credit quality by class of asset for loan-related lines in the consolidated statement of financial position, based on the Group's credit rating system.

In the table below loans to banks and customers of high grade are those having a minimal level of credit risk, normally with a credit rating on or close to sovereign level or very well collateralized. Other borrowers with good financial position and good debt service are included in the standard grade. Sub-standard grade comprises loans below standard grade but not individually impaired. For debt securities high grade is equivalent to Moody's Baa3 rating and above, sub-standard-below Baa3 but above B3, standard-below B3.

(in thousand Armenian drams)

	Notes	Neither past due nor impaired			Individually impaired 2011	Total 2011
		High grade 2011	Standard grade 2011	Sub-standard grade 2011		
Placements with banks and other financial institutions	11	212,050,966	-	-	24,364,298	236,415,264
Loans and reverse repurchase agreements	15	-	149,245,576	-	-	149,245,576
Available-for-sale assets		1,646	106,922,985	-	-	106,924,631
Held to maturity assets	13	137,340,298	-	-	3,265,916	140,606,214
Total		**349,392,910**	**256,168,561**		**27,630,214**	**633,191,685**

(in thousand Armenian drams)

	Notes	Neither past due nor impaired			Total 2010
		High grade 2010	Standard grade 2010	Sub-standard grade 2010	
Placements with banks and other financial institutions	11	125,300,174	32,801,927	-	158,102,101
Loans and reverse repurchase agreements	15	-	70,615,499	-	70,615,499
Available-for-sale assets		917	88,705,765	-	88,706,682
Held to maturity assets	13	95,678,521	4,132,916	-	99,811,437
Total		**220,979,612**	**196,256,107**	**-**	**417,235,719**

Impairment assessment

The main considerations for the loan impairment assessment include whether any payments of principal or interest are overdue by more than 30 days or there are any known difficulties in the cash flows of counterparties, credit rating downgrades, or infringement of the original terms of the contract. The Group addresses impairment assessment in two areas: individually assessed allowances and collectively assessed allowances.

Individually assessed allowances

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

Collectively assessed allowances

Allowances are assessed collectively for losses on loans to customers that are not individually significant and for individually significant loans where there is not yet objective evidence of individual impairment. Allowances are evaluated on each reporting date with each portfolio receiving a separate review.

The collective assessment takes account of impairment that is likely to be present in the portfolio even though there is no

yet objective evidence of the impairment in an individual assessment. Impairment losses are estimated by taking into consideration of the following information: historical losses on the portfolio, current economic conditions, the appropriate delay between the time a loss is likely to have been uncured and the time it will be identified as requiring an individually assessed impairment allowance, and expected receipts and recoveries once impaired. Local management is responsible for deciding the length of this period which can extend for as long as one year. The impairment allowance is then reviewed by credit management to ensure alignment with the Group's overall policy.

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

The geographical concentration of Group's monetary assets and liabilities is set out below:

(in thousand Armenian drams)

	2011			
	Armenia	**OECD**	**CIS and other foreign banks**	**Total**
Assets				
Cash	5,013,113	-	-	5,013,113
Placements with banks and other financial institutions	–	212,049,951	24,365,313	236,415,264
Financial instruments at fair value through profit or loss	–	344,720,503	–	344,720,503
Loan and reverse repurchase agreements	149,245,576	–	–	149,245,576
Available-for-sale assets	106,922,985	1,646	–	106,924,631
Held-to-maturity assets	–	137,340,298	3,265,916	140,606,214
Placements with the IMF	–	76,489,346	–	76,489,346
Property and equipment and intangible assets	39,009,845	–	–	39,009,845
Other assets	7,481,713	–	–	7,481,713
	307,673,232	**770,601,744**	**27,631,229**	**1,105,906,205**
Liabilities				
Notes and coins in circulation	398,777,362	-	-	398,777,362
Deposits and accounts of financial and other institutions	271,126,358	48,098	-	271,174,456
Financial liabilities at fair value through profit or loss	1,767,750	3,495	-	1,771,245
Due to the Government of the Republic of Armenia	84,204,353	-	-	84,204,353
Due to the IMF	-	306,460,839	-	306,460,839
Other borrowed funds	-	38,846,294	-	38,846,294
Debt securities issued	963,593	-	-	963,593
Other liabilities	3,409,701	-	-	3,409,701
	760,249,117	**345,358,726**	**-**	**1,105,607,843**
Net assets	**(452,575,885)**	**425,243,018**	**27,631,229**	**298,362**

(in thousand Armenian drams)

	2010			
	Armenia	OECD	CIS and other foreign banks	Total
Assets				
Cash	7,552,047	-	-	7,552,047
Placements with banks and other financial institutions	-	125,299,120	32,802,981	158,102,101
Financial instruments at fair value through profit or loss	-	404,632,917	-	404,632,917
Loan and reverse repurchase agreements	70,615,499	-	-	70,615,499
Available-for-sale assets	88,705,765	917	-	88,706,682
Held-to-maturity assets	-	95,678,521	4,132,916	99,811,437
Placements with the IMF	-	63,670,237	-	63,670,237
Property and equipment and intangible assets	26,895,368	-	-	26,895,368
Other assets	4,626,753	-	-	4,626,753
	198,395,432	**689,281,712**	**36,935,897**	**924,613,041**
Liabilities				
Notes and coins in circulation	348,164,734	-	-	348,164,734
Deposits and accounts of financial and other institutions	180,404,021	71,784	-	180,475,805
Financial liabilities at fair value through profit or loss	675,363	19,478	-	694,841
Due to the Government of the Republic of Armenia	110,534,685	-	-	110,534,685
Due to the IMF	-	278,087,230	-	278,087,230
Other borrowed funds	-	27,599,809	-	27,599,809
Debt securities issued	-	-	-	-
Other liabilities	1,499,990	-	-	1,499,990
	641,278,793	**305,778,301**	-	**947,057,094**
Net assets	**(442,883,361)**	**383,503,411**	**36,935,897**	**(22,444,053)**

Liquidity risk and funding management

Liquidity risk is the risk that the Group will be unable to meet its payment obligations when they fall due under normal and stress circumstances. As a fiscal agent of the Government and the monetary authority of the Republic of Armenia, the Bank is responsible for public debt service, the Government's foreign payments service and for smoothing out sharp fluctuations in national currency in the domestic market. From this perspective proper cash and liquidity management is crucial.

Based on the international reserve management objectives and grouping liquidity needs based liabilities' term structure, Armenia's international reserves have been divided into three

tranches – working capital, liquidity and investment tranches. While the first two are designed to meet short-term/instant and mid-term liquidity requirements, the purpose of the investment tranche is accumulation of wealth.

Depending on the designation of portfolio/tranche the policy varies in terms of benchmarks and the choice between active or passive management.

Analysis of financial liabilities by remaining contractual maturities

The tables below summarize the maturity profile of the Group's financial liabilities at 31 December based on contractual undiscounted repayment obligations except for trading derivatives which are shown at fair value in a separate column and gross settled derivatives which are shown by contractual maturity. Repayments which are subject to notice are treated as if notice were to be given immediately. However, the Group expects that many counterparties will not request repayment on the earliest date the Group could be required to pay and the table does not reflect the expected cash flows indicated by the Bank's deposit retention history.

(in thousand Armenian drams)

	2011						
	Demand or less than 1 month	1 to 3 months	3 months to 1 year	1 year to 5 years	More than 5 years	No maturity	Total
Financial liabilities							
Notes and coins in circulation	-	-	-	-	-	398,777,362	398,777,362
Deposits and accounts of financial and other institutions	269,428,441	7,460	1,768,724	-	-	-	271,204,625
Financial liabilities at fair value through profit or loss	1,771,245	-	-	-	-	-	1,771,245
Due to the Government of the Republic of Armenia	44,105,548	40,497,830	-	-	-	-	84,603,378
Due to the IMF	106,618,215	-	45,125,117	131,504,618	23,809,952	-	307,057,902
Other borrowed funds	-	-	360,427	17,886,032	26,255,488	-	44,501,947
Debt securities issued	-	-	1,000,000	-	-	-	1,000,000
Total non-discounted financial liabilities	**421,923,449**	**40,505,290**	**48,254,268**	**149,390,650**	**50,065,440**	**398,777,362**	**1,108,916,459**

(in thousand Armenian drams)

	2010						
	Demand or less than 1 month	1 to 3 months	3 months to 1 year	1 year to 5 years	More than 5 years	No maturity	Total
Financial liabilities							
Notes and coins in circulation	-	-	-	-	-	348,164,734	348,164,734
Deposits and accounts of financial and other institutions	180,489,100	-	-	-	-	-	180,489,100
Financial liabilities at fair value through profit or loss	694,841	-	-	-	-	-	694,841
Due to the Government of the Republic of Armenia	83,771,724	27,156,571	-	-	-	-	110,928,295
Due to the IMF	120,364,074	-	8,523,491	148,181,976	1,487,336	-	278,556,877
Other borrowed funds	-	-	238,146	1,585,982	30,393,480	-	32,217,608
Debt securities issued							
Total non-discounted financial liabilities	**385,319,739**	**27,156,571**	**8,761,637**	**149,767,958**	**31,880,816**	**348,164,734**	**951,051,455**

Market risk

Market risk is the risk that the fair value or future cash flows of financial instruments will fluctuate due to changes in market variables such as interest rates, foreign exchanges, and equity prices. The Group classifies exposures to market risk into either trading or non-trading portfolios. The market risk for the trading portfolio is managed and monitored based on sensitivity analysis. Non-trading positions are managed and monitored using other sensitivity analysis. Except for the concentrations within foreign currency, the Group has no significant concentration of market risk.

Market risk – Non-trading

Interest rate risk

Interest rate risk arises from the possibility that changes in interest rates will affect future cash flows or the fair values of financial instruments. The following table demonstrates the sensitivity to a reasonable possible change in interest rates, with all other variables held constant, of the Group's consolidated statement of comprehensive income.

Within the three level management structure the Board defines the overall risk tolerance, which is the acceptable level of interest rate risk in the long run. It also outlines portfolio optimization principles. The risk tolerance is defined as a minimum acceptable return over a certain period of time (now 3

years) with a 95 percent confidence level. The authority to set tactical benchmarks is delegated to the Investment Committee.

The purpose of tactical benchmarks is to maximize return in a shorter period (1 year). In contrast to strategic decisions, benchmarks take into account current market trends and forecasts. Optimal portfolios are constructed based on scenario analysis using VAR-MGARCH model simulated yield curves as well as internal and market consensus expectations on interest rates and credit spreads. For optimal portfolio selection Markowitz Model with certain limitations is used.

For risk monitoring, the Risk Management division of the Financial Department uses a number of widely used risk measures like Key Rate Duration, Information Ration, Spread Duration, PCA Duration, and Tracking Error.

The following table demonstrates the sensitivity of the Bank's equity, which is calculated by revaluing fixed rate available-for-sale assets at 31 December 2011 for the effects of the assumed changes in interest rates. The sensitivity of equity is analysed by maturity of the asset. The sensitivity of equity is based on the assumption that there are parallel shifts in the yield curve.

(in thousand Armenian drams)

Currency	Change in Yield Curve 2011	Effect on profit 2011	Change in Yield Curve 2010	Effect on profit 2010
AMD	+6.57%	(3,529,492)	+6.57%	(4,105,305)
AMD	-6%	3,223,281	-6%	3,749,137

The following table demonstrates the sensitivity to profit of the Bank, which is calculated by revaluing financial instruments at fair value through profit and loss as of 31 December 2011, based on the assumption of changing interest rates.

Currency	Increase in basis points 2011	Sensitivity of net interest income 2011	Increase in basis points 2010	Sensitivity of net interest income 2010
SDR	15	(305,308)	100	(1,813,855)
AMD	15	(17,890)	100	(51,491)
USD	15	(23,216)	100	(109,505)
EUR	15	(11,879)	100	(17,456)

Currency	Decrease in basis points 2011	Sensitivity of net interest income 2011	Decrease in basis points 2010	Sensitivity of net interest income 2010
SDR	-15	305,308	-25	453,464
AMD	-15	17,890	-25	12,873
USD	-15	23,216	-25	27,376
EUR	-15	11,879	-25	4,364

Currency risk

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

The following table shows the currencies which can affect the Bank's non-commercial dram-denominated assets and liabilities and projected flows thereon, as of 31 December, 2011. The analysis measures the impact of possible foreign currency fluctuations vis-à-vis the Armenian dram (provided that other variables remain constant) on profit or loss determined by the change in fair value of non-commercial dram-denominated assets and liabilities sensitive to the foreign currency. In the table below, the negative value denotes net potential decrease while the positive value denotes net potential increase, in profit or loss or in equity.

Currency	Increase in currency rate in % 2011	Effect on profit 2011	Increase in currency rate in % 2010	Effect on profit 2010
EUR	17.23%	32,384,098	25.00%	40,947,634
GBP	14.18%	6,484,220	17.58%	4,361,370
JPY	16.46%	11,276,229	25.00%	19,156,602
USD	11.13%	30,866,071	10.15%	27,399,128
SDR	14.18%	(32,611,118)	17.58%	(37,685,905)

Currency	Decrease in currency rate in % 2011	Effect on profit 2011	Decrease in currency rate in % 2010	Effect on profit 2010
EUR	-17.23%	(32,384,098)	-25.00%	(40,947,634)
GBP	-14.18%	(6,484,220)	-17.58%	(4,361,370)
JPY	-16.46%	(11,276,229)	-25.00%	(19,156,602)
USD	-11.13%	(30,866,071)	-10.15%	(27,399,128)
SDR	-14.18%	32,611,118	-17.58%	37,685,905

The currency composition of reserves is defined for each liquidity tranche, aiming to hedge the factors underlying the creation of each tranche. Armenia's foreign public debt is the major reason for holding reserves and is the main foreign currency demand driving factor. As a result, the currency composition of the reserves mainly mirrors the currency composition of debt. Currency composition for short term liquidity tranche is affected by the composition of the flows generated from foreign trade as well as possible intervention needs and current payments. The currency composition is subject to revision at least semi-annually.

Prepayment risk

Prepayment risk is the risk that the Group will incur a financial loss because its customers and counterparties repay or request repayment earlier or later than expected, such as fixed rate mortgages when interest rates fall.

The Group uses regression models to project the impact of varying levels of prepayment on its net interest income. The model makes a distinction between the different reasons for repayment (e.g. relocation, refinancing and renegotiation) and takes into account the effect of any prepayment penalties. The model is back tested against actual outcomes.

The effect on profit before tax for one year and on equity, assuming 10% of repayable financial instruments were to prepay at the beginning of the year, with all other variables held constant, is as follows:

	Effect on net interest income
2011	(20,362)
2010	(25,393)

Operational risk

Operational risk is the risk of loss arising from systems failure, human error, fraud or external events. When controls fail to perform, operational risks can cause damage to reputation, have legal or regulatory implications, or lead to

financial loss. The Group cannot expect to eliminate all operational risks, but a control framework and monitoring and responding to potential risks could be effective tools to manage the risks. Controls should include effective segregation of duties, access, authorisation and reconciliation procedures, staff education and assessment processes, including the use of internal audit.

29. Maturity analysis

The following table shows banking assets and liabilities by remaining contractual maturity dates as at 31 December 2011 and 2010. As most financial instruments of the Bank have fixed rates, the contract maturities present the dates on which the contract interest rate is revised.

(in thousand Armenian drams)

	2011							
	Less than 1 month	1 to 3 months	3 months to 1 year	1 year to 5 years	More than 5 years	No maturity	Overdue	Total
Assets								
Cash	5,013,113	-	-	-	-	-	-	5,013,113
Placements with banks and financial institutions	140,884,367	91,637,197	-	-	-	-	3,893,700	236,415,264
Financial instruments at fair value through profit or loss	344,720,503	-	-	-	-	-	-	344,720,503
Loans and reverse repurchase agreements	1,890,545	47,354,230	6,048,985	69,099,271	24,852,545	-	-	149,245,576
Available-for-sale assets	-	-	78,299,365	4,662,508	7,503,495	16,459,263	-	106,924,631
Held-to-maturity assets	-	89,011,650	48,358,880	3,235,684	-	-	-	140,606,214
Placements with the IMF	22,001,472	-	-	-	54,487,874	-	-	76,489,346
Property and equipment and intangible assets	-	-	-	-	-	39,009,845	-	39,009,845
Other assets	7,481,713	-	-	-	-	-	-	7,481,713
Total assets	**521,991,713**	**228,003,077**	**132,707,230**	**76,997,463**	**86,843,914**	**55,469,108**	**3,893,700**	**1,105,906,205**
Liabilities								
Notes and coins in circulation	-	-	-	-	-	398,777,362	-	398,777,362
Deposits and accounts of financial and other institutions	269,428,441	-	1,746,015	-	-	-	-	271,174,456
Financial liabilities at fair value through profit or loss	-	148,657	1,622,588	-	-	-	-	1,771,245
Due to the Government of the Republic of Armenia	44,105,548	40,098,805	-	-	-	-	-	84,204,353
Due to the IMF	106,618,215	-	45,125,117	131,045,420	23,672,087	-	-	306,460,839
Other borrowed funds	-	-	202,464	15,719,569	22,924,261	-	-	38,846,294
Debt securities issued	-	-	963,593	-	-	-	-	963,593
Other liabilities	3,409,701	-	-	-	-	-	-	3,409,701
Total liabilities	**423,561,905**	**40,247,462**	**49,659,777**	**146,764,989**	**46,596,348**	**398,777,362**	**-**	**1,105,607,843**
Net position as at 31 December 2011	**98,429,808**	**187,755,615**	**83,047,453**	**(69,767,526)**	**40,247,566**	**(343,308,254)**	**3,893,700**	**298,362**

(in thousand Armenian drams)

	2010						
	Less than 1 month	1 to 3 months	3 months to 1 year	1 year to 5 years	More than 5 years	No maturity	Total
Assets							
Cash	7,552,047	-	-	-	-	-	7,552,047
Placements with banks and financial institutions	119,902,034	32,748,474	5,451,593	-	-	-	158,102,101
Financial instruments at fair value through profit or loss	404,632,917	-	-	-	-	-	404,632,917
Loans and reverse repurchase agreements	6,704,810	3,201,300	2,179,257	56,109,584	2,420,548	-	70,615,499
Available-for-sale assets	-	-	56,636,853	1,533,497	9,597,802	20,938,530	88,706,682
Held-to-maturity assets	-	53,178,981	43,321,077	3,311,379	-	-	99,811,437
Placements with the IMF	12,176,896	-	-	-	51,493,341	-	63,670,237
Property and equipment	-	-	-	-	-	26,895,368	26,895,368
Other assets	4,626,753	-	-	-	-	-	4,626,753
Total assets	**555,595,457**	**89,128,755**	**107,588,780**	**60,954,460**	**63,511,691**	**47,833,898**	**924,613,041**
Liabilities							
Notes and coins in circulation	-	-	-	-	-	348,164,734	348,164,734
Deposits and accounts of financial and other institutions	180,475,805	-	-	-	-	-	180,475,805
Financial instruments at fair value through profit or loss	-	694,841	-	-	-	-	694,841
Due to the Government of the Republic of Armenia	56,421,717	54,112,968	-	-	-	-	110,534,685
Liabilities to IMF	120,364,074	-	8,523,491	147,798,146	1,401,519	-	278,087,230
Other borrowed funds	-	-	153,187	1,512,203	25,934,419	-	27,599,809
Other liabilities	1,499,990	-	-	-	-	-	1,499,990
Total liabilities	**358,761,586**	**54,807,809**	**8,676,678**	**149,310,349**	**27,335,938**	**348,164,734**	**947,057,094**
Net position as at 31 December 2010	**196,833,871**	**34,320,946**	**98,912,102**	**(88,355,889)**	**36,175,753**	**(300,330,836)**	**(22,444,053)**