

Absolut Bank Group
Consolidated Financial Statements

Year ended 31 December 2009

Together with Independent Auditors' Report

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Independent Auditors' Report

To the Shareholders and Board of Directors of Absolut Bank –

We have audited the accompanying consolidated financial statements of Absolut Bank and its subsidiaries (together the "Group"), which comprise the consolidated statement of financial position as at 31 December 2009, and the consolidated income statement, the consolidated statements of comprehensive income and of changes in equity and the consolidated cash flow statement for the year then ended, and a summary of significant accounting policies and other explanatory notes.

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. This responsibility includes: designing, implementing and maintaining internal control relevant to the preparation and fair presentation of consolidated financial statements that are free from material misstatement, whether due to fraud or error; selecting and applying appropriate accounting policies; and making accounting estimates that are reasonable in the circumstances.

Auditors' 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 on 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 financial statements. The procedures selected depend on the auditors' judgment, including the assessment of the risks of material misstatement of the 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 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 financial statements.

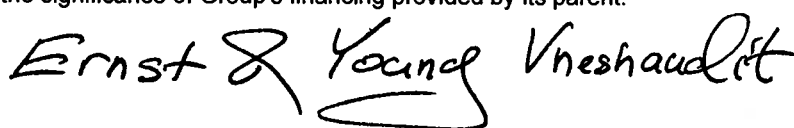
We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the consolidated financial statements present fairly, in all material respects, the financial position of the Group as at 31 December 2009, and its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards.

Emphasis of Matter

Without qualifying our opinion, we draw attention to Notes 1 and 31 to the consolidated financial statements which describe the significance of Group's financing provided by its parent.



1 March 2010

Consolidated statement of financial position**As of 31 December 2009***(Millions of Russian Rubles)*

	<i>Notes</i>	31 December 2009	31 December 2008
Assets			
Cash and cash equivalents	7	10 518	17 859
Mandatory cash balances with the Central Bank of the Russian Federation		638	169
Trading securities		1	141
Due from other banks	8	17 498	8 304
Derivative financial assets	9	73	1 057
Loans to customers	10	90 900	139 002
Investment securities available for sale	11	4 679	137
Property and equipment	12	4 093	4 192
Other assets	13	1 624	1 544
Total assets		130 024	172 405
Liabilities			
Due to other banks	14	55 097	100 716
Derivative financial liabilities	9	170	1 290
Customer accounts	15	47 738	34 153
Debt securities issued	16	6 236	11 119
Subordinated debt	18	6 944	6 744
Other liabilities	17	552	812
Total liabilities		116 737	154 834
Equity			
Share capital	19	2 455	2 455
Share premium	19	13 340	12 683
(Accumulated deficit)/Retained earnings		(2 535)	2 444
Revaluation surplus/(deficit) of investment securities available for sale		27	(11)
Total equity		13 287	17 571
Total equity and liabilities		130 024	172 405

Approved for issue and signed on behalf of the Management Board on 1 March 2010



 Nikolay Sidorov
 Chairman of the Board



 Andrey Larkin
 Chief Financial Officer

The accompanying notes on pages 6 to 55 are an integral part of these consolidated financial statements.

Consolidated income statement**For the year ended 31 December 2009***(Millions of Russian Rubles)*

	Notes	2009	2008
Interest income	21	17 102	16 461
Interest expense	21	(10 101)	(8 247)
Net interest income		7 001	8 214
Allowance for loan impairment	8, 10	(8 058)	(2 580)
Net interest income (loss) after allowance for loan impairment		(1 057)	5 634
Fee and commission income	22	570	581
Fee and commission expense	22	(145)	(147)
Net gains/(losses) from operations with securities	23	132	(655)
Net gains/(losses) from operations with derivatives	24	377	(481)
Net gains from trading in foreign currencies		419	944
Net foreign exchange translation differences		(294)	107
Other income	25	92	96
Non-interest income		1 151	445
Personnel expenses	26	(2 713)	(3 147)
Administrative and other operating expenses	26	(1 941)	(2 192)
Provision for losses on credit related commitments	17, 20	(30)	(89)
Non-interest expense		(4 684)	(5 428)
(Loss)/Profit before income tax expense		(4 590)	651
Income tax expense	27	(389)	(239)
(Loss)/Profit for the year		(4 979)	412

The accompanying notes on pages 6 to 55 are an integral part of these consolidated financial statements.

Consolidated statement of comprehensive income**For the year ended 31 December 2009***(Millions of Russian Rubles)*

	<u>Note</u>	<u>2009</u>	<u>2008</u>
(Loss)/Profit for the year		<u>(4 979)</u>	<u>412</u>
Other comprehensive income			
Unrealised gains/(losses) on investment securities available for sale		47	(14)
Income tax relating to components of other comprehensive income	27	<u>(9)</u>	<u>3</u>
Other comprehensive income for the year, net of tax		<u>38</u>	<u>(11)</u>
Total comprehensive income for the year		<u>(4 941)</u>	<u>401</u>

The accompanying notes on pages 6 to 55 are an integral part of these consolidated financial statements.

Consolidated statement of changes in equity**For the year ended 31 December 2009***(Millions of Russian Rubles)*

	<i>Share capital</i>	<i>Share premium</i>	<i>(Accumulated deficit)/ Retained earnings</i>	<i>Revaluation surplus/ (deficit) of investment securities available for sale</i>	<i>Total shareholders' equity</i>
31 December 2007	1 955	3 394	2 032	–	7 381
Total comprehensive income for the year	–	–	412	(11)	401
Issue of share capital (Note 19)	500	9 289	–	–	9 789
31 December 2008	2 455	12 683	2 444	(11)	17 571
Total comprehensive income for the year	–	–	(4 979)	38	(4 941)
Additional paid in capital (Note 19)	–	657	–	–	657
31 December 2009	2 455	13 340	(2 535)	27	13 287

The accompanying notes on pages 6 to 55 are an integral part of these consolidated financial statements.

Consolidated cash flow statement**For the year ended 31 December 2009***(Millions of Russian Rubles)*

	<i>Notes</i>	2009	2008
Cash flows from operating activities			
Interest received		16 844	16 341
Interest paid		(10 033)	(7 800)
Fees and commissions received		577	573
Fees and commissions paid		(145)	(147)
Income received/(Losses incurred) on operations with securities		131	(99)
Income received/(Losses incurred) on operations with derivatives		241	(367)
Income received from operations in foreign currencies		764	1 918
Other operating income received		92	96
Personnel expenses paid		(2 995)	(2 975)
Other operating expenses paid		(1 418)	(1 938)
Income tax paid		(193)	(705)
Cash flows from operating activities before changes in operating assets and liabilities		3 865	4 897
<i>Net (increase)/decrease in operating assets</i>			
Mandatory cash balances with the Central Bank of the Russian Federation		(469)	1 016
Trading securities		137	(1 470)
Due from other banks		(9 079)	5 766
Loans to customers		40 708	(32 236)
Other assets		(254)	584
<i>Net increase/(decrease) in operating liabilities</i>			
Due to other banks		(45 601)	38 912
Customer accounts		12 593	3 695
Promissory notes issued		1 754	(9 328)
Other liabilities		(32)	18
Net cash from operating activities		3 622	11 854
Cash flows from investing activities			
Purchase of investment securities available for sale		(4 411)	(149)
Purchase of property and equipment		(290)	(755)
Acquisition of software		(148)	(225)
Proceeds from sale of property and equipment		–	1
Net cash used in investing activities		(4 849)	(1 128)
Cash flows from financing activities			
Additional paid in capital		657	–
Redemption of Eurobonds		(6 808)	(2 816)
Contribution received for the additional share issue		–	195
Redemption of Ruble denominated bonds		–	(1 000)
Net cash used in financing activities		(6 151)	(3 621)
Effect of exchange rates changes on cash and cash equivalents		37	329
Net increase/(decrease) in cash and cash equivalents		(7 341)	7 434
Cash and cash equivalents, beginning	7	17 859	10 425
Cash and cash equivalents, ending	7	10 518	17 859

The accompanying notes on pages 6 to 55 are an integral part of these consolidated financial statements.

(Millions of Russian Rubles)

1. Principal activities

The accompanying consolidated financial statements comprise the accounts of Absolut Bank (the "Bank") and its subsidiaries (together the "Group"). The Bank is the parent company in the Group. The Bank was incorporated and is domiciled in the Russian Federation. The Bank is a joint stock company limited by shares and was set up in accordance with Russian regulations.

The Bank's principal business activity is commercial and retail banking operations within the Russian Federation. The Bank is operating under a full banking license issued by the Central Bank of the Russian Federation ("CBRF") since 1993. The Bank participates in the state deposit insurance scheme, which was introduced by the Federal Law #177-FZ "Deposits of individuals insurance in Russian Federation" dated 23 December 2003.

The Bank has 20 (31 December 2008: 20) branches within the Russian Federation.

The Bank's registered address is:

Tsvetnoy boulevard 18, Moscow, 127051, Russian Federation.

As of 31 December, the following shareholders owned equal or more than 5% of the outstanding shares.

Shareholder	2009 %	2008 %
KBC Bank NV	95	95
International Finance Corporation (IFC)	5	5
Total	100	100

KBC Bank NV as a member of KBC Group (hereinafter - "KBC") which owns 95% shares of the Bank.

KBC has developed the strategic plan which was the basis for a restructuring plan as requested by the European Commission. This plan considers subsidiaries in some countries, including Russia, as "non-core", which means that the Bank is subject to divestment. According to the plan the divestment is not planned in the near future. As of 31 December 2009 KBC provided the Bank with the financial support by placing its funds on the Bank's deposit accounts (Refer to Note 14) and providing subordinated loans (Refer to Note 18). The financial support from KBC is critical for continuity of the Bank's operations.

Subsidiaries

The consolidated financial statements include the following major subsidiaries:

2009			
Subsidiary	Ownership, %	Country of operation	Type of operation
LLC "Absolut Leasing"	100	Russian Federation	Finance lease
Absolut Capital Trust Limited	100	Cyprus	Capital borrowings
LLC "Absolut Capital"	100	Russian Federation	Financial services
LLC Leasing company "Absolut"	100	Russian Federation	Finance lease
2008			
Subsidiary	Ownership, %	Country of operation	Type of operation
LLC "Absolut Leasing"	100	Russian Federation	Finance lease
Absolut Capital Trust Limited	100	Cyprus	Capital borrowings
LLC "Absolut Capital"	100	Russian Federation	Financial services
LLC Leasing company "Absolut"	100	Russian Federation	Finance lease

(Millions of Russian Rubles)

1. Principal activities (continued)

Special purpose entities

The Bank consolidates special purpose entities it controls. In assessing and determining if the Bank controls such special purpose entities, judgement is made about the Bank's exposure to the risks, rewards and its ability to make operational decisions.

Included in the consolidated financial statements of the Group as at 31 December 2009 is one SPE (31 December 2008: two) located in Luxemburg and established for the purpose of raising finance in international capital markets (Refer to Note 4).

2. Basis of preparation

General

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

The Group is required to maintain its records and prepare its financial statements for regulatory purposes in Russian Rubles in accordance with Russian accounting and banking legislation and related instructions ("RAL"). These consolidated financial statements are based on the Group's RAL books and records, as adjusted and reclassified in order to comply with IFRS.

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.

These consolidated financial statements are presented in millions of Russian Rubles ("RUB"), unless otherwise indicated.

Inflation accounting

The Russian economy was considered hyperinflationary until 31 December 2002. As such, the Group applied IAS 29 *Financial Reporting in Hyperinflationary Economies*. The effect of applying IAS 29 is that non-monetary items, including components of equity, were restated to the measuring units current at 31 December 2002 by applying the relevant inflation indices to the historical cost, and that these restated values were used as a basis for accounting in subsequent periods.

3. Summary of accounting policies

Changes in accounting policies

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

Improvements to IFRS

In May 2008, the IASB issued amendments to IFRS, which resulted from the IASB's annual improvements project. They comprise amendments that result in accounting changes for presentation, recognition or measurement purposes as well as terminology or editorial amendments related to a variety of individual IFRS standards. Most of the amendments are effective for annual periods beginning on or after 1 January 2009, with earlier application permitted. Amendments included in May 2008 "Improvements to IFRS" did not have any impact on the accounting policies, financial position or performance of the Group.

IAS 1 Presentation of Financial Statements (Revised)

A revised IAS 1 was issued in September 2007, and became effective for annual periods beginning on or after 1 January 2009. This Standard introduces the statement of comprehensive income: it presents all items of recognised income and expense, either in one single statement, or in two linked statements. The revised standard also requires that the income tax effect of each component of comprehensive income be disclosed. In addition, it requires entities to present a comparative statement of financial position as at the beginning of the earliest comparative period when the entity has applied an accounting policy retrospectively, makes a retrospective restatement, or reclassifies items in the financial statements.

The Group has elected to present comprehensive income in two separate statements: income statement and statement of comprehensive income. The Group has not provided a restated comparative set of financial position for the earliest comparative period, as it has not adopted any new accounting policies retrospectively, has not made a retrospective restatement, or retrospectively reclassified items in the consolidated financial statements.

(Millions of Russian Rubles)

3. Summary of accounting policies (continued)

Changes in accounting policies (continued)

IFRS 7 Financial Instruments: Disclosures

The amendments to IFRS 7 were issued in March 2009, to enhance fair value and liquidity disclosures. With respect to fair value, the amendments require disclosure of a three-level fair value hierarchy, by class, for all financial instruments recognised at fair value and specific disclosures related to the transfers between levels in the hierarchy and detailed disclosures related to level 3 of the fair value hierarchy. In addition, the amendments modify the required liquidity disclosures with respect to derivative transactions and assets used for liquidity management.

IFRS 8 Operating Segments

IFRS 8 became effective for annual periods beginning on or after 1 January 2009. This Standard requires disclosure of information about the Group's operating segments and replaces the requirement to determine primary (business) and secondary (geographical) reporting segments of the Group. Adoption of this Standard did not have any impact on the financial position or performance of the Group. The Group determined that the operating segments are the same as the business segments previously identified under *IAS 14 Segment Reporting*.

Subsidiaries

Subsidiaries are those companies and other entities (including special purpose entities) in which the Group, directly or indirectly, has an interest of more than one half of the voting rights or otherwise has power to govern the financial and operating policies so as to obtain benefits.

Intercompany transactions, balances and unrealised gains on transactions between group companies are eliminated; unrealised losses are also eliminated unless the cost cannot be recovered. The Bank and all of its subsidiaries use uniform accounting policies consistent with the Group's policies.

Initial recognition of financial instruments

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

Date of recognition

All purchases and sales of financial assets that require delivery within the time frame established by regulation or market convention ("regular way" purchases and sales) are recorded at settlement date, which is the date that the Group delivers a financial asset. All other purchases and sales are recognised on the settlement date with the change in value between the commitment date and settlement date not recognised for assets carried at cost or amortised cost; recognised in profit or loss for trading securities, derivatives and other financial assets at fair value through profit or loss.

Cash and cash equivalents

Cash and cash equivalents are items which are readily convertible to known amounts of cash and which are subject to an insignificant risk of changes in value. All short-term placements beyond overnight placements are included in due from other banks. Amounts which relate to funds that are of a restricted nature are excluded from cash and cash equivalents. Cash and cash equivalents are carried at amortised cost.

Mandatory cash balances with the Central Bank of the Russian Federation

Mandatory cash balances with the CBRF are carried at amortised cost and represent non-interest bearing mandatory reserve deposits amount of which depends on the level of funds attracted by the credit institution which are not available to finance the Group's day to day operations and hence are not considered as part of cash and cash equivalents.

Trading securities

Trading securities are securities, which are either acquired for generating a profit from short-term fluctuations in price or trader's margin, or are securities included in a portfolio in which a pattern of short-term trading exists. The Group classifies securities into trading securities if it has an intention to sell them within a short period after purchase, i.e. within one to three months. Trading securities are not reclassified out of this category even when the Group's intentions subsequently change, except for rare circumstances (Refer to Note 10).

(Millions of Russian Rubles)

3. Summary of accounting policies (continued)

Trading securities (continued)

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

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 are carried at amortised cost using the effective interest method. Gains and losses are recognised in the consolidated income statement when the loans and receivables are derecognised or impaired, as well as through the amortisation process.

Securities classified as loans and receivables are initially measured at fair value, including transaction costs. They are subsequently measured at amortised cost. The difference between the acquisition cost and the redemption value is recognised as interest and recorded in the consolidated income statement on an accruals basis over the remaining term to maturity. It is recognised in the consolidated income statement, based on the effective rate of interest. Individual impairment losses for securities classified as loans and receivables are recognised – according to the same method as is used for amounts receivable as described below in this note – if there is evidence of impairment at reporting date.

Derivative financial instruments

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 the consolidated income statement.

Available for sale financial assets

Available-for-sale financial 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 financial assets are measured at fair value with gains or losses being recognised as a separate component of equity 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 equity is included in the consolidated income statement. However, interest calculated using the effective interest method is recognised in the consolidated income statement.

Impairment of financial assets

Impairment losses are recognised in profit or loss when incurred as a result of one or more events ("loss events") that occurred after the initial recognition of the financial asset and which have an impact on the amount or timing of the estimated future cash flows of the financial asset or group of financial assets that can be reliably estimated. If the Group determines that no objective evidence exists that impairment was incurred for an individually assessed financial asset, whether significant or not, it includes the asset in a group of financial assets with similar credit risk characteristics and collectively assesses them for impairment. The primary factors that the Group considers whether a financial asset is impaired are its overdue status and realisability of related collateral, if any.

(Millions of Russian Rubles)

3. Summary of accounting policies (continued)

Impairment of financial assets (continued)

The following other principal criteria are also used to determine that there is objective evidence that an impairment loss has occurred:

- ▶ any instalment is overdue and the late payment cannot be attributed to a delay caused by the settlement systems or any other reasonable factors preventing the borrower from effecting a regular payment;
- ▶ the borrower experiences a significant financial difficulty as evidenced by borrower's financial information that the Group obtains (overdue interest/principal payments on loans to other banks, unreasonable loan renegotiation requests on the part of the borrower) ;
- ▶ the borrower considers bankruptcy or a financial reorganisation or the Group has information on existence of the facts which may result in the borrower's bankruptcy (effective court rulings, considerable losses, negative cash inflows, force majeure events);
- ▶ there is an adverse change in the payment status of the borrower as a result of changes in the national or local economic conditions that impact the borrower (changes in effective legislation that may result in shrinking of the borrower's market or increase tax burden, imposition of discriminating measures in respect of the borrower, or regulatory restriction on margin level);
- ▶ the value of collateral significantly decreases as a result of deteriorating market conditions or the borrower has partially/ completely lost the collateral uncovered by insurance or insurance company refuses to pay.

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

Future cash flows in a group of financial assets that are collectively evaluated for impairment are estimated on the basis of the contractual cash flows of the assets and the experience of Management in respect of the extent to which amounts will become overdue as a result of past loss events and the success of recovery of overdue amounts. Past experience is adjusted on the basis of current observable data to reflect the effects of current conditions that did not affect past periods and to remove the effects of past conditions that do not exist currently.

Impairment losses are always recognised through an allowance account to write down the asset's carrying amount to the present value of expected cash flows (which exclude future credit losses that have not been incurred) discounted at the original effective interest rate of the asset. The calculation of the present value of the estimated future cash flows of a collateralised financial asset reflects the cash flows that may result from foreclosure less costs for obtaining and selling the collateral, whether or not foreclosure is probable.

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

Uncollectible assets are written off against the related impairment loss provision in the following cases:

- ▶ after all the necessary procedures to recover the asset have been completed and the amount of the loss has been determined. The procedures include those prescribed by the law, arising out of normal course of business or agreements concluded;
- ▶ the recovery of the indebtedness is not economically feasible due to its insignificance.

Determination of fair value

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

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

(Millions of Russian Rubles)

3. Summary of accounting policies (continued)

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.

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 (Refer to Note 10).

Promissory notes

Promissory notes purchased are included in trading securities, or in due from other banks or in loans and advances to customers, depending on their substance and are recorded, subsequently remeasured and accounted for in accordance with the accounting policies for these categories of assets.

Property and equipment

Property and equipment are stated at cost, restated to the equivalent purchasing power of the Russian Rouble at 31 December 2002 for assets acquired prior to 1 January 2003 less accumulated depreciation and provision for impairment, where required.

Construction in progress is carried at cost less provision for impairment where required. Upon completion, assets are transferred to property and equipment at their carrying amount. Construction in progress is not depreciated until the asset is available for use.

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

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

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

Depreciation on other items of premises and equipment is calculated using the straight-line method to allocate their cost to their residual values over their estimated useful lives as follows:

	<u>% per year</u>
Premises	2-3%
Equipment and vehicles	20%
Leasehold improvements	over the term of the underlying lease

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

(Millions of Russian Rubles)

3. Summary of accounting policies (continued)

Intangible assets

All of the Group's intangible assets have definite useful life and primarily include capitalised computer software. Acquired computer software licenses are capitalised on the basis of the costs incurred to acquire and bring to use the specific software. Development costs that are directly associated with identifiable and unique software controlled by the Group are recorded as intangible assets if the inflow of incremental economic benefits exceeding costs is probable.

Capitalised costs include staff costs of the software development team and cost of services received which are incremental to the software development. All other costs associated with computer software, e.g. its maintenance, are expensed when incurred. Capitalised computer software is amortised on a straight line basis over expected useful lives of 5 years.

Assets classified as held for sale

The Group classifies a non-current asset as held for sale if its carrying amount will be recovered principally through a sale transaction rather than through continuing use. For this to be the case, the non-current asset must be available for immediate sale in its present condition subject only to terms that are usual and customary for sales of such assets and its sale must be highly probable.

The sale qualifies as highly probable if the Bank's management is committed to a plan to sell the non-current asset and an active program to locate a buyer and complete the plan must have been initiated. Further, the non-current asset must have been actively marketed for a sale at price that is reasonable in relation to its current fair value and in addition the sale should be expected to qualify for recognition as a completed sale within one year from the date of classification of the non-current asset as held for sale.

The Group measures an asset classified as held for sale at the lower of its carrying amount and fair value less costs to sell. The Group recognises an impairment loss for any initial or subsequent write-down of the asset (or disposal group) to fair value less costs to sell if events or changes in circumstance indicate that their carrying amount may be impaired.

Due to other banks

Amounts due to other banks are recorded when money or other assets are advanced to the Group by counterparty banks. The non-derivative liability is carried at amortised cost.

Customer accounts

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

Debt securities in issue

Debt securities in issue include promissory notes, loan participation or other notes, and bonds issued by the Group. Debt securities are stated at amortised cost. If the Group purchases its own debt securities in issue, they are removed from the consolidated statement of financial position and the difference between the carrying amount of the liability and the consideration paid is recorded in the consolidated income statement.

Subordinated debt

Subordinated debt ranks behind all other creditors in case of liquidation. Subordinated debt is carried at amortised cost.

Leases

i. Finance - Group as lessor

Where the Group is a lessor in a lease which transfers substantially all the risks and rewards incidental to ownership to the lessee, the assets leased out are presented as a finance lease receivable and carried at the present value of the future lease payments. Finance lease receivables are initially recognised at commencement (when the lease term begins) using a discount rate determined at inception (the earlier of the date of the lease agreement and the date of commitment by the parties to the principal provisions of the lease).

(Millions of Russian Rubles)

3. Summary of accounting policies (continued)

Leases (continued)

The difference between the gross receivable and the present value represents unearned finance income. This income is recognised over the term of the lease using the net investment method (before tax), which reflects a constant periodic rate of return. Incremental costs directly attributable to negotiating and arranging the lease are included in the initial measurement of the finance lease receivable and reduce the amount of income recognised over the lease term. Finance income from leases is recorded within interest income in the consolidated income statement.

Impairment losses are recognised in profit or loss when incurred as a result of one or more events ("loss events") that occurred after the initial recognition of finance lease receivables. The Group uses the same principal criteria to determine that there is objective evidence that an impairment loss has occurred as for loans carried at amortised costs disclosed earlier in this note. Impairment losses are recognised through an allowance account to write down the receivables' net carrying amount to the present value of expected cash flows (which exclude future credit losses that have not been incurred) discounted at the interest rates implicit in the finance leases. The estimated future cash flows reflect the cash flows that may result from obtaining and selling the assets subject to the lease.

ii. Operating - Group as lessee

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

iii. Operating - Group as lessor

The Group presents assets subject to operating leases in the consolidated statement of financial position according to the nature of the asset. Lease income from operating leases is recognised in the consolidated income statement on a straight-line basis over the lease term as other income. The aggregate cost of incentives provided to lessees is recognised as a reduction of rental income over the lease term on a straight-line basis. Initial direct costs incurred specifically to earn revenues from an operating lease are added to the carrying amount of the leased asset.

Derecognition of financial assets and liabilities

Financial assets

The Group derecognises financial assets when (a) the assets are redeemed or the rights to cash flows from the assets otherwise expired or (b) the Group has transferred the rights to the cash flows from the financial assets or entered into a qualifying pass-through arrangement while (i) also transferring substantially all the risks and rewards of ownership of the assets or (ii) neither transferring nor retaining substantially all risks and rewards of ownership but not retaining control. Control is retained if the counterparty does not have the practical ability to sell the asset in its entirety to an unrelated third party without needing to impose additional restrictions on the sale.

Financial liabilities

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 the consolidated income statement.

Credit related commitments

The Group enters into credit related commitments, including letters of credit and financial guarantees. Financial guarantees represent irrevocable assurances to make payments in the event that a customer cannot meet its obligations to third parties and carry the same credit risk as loans. Financial guarantees are initially recognised at their fair value, which is normally evidenced by the amount of fees received. This amount is amortised on a straight line basis over the life of the commitment. At each reporting date, the guarantees are measured at the higher of (i) the unamortised balance of the amount at initial recognition and (ii) the best estimate of expenditure required to settle the commitment at the reporting date. Fees received are amortised to income on a straight line basis over the life of the guarantee. Management uses best estimates of the expenditures required to settle the obligations arising at the reporting date. The estimates of outcome and financial effect are determined based on experience of similar transactions, supplemented by the judgment of Management.

(Millions of Russian Rubles)

3. Summary of accounting policies (continued)

Taxation

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

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

Deferred income tax is provided using the statement of financial position liability method for temporary differences arising between the tax bases of assets and liabilities and their carrying amounts for financial reporting purposes. Deferred tax balances are measured at tax rates enacted or substantively enacted at the reporting date which are expected to apply to the period when the temporary differences will reverse. Deferred tax assets and liabilities are netted only within the individual companies of the Group. Deferred tax assets for deductible temporary differences are recorded only to the extent that it is probable that future taxable profit will be available against which the deductions can be utilised.

Russia also has various operating taxes, that are assessed on the Group's activities. These taxes are included as a component of other operating expenses.

Retirement and other employee benefit obligations

The Group does not have any pension arrangements separate from the State pension system of the Russian Federation, 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 Group has no significant post-retirement benefits.

Share capital and share premium

Ordinary shares are classified as equity. External costs directly attributable to the issue of new shares, other than on a business combination, are shown as a deduction from the proceeds in equity. Any excess of the fair value of consideration received over the par value of shares issued is recognised as share premium in equity. Contributions paid by the shareholders as the additional paid in capital are recognized as share premium in equity.

Fiduciary assets

Assets held by the Group in its own name, but on the account of third parties, are not reported on the consolidated statement of financial position. For the purpose of disclosure fiduciary activities do not encompass safe custody functions. Commissions received from fiduciary activities are shown in fee and commission income.

Segment reporting

The Group's segmental reporting is based on the following operating segments: Retail banking, Corporate banking and Financial markets.

Recognition of income and expenses

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

Fees integral to the effective interest rate include origination fees received or paid by the entity relating to the creation or acquisition of a financial asset or issuance of a financial liability, for example fees for considering loan applications, opening and servicing loan account, valuation and processing transaction documents. The Group does not designate loan commitments as financial liabilities at fair value through profit or loss.

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

(Millions of Russian Rubles)

3. Summary of accounting policies (continued)

Recognition of income and expenses (continued)

All other fees, commissions and other income and expense items are generally recorded on an accrual basis by reference to completion of the specific transaction assessed on the basis of the actual service provided as a proportion of the total services to be provided.

Portfolio and other management advisory and service fees are recognised based on the applicable service contracts, usually on a time-proportion basis. Asset management fees related to investment funds are recorded over the period the service is provided. The same principle is applied for custody services that are continuously provided over an extended period of time.

Foreign currency translation

The functional currency of each of the Group's consolidated entities is the currency of the primary economic environment in which the entity operates. The Bank's and the subsidiaries' functional currency and the Group's presentation currency is the national currency of the Russian Federation, Russian Rubles.

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

As of 31 December 2009 the principal rate of exchange used for translating foreign currency balances was USD 1 = RUB 30.2442 (31 December 2008: USD 1 = RUB 29.3804).

Future changes in accounting policies

Standards and interpretations issued but not yet effective

Amendment to IAS 39 Financial Instruments: recognition and measurement - Eligible Hedged Items

The amendment to IAS 39 was issued in August 2008, and becomes effective for annual periods beginning on or after 1 July 2009. The amendment addresses the designation of a one-sided risk in a hedged item, and designation of inflation as a hedged risk or portion in particular situations. It clarifies that an entity is permitted to designate a portion of the fair value changes or cash flow variability of a financial instrument as hedged item. Management does not expect the amendment to IAS 39 to affect the Group's consolidated financial statements as the Group has not entered into any such hedges.

IFRS 3 Business Combinations (revised in January 2008) and IAS 27 Consolidated and Separate Financial Statements (revised in January 2008)

The revised standards were issued in January 2008 and become effective for financial years beginning on or after 1 July 2009. Revised IFRS 3 introduces a number of changes in the accounting for business combinations that will impact the amount of goodwill recognised, the reported results in the period that an acquisition occurs, and future reported results. Revised IAS 27 requires that a change in the ownership interest of a subsidiary is accounted for as an equity transaction. Therefore, such a change will have no impact on goodwill, nor will it give rise to a gain or loss. Furthermore, the revised standard changes the accounting for losses incurred by the subsidiary as well as the loss of control of a subsidiary. The changes introduced by the revised Standards must be applied prospectively and will affect only future acquisitions and transactions with minority interests.

Improvements to IFRSs

In April 2009 the IASB issued the second 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 2010. There are separate transitional provisions for each standard. Amendments included in April 2009 "Improvements to IFRS" will have no impact on the accounting policies, financial position or performance of the Group, except the following amendments resulting in changes to accounting policies, as described below.

- ▶ IFRS 5 *Non-current Assets Held for Sale and Discontinued Operations*: clarifies that the disclosures required in respect of non-current assets and disposal groups classified as held for sale or discontinued operations are only those set out in IFRS 5. The disclosure requirements of other IFRSs only apply if specifically required for such non-current assets or discontinued operations. The Group expects that this amendment will have no impact on the Group's consolidated financial statements.
- ▶ IFRS 8 *Operating Segment Information*: clarifies that segment assets and liabilities need only be reported when those assets and liabilities are included in measures that are used by the chief operating decision maker. As the Group's chief operating decision maker does review segment assets and liabilities, the Group will continue to disclose this information.

(Millions of Russian Rubles)

3. Summary of accounting policies (continued)

Future changes in accounting policies (continued)

- ▶ IAS 7 *Statement of Cash Flows*: Explicitly states that only expenditure that results in recognising an asset can be classified as a cash flow from investing activities.
- ▶ IAS 36 *Impairment of Assets*: The amendment clarifies that the largest unit permitted for allocating goodwill, acquired in a business combination, is the operating segment as defined in IFRS 8 before aggregation for reporting purposes. The amendment will have no impact on the Group as the annual impairment test is performed before aggregation.

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. Earlier application is permitted. 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 Group expects that this amendment will have no impact on the Group's consolidated financial statements.

IFRS 9 Financial Instruments

In November 2009 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 2013. Entities may adopt the first phase for reporting periods ending on or after 31 December 2009. The first phase of IFRS 9 introduces new requirements on classification and measurement of financial assets. 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. The Group now evaluates the impact of the adoption of new Standard and considers the initial application date.

4. Significant accounting judgements and estimates

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

Impairment losses on loans and advances

The Group regularly reviews its loan portfolios to assess impairment. In determining whether an impairment loss should be recorded in the income statement, the Group makes judgments as to whether there is any observable data indicating that there is a measurable decrease in the estimated future cash flows from a portfolio of loans before the decrease can be identified with an individual loan in that portfolio. This evidence may include observable data indicating that there has been an adverse change in the payment status of borrowers in a group, or national or local economic conditions that correlate with defaults on assets in the group. Management uses estimates based on historical loss experience for assets with credit risk characteristics and objective evidence of impairment similar to those in the portfolio when scheduling its future cash flows. The Group uses its experienced judgment to adjust observable data for a group of loans or receivables to reflect current circumstances.

Finance leases and derecognition of financial assets

Management applies judgement to determine if substantially all the significant risks and rewards of ownership of financial assets and lease assets are transferred to counterparties, in particular which risks and rewards are the most significant and what constitutes substantially all risks and rewards.

Recognition of purchased loans

Management applies judgement to determine if substantially all the significant risks and rewards of ownership have been transferred to the Group under the agreements to acquire mortgage loans concluded with its counterparties, in particular which risks and rewards are the most significant and what constitutes substantially all risks and rewards. As of 31 December 2009 the Group recognised within Loans and advances to customers purchased loans in the amount of RUB 2 549 million (31 December 2008: RUB 2 871 million).

(Millions of Russian Rubles)

4. Significant accounting judgements and estimates (continued)

Consolidation of Special Purpose Entities

Judgement is also required to determine whether the substance of the relationship between the Group and a special purpose entity indicates that the special purpose entity is controlled by the Group. As of 31 December 2009 the Group consolidated one special purpose entities established in Luxembourg for the purpose of raising finance in international capital markets: Absolut Finance S.A. (31 December 2008: Absolut Capital (Luxembourg) S.A. and Absolut Finance S.A.).

Segment reporting

The Group does not allocate its premises, equipment and software balances as well as capital expenditure between the operating segments. The Group provides services for the retail and corporate customers within the same premises and the Group believes that currently there is no reasonable basis for allocation of premises, equipment, software as well as capital expenditure. The Group is in the process of development of a basis of allocation of such items and adjusting its internal management accounting system in order to potentially being able to make such allocations in the future.

5. Changes in presentation

Certain reclassifications have been made to the financial statements as at 31 December 2008 and for the year then ended to conform to the presentation as at 31 December 2009 and for the year then ended as current year presentation provides better view of the financial position of the Group.

Nature of reclassification	Amount	Line as per the previous report	Line as per current report
Consolidated statement of financial position:			
Investment securities available for sale	137	Other assets	Investment securities available for sale
Consolidated income statement:			
Net losses from operations with trading securities	(572)	Net losses from operations with trading securities	Net gains/(losses) from operations with securities
Net losses from earlier redemption of Eurobonds issued	(49)	Administrative and other operating expenses	Net gains/(losses) from operations with securities
Net losses from sale of debt securities classified as loans	(34)	Administrative and other operating expenses	Net gains/(losses) from sale of debt securities classified as loans
Administrative and other operating expenses	(31)	Personnel expenses	Administrative and other operating expenses
Consolidated cash flow statement:			
Investment securities available for sale	(149)	Other assets	Acquisition of investment securities available for sale

6. Segment information

For management purposes, the Group is organised into three operating segments based on products and services as follows:

- ▶ Corporate – comprises corporate lending including sales and repurchase agreements, corporate deposit services and placement of promissory notes among corporate clients, trade finance operations, leasing services, issuing of guarantees, foreign currency exchange transactions and other transactions with corporate customers.
- ▶ Financial markets – comprises securities trading, debt capital markets services (interbank and other borrowings, placement of promissory notes and bonds on money market, raising finance on loro accounts), foreign currency exchange and derivatives transactions on stock exchange and over the counter market.
- ▶ Retail – comprises retail services of opening and maintenance of settlement accounts, raising finance in the forms of promissory notes and retail deposits, debit and credit cards servicing, lending and foreign exchange transactions with individuals, individual entrepreneurs and small and medium size entities.

*(Millions of Russian Rubles)***6. Segment information (continued)**

Management monitors the operating results of its business units separately for the purpose of making decisions about resource allocation and performance assessment. Segment performance, as explained in the table below, is measured differently from profit or loss in the consolidated financial statements.

The Group allocates revenues and expenses between segments depending on the contractual counterparty and type of transaction.

The Group allocates in its internal management accounting system major part of the Group's assets and liabilities as well as income and expenses between the segments. Certain types of assets and liabilities, income and expenses that were not allocated have been presented as "unallocated" in the table below. Currently the Group is in the process of development of the basis of allocation of such items and adjusting its internal management accounting system to make such allocations in the future.

"Interest income from other segments" and "Interest expense relating to transactions with other segments" are defined on the basis of transfer pricing policy. According to the existing transfer pricing system, approved by the Board, funds are transferred between segments at historical market rate. Choice of market rate for each interest asset or liability depends on the currency and contractual maturity of this asset or liability.

Segment results are based on the direct and allocated revenues ("Interest income from other segments") attributable to the assets of the segment as well as on the direct and allocated expenses ("Interest expense relating to transactions with other segments") attributable to the liabilities of the segment.

The Group allocates administrative and other operating expenses between segments using the following principles of allocation: the major part of administrative and other operating expenses represents direct expenses attributable to cost centres which activities correspond to segment activities. The remaining part is allocated between the segments in the same proportion as the direct operating expenses are allocated.

The following table present income and profit and certain asset and liability information regarding the Group's operating segments for the year ended 31 December 2009:

	Retail Banking	Corporate Banking	Financial Markets	Total
Revenues comprise				
External interest income	6 793	9 114	1 195	17 102
Interest income from other segments	2 812	1 224	8 512	12 548
Dealing and other operating income	222	260	691	1 173
Fee and commission income	269	250	51	570
Total revenues	10 096	10 848	10 449	31 393
Expenses comprise				
Interest expense from other segments	(5 048)	(6 321)	(1 179)	(12 548)
External interest expense	(2 682)	(820)	(6 599)	(10 101)
Allowance for loan impairment	(1 256)	(6 824)	22	(8 058)
Personnel expenses	(1 568)	(1 016)	(129)	(2 713)
Administrative and other operating expenses	(1 169)	(480)	(97)	(1 746)
Dealing and other operating loss	–	(38)	(147)	(185)
Fee and commission expense	(42)	(17)	(86)	(145)
Total expenses	(11 765)	(15 516)	(8 215)	(35 496)
Segment results	(1 669)	(4 668)	2 234	(4 103)
Unallocated expenses				(489)
Unallocated revenues				2
Loss before tax				(4 590)
Income tax expense				(389)
Loss for the year				(4 979)
Assets and liabilities				
Segment assets	45 796	45 741	23 408	114 945
Deferred tax asset	–	–	–	–
Unallocated assets				15 079
Total assets				130 024
Segment liabilities	(32 480)	(17 196)	(66 625)	(116 301)
Unallocated liabilities				(436)
Total liabilities				(116 737)
Other segment information				
Depreciation and amortisation	(341)	(162)	(16)	(519)
Other provisions	6	(36)	–	(30)

(Millions of Russian Rubles)

6. Segment information (continued)

	Retail Banking	Corporate Banking	Financial Markets	Total
Dealing and other operating income comprise				
Net gains from operations with derivatives	–	–	524	524
Net gains from trading in foreign currencies	165	156	100	421
Net gains from operations with securities	–	66	66	132
Other income	51	38	1	90
Recovery of provision for losses on credit related commitments	6	–	–	6
Total dealing and other operating income	222	260	691	1 173
Dealing and other operating loss comprise				
Net losses from operations with derivatives	–	–	(147)	(147)
Provision for losses on credit related commitments	–	(36)	–	(36)
Net losses from trading in foreign currencies	–	(2)	–	(2)
Total dealing and other operating loss	–	(38)	(147)	(185)
Unallocated expenses comprise				
Net foreign exchange translation differences				(294)
Administrative and other operating expenses				(195)
Total unallocated expenses				(489)
Unallocated revenues comprise				
Other income				2

The following table present income and profit and certain asset and liability information regarding the Group's operating segments for the year ended 31 December 2008:

	Retail Banking	Corporate Banking	Financial Markets	Total
Revenues comprise				
External interest income	6 055	9 034	1 372	16 461
Interest income from other segments	1 095	1 257	8 373	10 725
Dealing and other operating income	249	305	556	1 110
Fee and commission income	229	328	24	581
Total revenues	7 628	10 924	10 325	28 877
Expenses comprise				
Interest expense from other segments	(4 124)	(5 543)	(1 058)	(10 725)
External interest expense	(917)	(550)	(6 780)	(8 247)
Personnel expenses	(1 969)	(1 006)	(172)	(3 147)
Allowance for loan impairment	(750)	(1 808)	(22)	(2 580)
Administrative and other operating expenses	(1 475)	(446)	(74)	(1 995)
Dealing and other operating loss	(34)	(94)	(1 167)	(1 295)
Fee and commission expense	(42)	(44)	(61)	(147)
Total expenses	(9 311)	(9 491)	(9 334)	(28 136)
Segment results	(1 683)	1 433	991	741
Unallocated expenses				(197)
Unallocated revenues				107
Profit before tax				651
Income tax expense				(239)
Profit for the year				412
Assets and liabilities				
Segment assets	59 876	82 077	11 079	153 032
Deferred tax asset				330
Unallocated assets				19 043
Total assets				172 405
Segment liabilities	(16 038)	(16 803)	(121 509)	(154 350)
Unallocated liabilities				(484)
Total liabilities				(154 834)
Other segment information				
Depreciation and amortisation	(217)	(91)	(8)	(316)
Other provisions	(34)	(55)	–	(89)

(Millions of Russian Rubles)

6. Segment information (continued)

	Retail Banking	Corporate Banking	Financial Markets	Total
Dealing and other operating income comprise				
Net gains from trading in foreign currencies	216	253	480	949
Other income	33	52	11	96
Net gains from operations with derivatives	–	–	65	65
Total dealing and other operating income	249	305	556	1 110
Dealing and other operating loss comprise				
Net losses from operations with securities	–	(34)	(621)	(655)
Net losses from operations with derivatives	–	–	(546)	(546)
Provision for losses on credit related commitments	(34)	(55)	–	(89)
Net losses from trading in foreign currencies	–	(5)	–	(5)
Total dealing and other operating loss	(34)	(94)	(1 167)	(1 295)
Unallocated expenses comprise				
Administrative and other operating expenses				(197)
Unallocated revenues comprise				
Net foreign exchange translation differences				107

Geographical information

The Group operates only in the Russian Federation. Balances with Russian counterparties actually outstanding from off-shore companies of the counterparties are allocated to the Russian Federation segment. The capital expenditure of the Group relates to the operations of the Group in the Russian Federation.

The Russian Federation segment has certain balances with counterparties in other countries. A breakdown of assets and liabilities of the Group with non-Russian counterparties is presented in Note 28.

7. Cash and cash equivalents

	31 December 2009	31 December 2008
Current accounts with the CBRF	5 886	9 740
Cash on hand	2 591	3 326
Settlement accounts with trading systems	1 399	1 676
Current accounts with other banks	469	1 444
Overnight placements with other banks	173	1 673
Cash and cash equivalents	10 518	17 859

8. Due from other banks

	31 December 2009	31 December 2008
Time deposits with other banks	17 498	7 439
Bonds of other banks	–	887
	17 498	8 326
Less – Allowance for impairment	–	(22)
Due from other banks	17 498	8 304

As of 31 December 2009 time deposits with other banks included balances with the Parent with the total aggregate amount of RUB 16 168 million or 92% of the total amount due from other banks. These loans mature from January till March 2010 and have effective interest rates from 0.2% till 6.79% per annum.

(Millions of Russian Rubles)

8. Due from other banks (continued)

As of 31 December 2008 time deposits with other banks included balances with the CBRF with the total aggregate amount of RUB 6 502 million or 78% of the total amount due from other banks. These loans matured in January 2009 and had effective interest rates of 7.5% per annum.

As of 31 December 2008 due from other banks included Ruble denominated bonds of Russian banks in the amount of RUB 887 million which were reclassified out of the trading securities portfolio during 2008. Refer to Note 10.

The movements in allowance for impairment of due from other banks were as follows:

	<u>2009</u>	<u>2008</u>
1 January	22	–
(Reversal)/Charge	(22)	22
31 December	<u>–</u>	<u>22</u>

The geographical concentration, analysis by credit quality, currency and interest rate risks analysis are disclosed in Note 28. Information about fair value of due from other banks is disclosed in Note 29. Maturity analysis of due from other banks is disclosed in Note 30. The information on related party balances is disclosed in Note 31.

9. Derivative financial instruments

The table below shows the fair values of derivative financial instruments, recorded as assets or liabilities, together with their notional amounts. The notional amount, recorded gross, is the amount of a derivative's underlying asset, reference rate or index and is the basis upon which changes in the value of derivatives are measured. The notional amounts indicate the volume of transactions outstanding at the year end and are not indicative of the credit risk.

	<u>31 December 2009</u>			<u>31 December 2008</u>		
	<u>Notional principal</u>	<u>Fair values</u>		<u>Notional principal</u>	<u>Fair value</u>	
		<u>Asset</u>	<u>Liability</u>		<u>Asset</u>	<u>Liability</u>
Interest rate contracts						
Swaps – foreign counterparty	907	–	(78)	1 028	–	(99)
Options – foreign counterparty	–	–	–	1 175	–	(32)
Foreign exchange contracts						
Swaps – foreign counterparty	4 092	16	(16)	1 733	19	(70)
Swaps – domestic counterparty	1 812	1	(45)	3 173	477	(176)
Forwards – foreign counterparty	111	1	–	2 556	32	(39)
Forwards – domestic counterparty	299	55	(31)	7 619	529	(874)
Total derivative assets/liabilities		<u>73</u>	<u>(170)</u>		<u>1 057</u>	<u>(1 290)</u>

Foreign and domestic counterparty in the table above stand for counterparties where foreign means non-Russian entities and domestic means Russian entities.

As of 31 December 2009 and 2008, the Group has positions in the following types of derivatives:

Forwards

Forwards contracts are contractual agreements to buy or sell a specified financial instrument at a specific price and date in the future. Forwards are customised contracts transacted in the over-the-counter market.

Swaps

Swaps are contractual agreements between two parties to exchange movements in interest and foreign currency rates and equity indices, and (in the case of credit default swaps) to make payments with respect to defined credit events based on specified notional amounts.

During 2007 in order to hedge interest rate gap between fixed interest rate loans and advances to customers and floating interest rate interbank liabilities the Group entered into several interest rate swaps with a foreign bank. The derivatives mature from 2011 to 2014.

(Millions of Russian Rubles)

9. Derivative financial instruments (continued)

Options

Options are contractual agreements that convey the right, but not the obligation, for the purchaser either to buy or sell a specific amount of a financial instrument at a fixed price, either at a fixed future date or at any time within a specified period.

During 2007 in order to hedge interest rate gap between fixed interest rate loans and advances to customers and floating interest rate interbank liabilities the Group entered into a collar transaction with a foreign bank. The derivative matured in 2009.

10. Loans to customers

Loans to customers by class comprise:

	31 December 2009	31 December 2008
Loans to legal entities		
Corporate loans	50 324	73 669
Trade finance	2 411	3 243
SME loans	2 376	3 996
Finance lease receivables	1 728	1 568
Corporate bonds	1 329	5 777
Loans to local authorities		
Municipal bonds	128	830
Loans to individuals		
Mortgage loans	32 907	36 719
Car loans	9 383	13 469
SME loans	1 570	2 545
Credit cards	1 107	1 362
Consumer loans	–	89
Reverse sale and repurchase agreements	–	20
Gross loans to customers	103 263	143 287
Less – Allowance for impairment	(12 363)	(4 285)
Loans to customers	90 900	139 002

As of 31 December 2009 corporate and municipal bonds in the amount RUB 1 329 million and RUB 128 million respectively represent debt securities reclassified out from trading securities portfolio (31 December 2008: RUB 5 777 million and RUB 830 million respectively).

(Millions of Russian Rubles)

10. Loans to customers (continued)

Following the amendments to IAS 39 and IFRS 7, "Reclassification of Financial Assets", the Group reclassified certain financial assets out of held for trading category as they were no longer held for the purpose of selling or repurchasing them in the near term. The reclassification was made with effect from 30 September 2008 at fair value at that date. The impact of reclassification is as follows:

	<i>Held for trading financial assets were reclassified to</i>	
	<i>Loans and receivables</i>	<i>Available for sale financial assets</i>
Carrying amount as at 31 December 2009	1 071	153
Fair value as at 31 December 2009	1 086	153
Fair value gain that would have been recognized on the reclassified assets for the year ended 31 December 2009 if the reclassification had not been made	1	16
Gain/(loss), income/(expense) recognized after reclassification in profit or loss for the year ended 31 December 2009:		
- Interest income	488	10
- Allowance for loan impairment	(56)	-
- Net gains from operations with debt securities classified as loans	67	-
Carrying amount as at 31 December 2008	7 164	137
Fair value as at 31 December 2008	6 694	137
Fair value loss that would have been recognized on the reclassified assets for the year ended 31 December 2008 if the reclassification had not been made	(858)	(18)
Gain/(loss), income/(expense) recognized after reclassification in profit or loss for the year ended 31 December 2008:		
- Interest income	246	2
- Allowance for loan impairment	(330)	-
- Net losses from operations with debt securities classified as loans	(34)	-

Financial assets were reclassified from financial assets held for trading to loans and receivables and available for sale financial assets due to the deterioration of Russian and international markets that has occurred during the third quarter of 2008 (Refer also to Note 11).

Allowance for impairment of loans to customers

A reconciliation of the allowance for impairment of loans to customers by class is as follows:

	<i>At 1 January 2009</i>	<i>Charge for the year/(recovery)</i>	<i>Amounts written off</i>	<i>At 31 December 2009</i>
Loans to legal entities				
Corporate loans	2 674	6 183	-	8 857
Trade finance	172	476	-	648
SME loans	264	251	-	515
Corporate bonds	288	88	-	376
Finance lease receivables	78	87	-	165
Loans to local authorities				
Municipal bonds	20	(10)	-	10
Loans to individuals				
Mortgage loans	353	418	-	771
Car loans	272	264	-	536
Credit cards	55	224	(1)	278
SME loans	109	99	(1)	207
Total	4 285	8 080	(2)	12 363

(Millions of Russian Rubles)

10. Loans to customers (continued)**Allowance for impairment of loans to customers (continued)**

	<i>At 1 January 2008</i>	<i>Charge for the year/(recovery)</i>	<i>Amounts written off</i>	<i>At 31 December 2008</i>
Loans to legal entities				
Corporate loans	1 306	1 368	–	2 674
Corporate bonds	–	288	–	288
SME loans	35	229	–	264
Trade finance	91	81	–	172
Finance lease receivables	24	54	–	78
Loans to local authorities				
Municipal bonds	–	20	–	20
Loans to individuals				
Mortgage loans	114	239	–	353
Car loans	120	152	–	272
SME loans	9	100	–	109
Credit cards	19	36	–	55
Consumer loans	10	(9)	(1)	–
Total	1 728	2 558	(1)	4 285

The table below distinguishes between loans and advances to customers assessed for impairment individually and on portfolio basis:

	<i>31 December 2009</i>	<i>31 December 2008</i>
Loans assessed for impairment on portfolio basis	74 413	134 886
Individually determined to be impaired	22 797	5 945
Past due but not impaired	6 053	2 456
Gross loans to customers	103 263	143 287
Less – Allowance for impairment of loans assessed for impairment on portfolio basis (including past due but not impaired)	(2 661)	(2 353)
Less – Allowance for impairment of loans individually determined to be impaired	(9 702)	(1 932)
Loans to customers	90 900	139 002

Concentration of loans to customers

As of 31 December 2009 the Group had a concentration of loans represented by RUB 14 391 million due from the ten largest third party borrowers (14% of gross loan portfolio) (2008 - RUB 13 027 million or 9%). An allowance of RUB 1 845 million (2008 - RUB 319 million) was recognised against these loans.

Loans are made principally within Russia in the following industry sectors:

	<i>31 December 2009</i>	<i>31 December 2008</i>
Individuals	44 967	54 204
Trade	19 351	34 038
Real estate	17 798	17 625
Manufacturing	10 814	14 775
Services	3 695	6 328
Construction	2 939	7 346
Finance	1 808	2 850
Agriculture	141	265
Municipals	128	830
Other	1 622	5 026
Gross loans to customers	103 263	143 287

*(Millions of Russian Rubles)***10. Loans to customers (continued)*****Finance lease receivables***

Included in corporate lending portfolio are finance lease receivables. The analysis of finance lease receivables at 31 December 2009 is as follows:

	<i>Not later than 1 year</i>	<i>Later than 1 year and not later than 5 years</i>	<i>Total</i>
Gross investments in finance lease	1 020	1 336	2 356
Unearned future finance income on finance lease	(272)	(356)	(628)
	748	980	1 728
Less – Allowance for impairment	(99)	(66)	(165)
Net investments in finance lease	649	914	1 563

The analysis of finance lease receivables at 31 December 2008 is as follows:

	<i>Not later than 1 year</i>	<i>Later than 1 year and not later than 5 years</i>	<i>Total</i>
Gross investments in finance lease	1 175	792	1 967
Unearned future finance income on finance lease	(198)	(201)	(399)
	977	591	1 568
Less – Allowance for impairment	(42)	(36)	(78)
Net investments in finance lease	935	555	1 490

Net investments in finance lease generally comprise lease contracts on various types of equipment and vehicles.

The geographical concentration, analysis by credit quality, currency and interest rate risks analysis are disclosed in Note 28. Information about fair value of loans to customers is disclosed in Note 29. Maturity analysis of loans to customers is disclosed in Note 30. The information on related party balances is disclosed in Note 31.

11. Investment securities available for sale

	<i>31 December 2009</i>	<i>31 December 2008</i>
Federal loan bonds (OFZ)	2 380	137
Corporate bonds	2 043	–
Municipal bonds	253	–
Bonds of the CBRF	3	–
Investment securities available for sale	4 679	137

As of 31 December 2009 federal loan bonds (OFZ) in the amount RUB 153 million (2008 – RUB 137 million) represent securities reclassified out from trading securities portfolio in 2008 (Refer to Note 10).

(Millions of Russian Rubles)

12. Property and equipment

The movements in property and equipment for the year ended 31 December 2009 were as follows:

	<i>Premises</i>	<i>Leasehold improvement</i>	<i>Computers and office equipment</i>	<i>Assets under construction</i>	<i>Total</i>
Cost					
31 December 2008	3 378	111	982	164	4 635
Additions	–	–	3	287	290
Transfers	18	10	233	(261)	–
Disposals	–	(26)	(11)	–	(37)
31 December 2009	3 396	95	1 207	190	4 888
Accumulated depreciation					
31 December 2008	126	45	272	–	443
Depreciation charge	88	24	261	–	373
Disposals	–	(12)	(9)	–	(21)
31 December 2009	214	57	524	–	795
Net book value:					
31 December 2008	3 252	66	710	164	4 192
31 December 2009	3 182	38	683	190	4 093

The movements in property and equipment for the year ended 31 December 2008 were as follows:

	<i>Premises</i>	<i>Leasehold improvement</i>	<i>Computers and office equipment</i>	<i>Assets under construction</i>	<i>Total</i>
Cost					
31 December 2007	2 232	38	428	1 202	3 900
Additions	–	6	3	746	755
Transfers	1 161	68	555	(1 784)	–
Disposals	(15)	(1)	(4)	–	(20)
31 December 2008	3 378	111	982	164	4 635
Accumulated depreciation					
31 December 2007	51	9	140	–	200
Depreciation charge	75	36	135	–	246
Disposals	–	–	(3)	–	(3)
31 December 2008	126	45	272	–	443
Net book value:					
31 December 2007	2 181	29	288	1 202	3 700
31 December 2008	3 252	66	710	164	4 192

Assets under construction consist of investments in acquisition of premises, construction works, leasehold improvements and refurbishment of premises in Moscow and regions of the Russian Federation, where the branch network is being developed. Upon completion, assets are transferred to premises and equipment.

As at 31 December 2009 premises and equipment contain fully depreciated assets in the amount of RUB 23 million (31 December 2008: 26 million).

*(Millions of Russian Rubles)***13. Other assets**

	31 December 2009	31 December 2008
Non-current assets held for sale	379	–
Software	316	317
Current income tax asset	275	118
Prepayments	185	259
Foreclosed assets	110	–
VAT on leasing operations	92	161
Precious coins	83	1
Property to transfer to leasing	61	134
Settlements	22	46
Restricted cash	12	12
Prepayments to suppliers for equipment to be leased	6	89
Accrued income	2	2
Due from employees	2	2
Deferred income tax asset	–	330
Other	79	73
Other assets	1 624	1 544

The movements in software for the year ended 31 December 2009 were as follows:

	Software
Cost	
31 December 2008	397
Additions	148
Disposals	(109)
31 December 2009	436
Accumulated depreciation	
31 December 2008	80
Depreciation charge	146
Disposals	(106)
31 December 2009	120
Net book value:	
31 December 2008	317
31 December 2009	316

The movements in software for the year ended 31 December 2008 were as follows:

	Software
Cost	
31 December 2007	177
Additions	225
Disposals	(5)
31 December 2008	397
Accumulated depreciation	
31 December 2007	15
Depreciation charge	70
Disposals	(5)
31 December 2008	80
Net book value:	
31 December 2007	162
31 December 2008	317

*(Millions of Russian Rubles)***14. Due to other banks**

	31 December 2009	31 December 2008
Time deposits and loans	52 669	95 144
Trade finance	1 500	3 297
Special purpose finance	831	1 038
Correspondent accounts and overnight placements of other banks	74	46
Brokerage accounts	23	16
Syndicated loans	–	1 175
Due to other banks	55 097	100 716

As of 31 December 2009 and 2008 due to banks were to a considerable extent (93% and 86% respectively) funded by parent resources (Refer to Note 31).

As of 31 December 2008 time deposits and loans included deposits from CBRF in the amount of RUB 7 065 million. Deposits mature within seven months after reporting date and have effective interest rates from 13.39% to 14.71% per annum.

Trade finance represents funds received from foreign financial institutions either directly by the Group or by the beneficiaries under documentary operations if there is a lending arrangement between the Group and the financing bank, under which the Group is liable for the funds' repayment. Funds mature from 2010 to 2015 and have effective interest rates from 2.50% to 12.12% per annum (31 December 2008: from 3.01% to 17.33% per annum).

As of 31 December 2009 and 2008 special purpose finance represents loans from 3 foreign banks, granted to the Group under credit line facility agreement for the special purposes, such as expansion of the consumer financing portfolio, mortgage lending programs and programs of development of small business in the private sector in the Russian Federation. Loans mature from 2010 to 2014 and have effective interest rates from 3.64% to 9.98% per annum (31 December 2008: from 6.27% to 10.00% per annum).

The Group is obligated to comply with financial covenants in relation to special purpose finance disclosed above. These covenants include capital adequacy ratios and various other financial performance ratios.

The geographical concentration, currency and interest rate risks analysis are disclosed in Note 28. Information about fair value of due to other banks is disclosed in Note 29. Maturity analysis of due to other banks is disclosed in Note 30. The information on related party balances is disclosed in Note 31.

15. Customer accounts

	31 December 2009	31 December 2008
State and public organisations		
Current accounts	79	242
Term deposits	70	–
Legal entities		
Current accounts	8 540	7 446
Term deposits	6 806	10 736
Individuals		
Term deposits	29 521	13 419
Current accounts	2 722	2 310
Customer accounts	47 738	34 153

As of 31 December 2009 customer accounts in the amount of RUB 213 million (31 December 2008: RUB 213 million) represent the balances on brokerage accounts of legal entities and individuals.

As of 31 December 2009 customer accounts of RUB 7 795 million or 16 % (of total customer accounts) were due to the ten largest third party customers (31 December 2008: RUB 7 223 million or 21%).

(Millions of Russian Rubles)

15. Customer accounts (continued)

An analysis of customer accounts by economic sector follows:

	31 December 2009	31 December 2008
Individuals	32 243	15 729
Insurance	5 012	2 468
Trade	4 395	6 235
Construction / real estate	1 644	1 645
Manufacturing	634	799
Transport	562	1 302
Financial services	514	3 761
Agriculture	135	29
Services	128	440
Oil and gas	108	43
Telecom	46	31
Other	2 317	1 671
Customer accounts	47 738	34 153

The geographical concentration, currency and interest rate risks analysis are disclosed in Note 28. Information about fair value of customer accounts is disclosed in Note 29. Maturity analysis of customer accounts is disclosed in Note 30. The information on related party balances is disclosed in Note 31.

16. Debt securities issued

	31 December 2009	31 December 2008
Promissory notes	3 220	1 336
Eurobonds (Loan participation notes)	3 016	9 783
Debt securities issued	6 236	11 119

In March 2007 the Group placed 9.13% loan participation notes due in March 2010 for a total nominal amount of USD 175 million. As of 31 December 2009 the carrying value of these notes was RUB 3 016 million (31 December 2008: RUB 4 231 million). The effective interest rate was 9.9% per annum.

In April 2006 the Group placed 8.75% loan participation notes due in April 2009 for a total nominal amount of USD 150 million at 0.648% discount to the nominal value. In May 2006 the Group issued additional tranche of 8.75% loan participation notes due in April 2009 with a total nominal amount of USD 50 million, which were placed at 1% discount to the nominal value. As of 31 December 2008 the carrying value of these notes was RUB 5 552 million. The effective interest rate was 9.8% per annum. In January 2009 the Group redeemed prior to maturity USD 23 million 8.75% loan participation notes due in April 2009. These notes were bought back by the Group during 2008 and January 2009. In April 2009 the Group fully redeemed the remaining part of these two tranches at par – USD 177 million.

Promissory notes are represented by debt securities issued by the Group with a discount to face value in Russian Rubles and foreign currencies.

The geographical concentration, currency and interest rate risks analysis are disclosed in note 28. Information about fair value of debt securities issued is disclosed in note 29. Maturity analysis of debt securities issued is disclosed in note 30. The information on related party balances is disclosed in Note 31.

*(Millions of Russian Rubles)***17. Other liabilities**

	31 December 2009	31 December 2008
Accrued bonuses and unused vacations including social security	186	468
Provisions for guarantees and commitments	119	89
Finance lease payments received in advance	97	117
Taxes payable other than income	57	41
Other accrued expenses	41	26
Accounts payable	29	31
Deferred income	21	14
Provision for legal claims	2	–
Other	–	26
Other liabilities	552	812

The movements in provisions were as follows:

	Legal claims	Guarantees and commitments
31 December 2007	–	–
Charge (reversal)	–	89
31 December 2008	–	89
Charge (reversal)	2	30
31 December 2009	2	119

18. Subordinated debt

In August 2006 the Group entered into a subordinated loan agreement with a foreign financial institution for the amount of USD 20 million. The loan is repayable in 6 semi-annual instalments starting from 15 February 2012 and has a floating interest rate of six-months LIBOR + 3.95% per annum (31 December 2008: LIBOR + 2.95%). The effective interest rate at 31 December 2009 was 5.19% per annum (31 December 2008: 6.33% per annum). As of 31 December 2009 the carrying value of this loan was RUB 611 million (31 December 2008: RUB 595 million).

In June, September and November 2007 the Group attracted three subordinated loans in the amount of USD 100 million, USD 55 million, USD 50 million for the period of 10 years from the Group's Parent. For the first five years the rates are fixed at 8.03, 6.34 and 5.81% per annum respectively, subsequently floating interest rate of six-month LIBOR + 3.75%, six-month LIBOR + 2.75%, six-month LIBOR + 2.75% per annum respectively are set. The effective interest rates at 31 December 2009 were 8.34, 6.49 and 5.97% per annum respectively (31 December 2008: 8.37, 6.49 and 5.97% per annum respectively). As of 31 December 2009 the carrying value of these loans were RUB 3 140 million, RUB 1 683 million and RUB 1 510 million respectively (31 December 2008: RUB 3 049 million, RUB 1 634 million and RUB 1 466 million respectively).

Interest rate analysis of subordinated debt is disclosed in Note 28. Information about fair value of subordinated debt is disclosed in Note 29. The information on related party balances is disclosed in Note 31.

(Millions of Russian Rubles)

19. Equity

Movements in shares outstanding, issued and fully paid were as follows:

	Number of shares (in millions)	Ordinary shares (inflation adjusted amount)	Share premium	Total
31 December 2007	134	1 955	3 394	5 349
New shares issued	50	500	9 289	9 789
31 December 2008	184	2 455	12 683	15 138
Additional paid in capital	–	–	657	657
31 December 2009	184	2 455	13 340	15 795

All ordinary shares have a nominal value of RUB 10 per share and rank equally. Each share carries one vote. All shares have been fully paid in.

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

On 3 October 2007 shareholders took a decision to increase the share capital at the extraordinary general shareholders meeting. 50 million ordinary shares were placed at 5.34 EUR per share among the existing shareholders so that ownership structure remains the same. IFC and KBC Bank N.V., Belgium contributed the amounts due for the share issue in December 2007. On 21 March 2008 the CBRF registered the share issue and receipts were converted into the share capital and share premium. As a result, the share capital of the Bank has increased by RUB 500 million and amounted to RUB 2 455 million. The share premium increased by RUB 9 289 million and amounted to RUB 12 683 million.

On 30 June 2009 KBC Bank N.V. granted EUR 15 million to the Group as additional paid in capital without issue of new shares.

20. Commitments and contingencies

Operating environment

Russia continues economic reforms and development of its legal, tax and regulatory frameworks as required by a market economy. The future stability of the Russian economy is largely dependent upon these reforms and developments and the effectiveness of economic, financial and monetary measures undertaken by the government.

The Russian economy is vulnerable to market downturns and economic slowdowns elsewhere in the world. The global financial crisis has resulted in a decline in the gross domestic product, capital markets instability, significant deterioration of liquidity in the banking sector, and tighter credit conditions within Russia. While the Russian Government has introduced a range of stabilization measures aimed at providing liquidity to Russian banks and companies, there continues to be uncertainty regarding the access to capital and cost of capital for the Group and its counterparties, which could affect the Group's financial position, results of operations and business prospects.

Also, factors including increased unemployment in Russia, reduced corporate liquidity and profitability, and increased corporate and personal insolvencies, have affected the Group's borrowers' ability to repay the amounts due to the Group. In addition, changes in economic conditions have resulted in deterioration in the value of collateral held against loans and other obligations. To the extent that information is available, the Group has reflected revised estimates of expected future cash flows in its impairment assessment.

While management believes it is taking appropriate measures to support the sustainability of the Group's business in the current circumstances, unexpected further deterioration in the areas described above could negatively affect the Group's results and financial position in a manner not currently determinable.

Legal

In the ordinary course of business, the Group is subject to legal actions and complaints. Management believes that the ultimate liability, if any, arising from such actions or complaints will not have a material adverse effect on the financial condition or the results of future operations of the Group.

As of 31 December 2009, the Group was engaged in number of litigation proceedings. Provision of RUB 2 million has been made as it is likely that such an amount of loss will occur (Refer to Note 17).

(Millions of Russian Rubles)

20. Commitments and contingencies (continued)

Taxation

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

In accordance with tax legislation input VAT on leasing operations is subject to recovery either through offset against output VAT or cash refund (Refer to Note 13). The excess input VAT is to be offset automatically against output VAT within three months from the end of the tax period when the excess input VAT was declared, i.e. when the respective VAT declaration was submitted. Upon the expiration of the three month period the remainder of input VAT which was not offset by the tax authorities is to be refunded to the taxpayer in cash upon its written claim or the taxpayer is eligible to apply the alternative method of VAT recovery (offset against other taxes).

As at 31 December 2009 management believes that its interpretation of the relevant legislation is appropriate and that the Group's tax, currency and customs positions will be sustained.

Capital expenditure commitments

As of 31 December 2009 the Group had contractual capital expenditure commitments in respect of premises and equipment totaling RUB 6 million (31 December 2008: RUB 12 million). The Group has already allocated the necessary resources in respect of these commitments. The Group believes that future net income and funding will be sufficient to cover this and any similar such commitments.

Operating lease commitments

Where the Group is the lessee, the future minimum lease payments under non-cancellable operating leases are as follows:

	31 December 2009	31 December 2008
Not later than 1 year	103	221
Later than 1 year and not later than 5 years	242	357
Later than 5 years	95	109
Total operating lease commitments	440	687

Credit related commitments

The primary purpose of these instruments is to ensure that funds are available to a customer as required. Guarantees and standby letters of credit, which represent irrevocable assurances that the Group will make payments in the event that a customer cannot meet its obligations to third parties, carry the same credit risk as loans. Documentary and commercial letters of credit, which are written undertakings by the Group on behalf of a customer authorising a third party to draw drafts on the Group up to a stipulated amount under specific terms and conditions, are collateralised by the underlying shipments of goods to which they relate or cash deposits and therefore carry less risk than a direct borrowing.

Commitments to extend credit represent unused portions of authorisations in the form of loans, guarantees or letters of credit. With respect to credit risk on commitments to extend credit, the Group is potentially exposed to loss in an amount equal to the total unused commitments. However, the likely amount of loss is less than the total unused commitments since most commitments to extend credit are contingent upon customers maintaining specific credit standards. The Group monitors the term to maturity of credit related commitments because longer-term commitments generally have a greater degree of credit risk than shorter-term commitments.

*(Millions of Russian Rubles)***20. Commitments and contingencies (continued)*****Credit related commitments***

Outstanding credit related commitments are as follows:

	31 December 2009	31 December 2008
Undrawn credit lines	9 904	17 007
Guarantees issued	2 046	1 558
Import letters of credit	615	923
	12 565	19 488
Less – Provisions	(119)	(89)
Total credit related commitments	12 446	19 399

Fiduciary assets

The Group provides depositary services to its customers. These assets are not included in the Group's consolidated statement of financial position as they are not assets of the Group.

Trust activities of the Group

The assets under management are not reported on the Group's consolidated statement of financial position as they are not assets of the Group. They represent assets transferred to the Group for the management under individual asset management agreements or under collective investment programmes. The assets managed by the Group are disclosed at their fair value and fall into the following categories:

	31 December 2009	31 December 2008
Corporate shares	18	15
Corporate bonds	8	15
Cash at brokers	3	20
Futures, long position	–	7
Total assets under management	29	57

21. Interest income and expense

	2009	2008
Interest income		
Loans to customers	15 911	15 236
Due from other banks	994	506
Investment securities available for sale	187	2
Correspondent accounts	2	8
	17 094	15 752
Debt trading securities	8	709
Interest income	17 102	16 461
Interest expense		
Term placements of other banks	5 516	5 242
Term deposits of individuals	2 677	916
Debt securities issued	720	1 264
Term deposits of legal entities	700	417
Subordinated debt	487	400
Correspondent accounts of other banks	1	5
Other	–	3
Interest expense	10 101	8 247

Interest income accrued on loans, for which individual impairment allowances have been recognized, for the year ended 31 December 2009, comprised RUB 871 million (2008 – RUB 171 million).

*(Millions of Russian Rubles)***22. Fee and commission income and expense**

	<u>2009</u>	<u>2008</u>
Commission on plastic cards settlements	137	136
Other settlement transactions	103	111
Cash transactions	97	94
Guarantees issued	66	46
Letters of credit	51	98
Acting as currency control agent	45	54
Commission on cash collection	15	17
Brokerage	14	19
Transactions with securities	14	1
Asset management	1	1
Other	27	4
Fee and commission income	<u>570</u>	<u>581</u>
Plastic card	44	43
Cash transaction	29	33
Settlement transactions	24	22
Transactions with securities	17	–
Letters of credit	14	30
Guarantees	4	5
Currency conversion operations	3	5
Other	10	9
Fee and commission expense	<u>145</u>	<u>147</u>

23. Net gains/(losses) from operations with securities

	<u>2009</u>	<u>2008</u>
Net gains/(losses) from sale of debt securities classified as loans	67	(34)
Net gains/(losses) from operations with Eurobonds issued	38	(49)
Investment securities available for sale:		
- Government bonds	19	–
- Corporate bonds	6	–
- State and municipal bonds	1	–
Trading securities:		
- Promissory notes	1	(2)
- State and municipal bonds	–	(33)
- Government bonds	–	(45)
- Corporate shares	–	(117)
- Corporate bonds	–	(369)
Other	–	(6)
Net gains/(losses) from operations with securities	<u>132</u>	<u>(655)</u>

24. Net gains/(losses) from operations with derivatives

	<u>2009</u>	<u>2008</u>
Net gains/(losses) from operations with swaps and forwards on foreign currency	388	(412)
Net losses from operations with interest rate swaps	(5)	(82)
Net losses from operations with interest rate options	(6)	(31)
Net losses from operations with futures on foreign currencies	–	(21)
Net gains from operations with futures on shares	–	65
Net gains/(losses) from operations with derivatives	<u>377</u>	<u>(481)</u>

*(Millions of Russian Rubles)***25. Other income**

	2009	2008
Rental income	33	36
Income from sale of foreclosed assets	19	7
Penalties received	11	25
Income from operations with precious coins	11	–
Dividends received	–	7
Other	18	21
Other income	92	96

26. Personnel and other operating expenses

	2009	2008
Fixed wages and salaries	2 350	2 593
Social security costs	311	393
Severance payments	28	41
Employee benefits and allowances	13	48
Variable staff remuneration	11	72
Personnel expenses	2 713	3 147
Depreciation of premises and equipment	373	246
Other expenses related to premises and equipment	268	179
Taxes other than on income	221	272
Rent	173	234
Amortisation of software	146	70
Advertising and marketing services	142	371
IT expenses	115	219
Contribution to state deposit insurance system	102	70
Professional services	101	65
Communication expenses	93	148
Security services	54	48
Personnel related expenses	35	26
Administrative expenses	26	63
Mailing and postal services	25	42
Business trip expenses	19	67
Charity	2	9
Provision for legal claims	2	–
Other	44	63
Other operating expenses	1 941	2 192

27. Taxation

The corporate income tax expense comprises:

	2009	2008
Current tax charge	36	556
Deferred tax charge/(credit) – origination and reversal of temporary differences	362	(320)
Less: deferred tax recognised directly in other comprehensive income	(9)	3
Income tax expense	389	239

Russian legal entities must file individual tax declarations. The tax rate for banks for profits other than on state securities was 20% for 2009 and 24% for 2008. The tax rate for companies other than banks was also 20% for 2009 and 24% for 2008. The tax rate for interest income on state securities was 15% for Federal taxes.

(Millions of Russian Rubles)

27. Taxation (continued)

The effective income tax rate differs from the statutory income tax rates. A reconciliation of the income tax expense based on statutory rates with actual is as follows:

	<u>2009</u>	<u>2008</u>
Profit/(loss) before tax	(4 590)	651
Statutory tax rate	20%	24%
Theoretical income tax expense/(benefit) at the statutory rate	(918)	156
Change in unrecognised deferred tax assets	1 277	–
Income on state securities taxed at different rates	(8)	(11)
Non-deductible expenditures	30	33
Underpaid current tax for prior periods	8	–
Tax exempt income	–	(3)
Effect of changes in tax rates (from 24% to 20%)	–	66
Other non-temporary differences	–	(2)
Income tax expense	389	239

Deferred tax assets and liabilities as of 31 December and their movements for the respective years comprise:

	<u>Origination and reversal of temporary differences</u>			<u>Origination and reversal of temporary differences</u>			
	<u>31 December 2007 (at 24%)</u>	<u>In the income statement</u>	<u>In other comprehensive income</u>	<u>31 December 2008 (at 20%)</u>	<u>In the income statement</u>	<u>In other comprehensive income</u>	<u>31 December 2009 (at 20%)</u>
Tax effect of deductible temporary differences:							
Allowance for loan impairment	–	136	–	136	(136)	–	–
Deferred income/accrued expenses	83	38	–	121	(24)	–	97
Effective interest rate accrual	–	114	–	114	(69)	–	45
Derivatives	28	14	–	42	(25)	–	17
Unutilised tax losses (begin to expire in 2018)	–	17	–	17	1 616	–	1 633
Securities	29	(27)	3	5	–	(3)	2
Deferred tax asset	140			435			1 794
Tax effect of taxable temporary differences:							
Property and equipment	(61)	(44)	–	(105)	12	–	(93)
Allowance for loan impairment	(36)	36	–	–	(418)	–	(418)
Securities	–	–	–	–	–	(6)	(6)
Effective interest rate accrual	(24)	24	–	–	–	–	–
Others	(9)	9	–	–	–	–	–
Deferred tax liability	(130)			(105)			(517)
Unrecognised deferred tax asset	–			–			(1 277)
Deferred tax asset, net	10			330			–

The Group has available RUB 1 633 million of tax losses carried forwards which begin to expire in 2018, if not utilised.

(Millions of Russian Rubles)

28. Risk management

Introduction

Risk is inherent in the Group's activity 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 soundness 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, market risk (both trading and non-trading) and operational risk.

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

Board of Directors

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

Management Board

The Management Board has the responsibility to monitor the overall risk process within the Group.

Risk Committees

The Risk Committees have the overall responsibility for the development of the risk strategy and implementing principles, frameworks, policies and limits. They are responsible for the fundamental risk issues and manage and monitor relevant risk decisions. The Risk Committees of the Group include:

- ▶ Assets and Liabilities committee (combined ALCO / Trading risk committee);
- ▶ Credit risk committee;
- ▶ Credit committees;
- ▶ Operational risk committee.

Risk Management

The Value and Risk Management Department (VRM) is responsible for implementing and maintaining risk related procedures to ensure an independent control process.

Compliance

Compliance function in the Group is particularly dedicated to comprehensive control in the meaning of identification, assessment and analysis of the risks linked to the following domains:

- ▶ Anti-money laundering and counter - terrorism financing;
- ▶ Investor protection, i.e. market abuse (insider trading and market manipulation), transactions with financial instruments including personal transactions and incompatibility of mandates, conflicts of interests, interests of borrowers;
- ▶ Data protection, including personal data, banking secrecy, duty of confidentiality etc.;
- ▶ Ethics and anti-fraud fighting.

Credit Product factory

Credit Product Factory is an independent (from business) unit, managing counterparty risk (legal entities and individuals) on a transactional level. At the same time this unit is responsible for:

- ▶ Management of the lending processes of the Bank end-to-end;
- ▶ Development of transactional counterparty risk assessment models;
- ▶ IFRS provisioning methodology, calculation and reporting.

(Millions of Russian Rubles)

28. Risk management (continued)

Risk management structure (continued)

Asset and Liability Management Department

Asset and Liability Management Department is responsible for managing the Group's assets and liabilities and the overall financial structure. It is also primarily responsible for the funding and liquidity risks of the Group.

Audit committee

The Audit Committee assists the Board of Directors. It does this by supervising, on behalf of the Board, the integrity, efficiency and effectiveness of the internal control measures and the risk management in place, paying special attention to correct financial reporting. The Audit Committee also oversees the company's processes to comply with laws and regulations.

Internal Audit

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 management, and reports its findings and recommendations to the Audit Committee.

Risk measurement

The Group's risks are measured using a method which reflects both the expected loss likely to arise in normal circumstances and unexpected losses, which are an estimate of the ultimate actual loss based on statistical models. The models make use of probabilities derived from historical experience, adjusted to reflect the economic environment. The Group also runs worst case scenarios that would arise in the event that extreme events which are unlikely to occur do, in fact, occur.

Monitoring and controlling risks is primarily performed based on limits established by the Group. These limits reflect the business strategy and market environment of the Group as well as the level of risk that the Group is willing to accept, with additional emphasis on selected industries. In addition the Group monitors and measures the overall risk bearing capacity in relation to the aggregate risk exposure across all risks types and activities.

For the purposes of managing market risk (both trading and non-trading) the Group's statement of financial position was virtually split into two parts: the Banking Book and the Trading Book.

Trading book - includes the Group's proprietary positions in financial instruments which are intentionally held for short-term resale and/or which are taken on by the Group with the intention of benefiting in the short term from actual and/or expected differences between their buying and selling prices.

Banking book - includes everything, except for the assets and liabilities of the Trading book, both financial assets and liabilities and financial commitments and contingencies,

The split of the books reflects not only the split of the items in statement of financial position, but also the risks and the limits for them. Within the Banking book all the market risks are minimised.

Information compiled from all the businesses is examined and processed in order to analyse, control and identify early risks. On a monthly basis this information is presented to the Management Board and the Risk Committees. Audit Committee receives a comprehensive risk report once a quarter which is designed to provide all the necessary information to assess and conclude on all relevant risks of the Group.

For all levels throughout the Group, specifically tailored risk reports are prepared and distributed in order to ensure that all business divisions have access to extensive, necessary and up-to-date information.

Risk mitigation

As part of its overall risk management, the Group uses derivatives and other instruments to manage exposures resulting from changes in interest rates and foreign currencies rates.

The Group actively uses collateral to reduce its credit risks (see below for more details).

(Millions of Russian Rubles)

28. Risk management (continued)

Risk management structure (continued)

Excessive risk concentration

Concentrations arise when a number of counterparties are engaged in similar business activities, or have similar economic features that would cause their ability to meet contractual obligations to be similarly affected by changes in economic, political or other conditions. Concentrations indicate the relative sensitivity of the Group's performance to developments affecting a particular industry location.

In order to avoid excessive concentrations of risks, the Group's policies and procedures include specific guidelines to focus on maintaining a diversified portfolio. Identified concentrations of credit risks are controlled and managed accordingly.

Credit risk

The Group takes on exposure to credit risk which is the risk that one party to a financial instrument will cause a financial loss for the other party by failing to discharge an obligation. Exposure to credit risk arises as a result of the Group's lending and other transactions with counterparties giving rise to financial assets.

The Group structures the levels of credit risk it undertakes by placing limits on the amount of risk accepted in relation to one borrower, or groups of borrowers, and to industry segments. The concentration limits (on the level of credit risk by product and/or industry sector) are responsibility of Credit Risk Committee. Such risks are monitored on a quarterly basis.

Individual credit limits (per borrower, or groups of borrowers) are set in the Group by the Credit committees (collegial bodies) in accordance with the approved powers.

In 2009, the Group had the following committees whose competence included setting individual credit risk limits:

- ▶ Main Credit Committee (regular meetings are held at least twice a week, areas of competence cover review and approval of any credit limits , approve limits for transactions with banking counterparties)
- ▶ Operative Credit Committee (regular meetings are held at least once a week, major areas of competence cover review and approval of credit limits from 1.25 million EUR to 7.5 million EUR (depending on internal rating of the Client);
- ▶ SME Credit Committee (major areas of competence cover review and approval of credit limits up to 1 million EUR for SME clients);
- ▶ Credit Committee of Retail business (areas of competence cover review and approval of credit limits from 0,05 to 0,1 million EUR (plastic cards), from 1 to 5 million EUR (Mortgage loans), from 0,2 to 0,5 million EUR (Car loans) for transactions with Retail clients);
- ▶ Small Credit Committee of Retail business (areas of competence cover review and approval of credit limits up to 0,05 million EUR (plastic cards), up to 1 million EUR (Mortgage loans), up to 0,2 million EUR (Car loans) for transactions with Retail clients);

All the committees operate at the Head office of the Group except for sub-sections of the Small Credit Committee which are organised at branches and take decisions on granting retail loans and loans to SMEs.

A decision on credit risk limit is taken on the basis of analysing financial and non-financial information (both financial and management reporting information is used for the analysis) on the borrower's business. During the analysis special attention is paid to financial indicators of the business, including the analysis of assets and liabilities, equity, revenues and profit – both in static and in dynamic. When analysing financial position of individuals, the Group pays special attention to confirmation of the borrower's claimed income and availability of assets owned by the borrower, which could serve as the evidence of the solid financial position. The main goal of the analysis is to determine opportunities and sources for repayment of loans. All information on material risks relating to the customers whose credit status is deteriorating is timely analysed by the management.

Credit risk monitoring includes control of all the terms and conditions identified when the limit was set, in particular, intended purpose, account turnovers, credit portfolio, financial position and performance, etc. Corporate borrowers are monitored on quarterly basis whereas individuals are reviewed annually.

(Millions of Russian Rubles)

28. Risk management (continued)

Credit risk (continued)

The Group accepts the following assets for pledge as collateral: residential and non-residential properties, land, construction in progress assets, production and trading equipment, vehicles and production machinery, goods (finished products), raw materials, inventories, securities, other assets. Guarantees of the business owners or the Group's revenue generating or asset holding companies are accepted as additional collateral for loans. The Group usually uses a combination of different types of collateral and applies certain discounts to the value of collateral pledged. Mortgage pledge under a real risk of its loss or damage is insured by one of the insurance companies accredited by the Group. Lending is performed in accordance with the provisions and principles of the Lending policy of the Group. Lending process implies a set of thoroughly regulated procedures, which establish the order of work with a borrower.

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

As the Group is a member of KBC Group it implements on a revolving basis methodological principles and procedures focused on credit risk measurement, controlling and its reduction.

The table below shows the maximum exposure to credit risk for the components of the statement of financial position, including derivatives. The maximum exposure is shown gross, before the effect of mitigation through the use of master netting and collateral agreements.

	<i>Notes</i>	<i>Maximum exposure 31 December 2009</i>	<i>Maximum exposure 31 December 2008</i>
Cash and cash equivalents (excluding cash on hand)	7	7 927	14 533
Mandatory cash balances with the Central Bank of the Russian Federation		638	169
Trading securities		1	141
Due from other banks	8	17 498	8 304
Derivative financial assets	9	73	1 057
Loans to customers	10	90 900	139 002
Investment securities available for sale	11	4 679	137
Other assets	13	117	59
Financial commitments and contingencies	20	12 446	19 399
Total maximum credit risk exposure		134 279	182 801

Where financial instruments are recorded at fair value, the amounts shown above represent the current credit risk exposure but not the maximum risk exposure that could arise in the future as a result of changes in values.

For more details on the maximum exposure to credit risk for each class of financial instrument, references shall be made to the specific notes. The effect of collateral and other risk mitigation techniques is shown below.

Credit quality per class of financial assets

The Group analyses the credit quality of debt investment securities available for sale, debt trading securities and due from other banks on the basis of international ratings of the issuers. As Fitch and Standard & Poor's international rating scales are in general consistent in credit risk characteristics that they assign to particular ratings, the Group gathers and uses for the purpose of credit quality analysis ratings by either Fitch or Standard & Poor's as being complementary.

AAA - the highest credit rating assigned. The obligor's capacity to meet its financial commitment on the obligation is extremely strong.

AA - differs from the highest-rated obligations only to a small degree. The obligor's capacity to meet its financial commitment on the obligation is very strong.

A - more susceptible to the adverse effects of changes in circumstances and economic conditions than obligations in higher-rated categories. However, the obligor's capacity to meet its financial commitment on the obligation is still strong.

BBB - exhibits adequate protection parameters. However, adverse economic conditions or changing circumstances are more likely to lead to a weakened capacity of the obligor to meet its financial commitment on the obligation.

(Millions of Russian Rubles)

28. Risk management (continued)**Credit risk (continued)**

Obligations rated 'BB', 'B', 'CCC', 'CC', and 'C' are regarded as having significant speculative characteristics. 'BB' indicates the least degree of speculation and 'C' the highest. While such obligations will likely have some quality and protective characteristics, these may be outweighed by large uncertainties or major exposures to adverse conditions.

BB - less vulnerable to nonpayment than other speculative issues. However, it faces major ongoing uncertainties or exposure to adverse business, financial, or economic conditions which could lead to the obligor's inadequate capacity to meet its financial commitment on the obligation.

B - more vulnerable to nonpayment than obligations rated 'BB', but the obligor currently has the capacity to meet its financial commitment on the obligation. Adverse business, financial, or economic conditions will likely impair the obligor's capacity or willingness to meet its financial commitment on the obligation.

Analysis by credit quality of debt investment securities available for sale, debt trading securities and due from other banks outstanding at 31 December 2009 and 2008 is as follows:

	31 December 2009		31 December 2008		
	<i>Debt investment securities available for sale</i>	<i>Due from other banks</i>	<i>Debt trading securities</i>	<i>Debt investment securities available for sale</i>	<i>Due from other banks</i>
AA+ to AA-	–	449	–	–	–
A+ to A-	–	16 177	–	–	100
BBB+ to BBB-	4 392	798	141	137	6 979
BB+ to BB-	287	74	–	–	160
B+ to B-	–	–	–	–	382
Unrated	–	–	–	–	683
Total	4 679	17 498	141	137	8 304

Starting from 1 January 2009 the credit quality of corporate loans and trade finance is managed by the Group based on credit ratings set in accordance with internal PD model. PD model was applied by the Group in order to divide clients into the groups based on their creditworthiness using a statistical model of default probabilities for corporate clients.

Probability of Default (PD) - is the probability of insolvency of the counterparty for a specified period. In the practice of the Group the probability of default is estimated for the time horizon of one year. Rating of the probability of default (PD-rating) - is an indicator which takes values from 1 to 12 (where PDs 10, 11 and 12 – are determined to be impaired or default), which is set to each counterparty that has a calculated value of the probability of default on a special scale. The table below shows the master scale of PD ratings:

PD rating	Probability of default (%)
1	Up to 0.1
2	from 0.1 to 0.2
3	from 0.2 to 0.4
4	from 0.4 to 0.8
5	from 0.8 to 1.6
6	from 1.6 to 3.2
7	from 3.2 to 6.4
8	from 6.4 to 12.8
9	from 12.8 to 100
10	100
11	100
12	100

(Millions of Russian Rubles)

28. Risk management (continued)**Credit risk (continued)**

The PD-ratings 10, 11 and 12 are not calculated using the PD-model, and are assigned on the individual basis.

The table below shows the summarized credit quality of corporate loans and trade finance based on PD ratings as of 31 December 2009.

	<i>Neither past due nor impaired loans</i>									<i>Loans past due but not impaired</i>	<i>Individually Impaired loans (10 - 12)</i>	<i>Total</i>	
	<i>1</i>	<i>2</i>	<i>3</i>	<i>4</i>	<i>5</i>	<i>6</i>	<i>7</i>	<i>8</i>	<i>9</i>				<i>Not rated</i>
Corporate loans	–	125	–	2 072	3 414	5 957	8 838	3 285	4 223	96	5 054	17 260	50 324
Trade finance	–	–	–	–	50	14	48	23	575	–	–	1 701	2 411
Total	–	125	–	2 072	3 464	5 971	8 886	3 308	4 798	96	5 054	18 961	52 735

The credit quality of other part of the loan portfolio as of 31 December 2009 and for all loans to customers as of 31 December 2008 was managed by the Group by assigning one out of five quality categories. This classification is effected based on CBRF guidelines and the Group's internal methodologies. Risk assessment and financial assets classification is effected based on two principal parameters: evaluation of the financial position and debt servicing quality. The counterparty's financial position is determined by analyzing its creditworthiness and financial stability, assessing the turnover on the accounts, reviewing its credit history, as well as other objective and subjective factors. Debt servicing is assessed by identifying the fact of debt servicing as such, existence of overdue payments, use of funds of the specified purpose and sources of repayment.

The table below shows the credit quality by class (from 1 – 5 in the descending order of quality) of loans to customers.

	<i>Neither past due nor impaired loans</i>					<i>Loans past due but not impaired</i>	<i>Individually Impaired loans</i>	<i>Total</i>
	<i>1 High grade</i>	<i>2 Standard grade</i>	<i>3 Sub-standard grade</i>	<i>4 Problem grade</i>	<i>5 Loss grade</i>			
31 December 2009								
Corporate loans	6 606	13 324	6 395	1 623	62	5 054	17 260	50 324
Mortgage loans	886	28 651	935	328	602	553	952	32 907
Car loans	44	8 327	59	18	54	190	691	9 383
SME loans	2 103	513	384	100	17	73	756	3 946
Trade finance	647	28	–	35	–	–	1 701	2 411
Finance lease receivables	–	1 014	–	–	–	22	692	1 728
Corporate bonds	145	49	–	–	700	–	435	1 329
Credit cards	10	595	13	6	12	161	310	1 107
Municipal bonds	–	–	–	–	128	–	–	128
Total	10 441	52 501	7 786	2 110	1 575	6 053	22 797	103 263

	<i>Neither past due nor impaired loans</i>					<i>Loans past due but not impaired</i>	<i>Individually Impaired loans</i>	<i>Total</i>
	<i>1 High grade</i>	<i>2 Standard grade</i>	<i>3 Sub-standard grade</i>	<i>4 Problem grade</i>	<i>5 Loss grade</i>			
1 December 2008								
Corporate loans	25 656	33 301	8 192	1 165	96	1 231	4 028	73 669
Mortgage loans	288	35 374	93	37	16	482	429	36 719
Car loans	49	12 839	20	5	7	234	315	13 469
SME loans	4 176	1 236	516	164	21	90	338	6 541
Corporate bonds	2 284	1 160	579	1 311	–	–	443	5 777
Trade finance	1 251	199	1 580	–	–	17	196	3 243
Finance lease receivables	–	1 387	–	–	–	41	140	1 568
Credit cards	3	935	4	2	1	361	56	1 362
Municipal bonds	502	–	–	328	–	–	–	830
Consumer loans	–	89	–	–	–	–	–	89
REPO	–	20	–	–	–	–	–	20
Total	34 209	86 540	10 984	3 012	141	2 456	5 945	143 287

(Millions of Russian Rubles)

28. Risk management (continued)

Credit risk (continued)

It is the Group's policy to maintain accurate and consistent risk ratings across the credit portfolio. This facilitates focused management of the applicable risks and the comparison of credit exposures across all lines of business and products. The rating system is supported by a variety of financial analytics, combined with processed market information to provide the main inputs for the measurement of counterparty risk. All internal risk ratings are tailored to the various categories and are derived in accordance with the Group's rating policy. The attributable risk ratings are assessed and updated regularly.

Aging analysis of past due but not impaired loans to customers

	Less than 30 days	31 to 90 days	91 to 180 days	181 to 365 days	Total 2009
Corporate loans	2 452	667	1 592	343	5 054
Mortgage loans	553	–	–	–	553
Car loans	189	1	–	–	190
Credit cards	161	–	–	–	161
SME loans	73	–	–	–	73
Finance lease receivables	15	7	–	–	22
Total	3 443	675	1 592	343	6 053
	Less than 30 days	31 to 90 days	91 to 180 days	181 to 365 days	Total 2008
Corporate loans	1 182	49	–	–	1 231
Mortgage loans	482	–	–	–	482
Credit cards	319	18	24	–	361
Car loans	234	–	–	–	234
SME loans	90	–	–	–	90
Finance lease receivables	41	–	–	–	41
Trade finance	17	–	–	–	17
Total	2 365	67	24	–	2 456

Collateral and other credit enhancements

The required level of collateral cover is set by the Group's specialists for the groups of related borrowers with specified description of collateral types and taking into account lending limits set for these groups of related borrowers. The value of collateral is determined by application of a discount to market price of collateral. For inventory pledged, for which sales prices are readily available (cars, metals, raw materials, etc.), the evaluation basis is pricelist (adequacy review of prices is performed in accordance with internal procedures). The discount applied to these prices is from 20 to 30%. Prices on goods considerably dependent upon specific qualities of a particular product (footwear, household appliances, foods, etc.) are evaluated on the basis of carrying amounts, warehouse accounting prices, etc. with more substantial discounts (50% and more). For real estate, collateral is assessed on the basis of market value as reported by the professional valuer with a discount individually determined depending on the type of the asset, except for typical corporate business products. The amount of the required collateral cover is dependent upon lending exposure. The amount of this lending exposure is in all cases less than the discounted value of collateral. Credit cards loans and the majority of consumer loans are not collateralised.

(Millions of Russian Rubles)

28. Risk management (continued)**Collateral and other credit enhancements (continued)**

Fair value of collateral in respect of loans past due but not impaired and in respect of loans individually determined to be impaired at 31 December 2009 was as follows:

	<i>Residential mortgage</i>	<i>Other real estate</i>	<i>Securities</i>	<i>Vehicles</i>	<i>Other assets</i>	<i>Total</i>
Fair value of collateral - loan past due but not impaired						
Corporate loans	1 240	3 036	–	54	573	4 903
Mortgage loans	521	1	13	–	–	535
Car loans	–	–	–	188	–	188
SME loans	19	27	–	8	19	73
Finance lease receivables	–	–	–	15	5	20
Total	1 780	3 064	13	265	597	5 719
Fair value of collateral – individually impaired loans						
Corporate loans	1 488	10 554	–	100	4 117	16 259
Trade finance	–	613	–	–	1 088	1 701
Mortgage loans	900	8	16	–	–	924
SME loans	48	287	–	98	284	717
Car loans	–	–	–	663	–	663
Finance lease receivables	–	403	–	–	92	495
Total	2 436	11 865	16	861	5 581	20 759

Other assets pledged as collateral for loans past due but not impaired and individually impaired loans at 31 December 2009 comprise non-traded equities/ shares in the charter capital of the borrowers and their related parties (RUB 1 349 million), equipment (RUB 884 million), inventories (RUB 3 773 million) and pledge of rights (RUB 172 million).

Fair value of collateral in respect of loans past due but not impaired and in respect of loans individually determined to be impaired at 31 December 2008 was as follows:

	<i>Residential mortgage</i>	<i>Other real estate</i>	<i>Securities</i>	<i>Vehicles</i>	<i>Other assets</i>	<i>Total</i>
Fair value of collateral - loan past due but not impaired						
Corporate loans	–	703	–	116	186	1 005
Mortgage loans	456	–	19	–	–	475
Car loans	–	–	–	234	–	234
SME loans	6	99	–	16	36	157
Total	462	802	19	366	222	1 871
Fair value of collateral – individually impaired loans						
Corporate loans	–	2 755	–	28	1 083	3 866
Mortgage loans	353	8	13	–	–	374
SME loans	28	96	–	45	154	323
Car loans	–	–	–	308	–	308
Total	381	2 859	13	381	1 237	4 871

Other assets pledged as collateral for loans past due but not impaired and individually impaired loans at 31 December 2008 comprise non-traded equities/ shares in the charter capital of the borrowers and their related parties (RUB 284 million), equipment (RUB 282 million) and inventories (RUB 893 million).

See Note 10 for more detailed information with respect to the allowance for impairment of loans to customers.

(Millions of Russian Rubles)

28. Risk management (continued)

Collateral and other credit enhancements (continued)

Carrying amount per class of financial assets whose terms have been renegotiated

The table below shows the carrying amount loans to customers that would otherwise be past due or impaired whose terms have been renegotiated:

	31 December 2009		31 December 2008	
	<i>Unimpaired</i>	<i>Impaired</i>	<i>Unimpaired</i>	<i>Impaired</i>
Corporate loans	9 566	13 760	3 415	496
Mortgage loans	1 927	48	10	–
SME	839	294	203	20
Trade finance	582	1 605	1 541	16
Car loans	64	2	2	–
Plastic cards	3	–	–	–
Total	12 981	15 709	5 171	532

The renegotiation of terms includes extending of payment arrangements and the arrangement of interest rates, fines and commissions.

Impairment assessment

The main considerations for the loan impairment assessment include whether any payments of principal or interest are overdue 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 realizable 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 (including credit cards, residential mortgages and unsecured consumer lending) 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 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. The impairment allowance is then reviewed by credit management to ensure alignment with the Group's overall policy.

(Millions of Russian Rubles)

28. Risk management (continued)***Collateral and other credit enhancements (continued)***

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

	31 December 2009				31 December 2008			
	Russia	OECD	Other	Total	Russia	OECD	Other	Total
Assets:								
Cash and cash equivalents	10 072	441	5	10 518	15 725	2 117	17	17 859
Mandatory cash balances with the Central Bank of the Russian Federation	638	–	–	638	169	–	–	169
Trading securities	1	–	–	1	141	–	–	141
Due from other banks	916	16 582	–	17 498	8 158	100	46	8 304
Derivative financial assets	57	16	–	73	1 006	51	–	1 057
Loans to customers	90 900	–	–	90 900	139 002	–	–	139 002
Investment securities available for sale	4 679	–	–	4 679	137	–	–	137
Other assets	117	–	–	117	59	–	–	59
	107 380	17 039	5	124 424	164 397	2 268	63	166 728
Liabilities:								
Due to other banks	1 831	53 196	70	55 097	9 174	91 096	446	100 716
Derivative financial liabilities	76	94	–	170	1 050	240	–	1 290
Customer accounts	47 373	124	241	47 738	33 805	163	185	34 153
Debt securities issued	3 220	3 016	–	6 236	1 296	9 818	5	11 119
Other liabilities	148	–	–	148	120	–	–	120
Subordinated debt	–	6 944	–	6 944	–	6 744	–	6 744
	52 648	63 374	311	116 333	45 445	108 061	636	154 142
Net position	54 732	(46 335)	(306)	8 091	118 952	(105 793)	(573)	12 586
Financial commitments and contingencies	10 668	684	1 094	12 446	17 490	889	1 020	19 399

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. To limit this risk, management has arranged diversified funding sources in addition to its core deposit base, manages with liquidity in mind, and monitors future cash flows and liquidity on a daily basis. This incorporates an assessment of expected cash flows and the availability of high grade collateral which could be used to secure additional funding if required.

The Group has committed lines of credit that it can access to meet liquidity needs. In addition, the Group maintains a cash deposit (obligatory reserve) with the CBRF, the amount of which depends on the level of customer funds attracted.

The liquidity position is assessed and managed by the Group primarily on a standalone basis, based on certain liquidity ratios established by the CBRF and on stress testing.

Due to the operational liquidity needs liquidity target consists of two parts: cash and equivalents and bonds available for sale.

- ▶ The cash part serves as a liquidity buffer. The main reason for holding this buffer is to prevent the liquidity deficit in case of early repayment of large term deposits of clients.
- ▶ The available for sale bond portfolio serves as collateral with the CBRF. The minimum volume of the bond portfolio is determined by the volume of the necessary collateral in CBRF. The actual volume is determined according to the liquidity requirements to the liquid assets in part of bonds additionally to cash liquid assets.

(Millions of Russian Rubles)

28. Risk management (continued)**Liquidity risk and funding management (continued)***Analysis of financial liabilities by remaining contractual maturities*

The table below summarizes the maturity profile of the Group's financial liabilities at 31 December 2009 based on contractual undiscounted repayment obligations. Repayments which are subject to notice are treated as if notice were to be given immediately. However, the Group expects that many customers 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 Group's deposit retention history.

Financial liabilities As at 31 December 2009	Less than 3 months	3 to 12 months	1 to 5 years	Over 5 years	Total
Due to other banks	2 463	28 066	15 811	18 071	64 411
Foreign exchange derivative contracts					
- Contractual amounts payable	330	54	–	–	384
- Contractual amounts receivable	(246)	(46)	–	–	(292)
Customer accounts	24 233	16 343	10 327	–	50 903
Debt securities issued	3 536	1 823	1 323	–	6 682
Subordinated debt	137	328	2 444	7 492	10 401
Total undiscounted financial liabilities	30 453	46 568	29 905	25 563	132 489

Financial liabilities As at 31 December 2008	Less than 3 months	3 to 12 months	1 to 5 years	Over 5 years	Total
Due to other banks	15 361	28 299	48 225	15 099	106 984
Foreign exchange derivative contracts					
- Contractual amounts payable	2 306	3 827	–	–	6 133
- Contractual amounts receivable	(2 114)	(2 860)	–	–	(4 974)
Customer accounts	23 934	10 693	280	27	34 934
Debt securities issued	969	6 494	4 929	–	12 392
Subordinated debt	136	329	2 263	7 901	10 629
Total undiscounted financial liabilities	40 592	46 782	55 697	23 027	166 098

The table below shows the contractual expiry by maturity of the Group's financial commitments and contingencies.

	Less than 3 months	3 to 12 months	1 to 5 years	Over 5 years	Total
2009	6 066	5 325	987	187	12 565
2008	7 245	5 110	5 546	1 587	19 488

The Group expects that not all of the contingent liabilities or commitments will be drawn before expiry of the commitments.

The Group's capability to repay its liabilities relies on its ability to realize an equivalent amount of assets within the same period of time.

The maturity analysis does not reflect the historical stability of current accounts. Their liquidation has historically taken place over a longer period than indicated in the tables above. These balances are included in amounts due in less than three months in the tables above.

Included in customer accounts are term deposits of individuals. In accordance with the Russian legislation, the Group is obliged to repay such deposits upon demand of a depositor. Refer to Note 15.

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 a VaR methodology, which reflects the interdependency between risk variables. 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.

(Millions of Russian Rubles)

28. Risk management (continued)

Market risk (continued)

Market risk – Trading

The responsible committees have set limits on the level of risk that may be accepted. The Group applies a VaR methodology to assess the market risk positions held and to estimate the potential economic loss based upon a number of parameters and assumptions for various changes in market conditions. VaR is a method used in measuring financial risk by estimating the potential negative change in the market value of a portfolio at a given confidence level and over a specified time horizon. The Group uses a historical VaR model for equity and currency risk. These calculations are based on the historical data from the last 2 years.

For managing the interest rate risk the sensitivity to the reasonable possible change (RPC) of yield curve is applied. RPC is constructed for instruments which generates future cash flows.

Simultaneously with VaR and sensitivity the Group establishes position limits on issuers, shares, collateral under reverse REPO deals, etc.

Objectives and limitations of the VaR Methodology

The Group uses historical VaR model to assess possible changes in the market value of the trading portfolio based on historical data from the past two years. The VaR models are designed to measure market risk in a normal market environment. The distribution is calculated by using historical data. The use of VaR has limitations because it assumes that future price movements will follow a statistical distribution. Due to the fact that VaR relies heavily on historical data to provide information and may not clearly predict the future changes and modifications of the risk factors, the probability of large market moves may be underestimated if changes in risk factors fail to align with the historical distribution assumption. VaR may also be under- or over-estimated due to the assumptions placed on risk factors and the relationship between such factors for specific instruments. Even though positions may change throughout the day, the VaR only represents the risk of the portfolios at the close of each business day, and it does not account for any losses that may occur beyond the 99% confidence level.

In practice the actual trading results will differ from the VaR calculation and, in particular, the calculation does not provide a meaningful indication of profits and losses in stressed market conditions. To determine the reliability of the VaR models, actual outcomes are monitored regularly to test the validity of the assumptions and the parameters used in the VaR calculation.

VaR assumptions

The VaR that the Group measures is an estimate, using a confidence level of 99% of the potential loss that is not expected to be exceeded if the current market risk positions were to be held unchanged for one day. The use of a 99% confidence level means that, within a one day horizon, losses exceeding the VaR figure should occur, on average, not more than once every hundred days.

Since VaR is an integral part of the Group's market risk management, VaR limits have been established for trading operations and exposures are reviewed daily against the limits by management.

VaR 1d, 99%	<i>Foreign exchange</i>	<i>Equity</i>	<i>Effects of correlation</i>	<i>Total</i>
31 December 2009	(20.94)	(0.21)	0.21	(20.94)
31 December 2008	(1.15)	(0.28)	0.25	(1.18)

(Millions of Russian Rubles)

28. Risk management (continued)

Market risk (continued)

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 income statement.

The sensitivity of the income statement is the effect of the assumed changes in interest rates on the net interest income for one year, based on the floating rate non-trading financial assets and financial liabilities held at 31 December. The sensitivity of equity is calculated by revaluing fixed rate available-for-sale financial assets at 31 December for the effects of the assumed changes in interest rates based on the assumption that there are parallel shifts in the yield curve.

	Increase in basis points 2009	Sensitivity of loss before tax 2009	Sensitivity of equity 2009
Currency			
RUR	711	8	(153)
EUR	85	7	–
USD	16	13	–
	Decrease in basis points 2009	Sensitivity of loss before tax 2009	Sensitivity of equity 2009
Currency			
RUR	711	(8)	153
EUR	85	(7)	–
USD	16	(13)	–
	Increase in basis points 2008	Sensitivity of profit before tax 2008	Sensitivity of equity 2008
Currency			
RUR	2 181	35	(91)
EUR	35	4	–
USD	92	76	–
	Decrease in basis points 2008	Sensitivity of profit before tax 2008	Sensitivity of equity 2008
Currency			
RUR	2 181	(35)	91
EUR	35	(4)	–
USD	92	(76)	–

Currency risk

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

According to the CBRF instruction, FX position in each currency shouldn't exceed 10% of the total Bank's capital, calculated by RAL. Within the Banking Book and the Trading Book virtual split almost all the Group's limit is transferred to the Trading Book. Moreover part of FX position limit is transferred for branches settlements. Speculative operations within the Banking book are in conflict with Parent principles. According to the Parent principles, all foreign exchange risk should be transferred to the Trading book. Thus the currency risk in the Banking Book is minimized (the target value is 0).

(Millions of Russian Rubles)

28. Risk management (continued)

Market risk (continued)

The tables below indicate the currencies to which the Group had significant exposure at 31 December 2009 on its non-trading monetary assets and liabilities and its forecast cash flows. The analysis calculates the effect of a reasonably possible movement of the currency rate against the RUB, with all other variables held constant on the income statement (due to the fair value of currency sensitive non-trading monetary assets and liabilities). The effect on equity does not differ from the effect on the income statement. A negative amount in the table reflects a potential net reduction in income statement or equity, while a positive amount reflects a net potential increase.

Currency	Change in	Effect on profit	Change in	Effect on profit
	currency rate in % 2009	before tax 2009	currency rate in % 2008	before tax 2008
USD	12	(406)	12	(178)
EUR	25	(212)	25	(81)

Operational risk

Operational risk is defined as the risk of loss resulting from inadequate or failed internal processes, people and systems or from external events. Operational risks include the risk of fraud, and legal, compliance and tax risks.

The Group continues the implementation of an operational risk management framework supported by operational risk management governance. The main precept of operational risk management is that ultimate responsibility for managing operational risk lies with line management, which receives support from local operational risk managers ('LORM') and is supervised by the operational risk committee ('ORC'). The ORC takes concrete risk mitigating measures either directly or via line management. The LORMs are specifically trained employees who also keep business functions.

The framework consists of a number of building blocks for managing operational risks, which are gradually being implemented. These building blocks are described in the ORM Policy, which also includes the methodology applied to define the operational risk capital charge as well as the methodologies used for IFRS and RAL provisioning purposes. The building blocks consist of:

- ▶ The Loss Events Database: since 2009 all operational losses of EUR 1,000 or more are recorded in a central database and reported to the ORC twice a year;
- ▶ Standards of Best Practice: The Bank translated standards of best practices into internal procedures. These standards cover such risks as access rights management, dual controls, accounting controls, complaints handling, etc. The ORC monitors the proper implementation of these standards and may allow exceptions to be made pursuant to a strict waiver procedure;
- ▶ Key Risk Indicators ('KRI'): A KRI implementation project has been launched. KRIs help monitor the exposure against certain operational risks. For a selected number of KRIs data are already being collected. The LORMs assume an essential role in determining the KRI in consultancy with the ORM Division.

29. Fair values of financial instruments

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

The Group uses the following hierarchy for determining and disclosing the fair value of financial instruments by valuation technique:

- ▶ Level 1: quoted (unadjusted) prices in active markets for identical assets or liabilities;
- ▶ Level 2: techniques for which all inputs which have a significant effect on the recorded fair value are observable, either directly or indirectly.

(Millions of Russian Rubles)

29. Fair values of financial instruments (continued)

The following table shows an analysis of financial instruments recorded at fair value by level of the fair value hierarchy:

At 31 December 2009	Level 1	Level 2	Total
Financial assets			
Trading securities	1	–	1
Derivative financial instruments	–	73	73
Investment securities available for sale	4 679	–	4 679
	4 680	73	4 753
Financial liabilities			
Derivative financial instruments	–	170	170
	–	170	170
At 31 December 2008			
	Level 1	Level 2	Total
Financial assets			
Trading securities	141	–	141
Derivative financial instruments	–	1 057	1 057
Investment securities available for sale	137	–	137
	278	1 057	1 335
Financial liabilities			
Derivative financial instruments	–	1 290	1 290
	–	1 290	1 290

There have been no transfers from level 2 to level 1 and vice versa in 2009.

Financial instruments recorded at fair value

The following is a description of the determination of fair value for financial instruments which are recorded at fair value using valuation techniques. These incorporate the Group's estimate of assumptions that a market participant would make when valuing the instruments.

Derivatives

Derivatives valued using a valuation technique with market observable inputs are mainly interest rate swaps, currency swaps and forward foreign exchange contracts. The most frequently applied valuation techniques include forward pricing and swap models, using present value calculations. The models incorporate various inputs including the credit quality of counterparties, foreign exchange spot and forward rates and interest rate curves.

Fair value of financial assets and liabilities not carried at fair value

Set out below is a comparison by class of the carrying amounts and fair values of the Group's financial instruments that are not carried at fair value in the consolidated statement of financial position. The table does not include the fair values of non-financial assets and non-financial liabilities.

	31 December 2009			31 December 2008		
	Carrying value	Fair value	Unrecognised gain/(loss)	Carrying value	Fair value	Unrecognised gain/(loss)
Financial assets						
Cash and cash equivalents	10 518	10 518	–	17 859	17 859	–
Mandatory cash balances with the Central Bank of the Russian Federation	638	638	–	169	169	–
Due from other banks	17 498	17 498	–	8 304	8 304	–
Loans to customers	90 900	88 298	(2 602)	139 002	128 833	(10 169)
Financial liabilities						
Due to other banks	55 097	48 560	6 537	100 716	91 774	8 942
Customer accounts	47 738	47 251	487	34 153	34 232	(79)
Debt securities issued	6 236	6 386	(150)	11 119	10 250	869
Subordinated debt	6 944	7 151	(207)	6 744	5 295	1 449
Total unrecognised change in unrealised fair value			4 065			1 012

(Millions of Russian Rubles)

29. Fair values of financial instruments (continued)

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

Cash and cash equivalents are carried at amortised cost, which approximates current fair value.

Loans and receivables carried at amortised cost

The fair value of floating rate instruments is normally their carrying amount. The estimated fair value of fixed interest rate instruments is based on estimated future cash flows expected to be received discounted at current interest rates for new instruments with similar credit risk and remaining maturity.

The Group believes that the carrying amount of due from other banks balances closely approximates their fair value as all the loans granted to other banks are of a short term nature and expire shortly after the reporting date.

Liabilities carried at amortised cost

The fair value of debt securities in issue is based on quoted market prices. The estimated fair value of fixed interest rate instruments with stated maturity, for which a quoted market price is not available, was estimated based on expected cash flows discounted at current interest rates for new instruments with similar credit risk and remaining maturity. The fair value of liabilities repayable on demand or after a notice period ("demandable liabilities") is estimated as the amount payable on demand, discounted from the first date that the amount could be required to be paid.

30. Maturity analysis of assets and liabilities

In its day-to-day liquidity management performed by the Treasury and liquidity reporting to ALCO the Group uses information from management accounts, which are based on statutory financial reporting figures. The liquidity analysis based on the international financial reporting figures as adjusted above is used as a subsequent control tool and in reporting to the international finance creditors.

The tables below shows an analysis of financial assets and liabilities as of 31 December 2009 and 2008 according to when they are contracted to be recovered or settled, except for mortgage loans, which are divided based on recursion model, which uses statistic data for period of 1 year for estimation of future payments. See Note 28 for the Group's contractual undiscounted repayment obligations.

31 December 2009	Demand and less than 1 month	From 1 to 3 months	From 3 to 12 months	From 12 months to 5 years	Over 5 years	Overdue	Total
Cash and cash equivalents	10 518	–	–	–	–	–	10 518
Mandatory cash balances with the Central Bank of the Russian Federation	638	–	–	–	–	–	638
Trading securities	1	–	–	–	–	–	1
Due from other banks	5 266	9 128	2 803	300	1	–	17 498
Derivative financial assets	50	23	–	–	–	–	73
Loans to customers	5 255	8 958	22 400	41 605	5 662	7 020	90 900
Investment securities available for sale	4 679	–	–	–	–	–	4 679
Other assets	107	10	–	–	–	–	117
Total financial assets	26 514	18 119	25 203	41 905	5 663	7 020	124 424
Due to other banks	2 116	359	26 673	13 839	12 110	–	55 097
Derivative financial liabilities	54	30	8	78	–	–	170
Customer accounts	17 223	6 703	15 366	8 446	–	–	47 738
Debt securities issued	17	3 443	1 696	1 080	–	–	6 236
Other liabilities	144	1	3	–	–	–	148
Subordinated debt	123	15	316	2 018	4 472	–	6 944
Total financial liabilities	19 677	10 551	44 062	25 461	16 582	–	116 333
Net liquidity gap	6 837	7 568	(18 859)	16 444	(10 919)	7 020	8 091
Cumulative liquidity gap	6 837	14 405	(4 454)	11 990	1 071	8 091	

(Millions of Russian Rubles)

30. Maturity analysis of assets and liabilities (continued)

The Group has received significant funds from the Parent (as of 31 December 2009 – RUB 57 657 million). Any significant withdrawal of these funds would have an adverse impact on the operations of the Group. Management believes that this level of funding will remain with the Group for the foreseeable future and that in the event of withdrawal of funds, the Group would be given sufficient notice so as to realize its liquid assets to enable repayment.

31 December 2008	<i>Demand and less than 1 month</i>	<i>From 1 to 3 months</i>	<i>From 3 to 12 months</i>	<i>From 12 months to 5 years</i>	<i>Over 5 years</i>	<i>Overdue</i>	<i>Total</i>
Cash and cash equivalents	17 859	–	–	–	–	–	17 859
Mandatory cash balances with the Central Bank of the Russian Federation	169	–	–	–	–	–	169
Trading securities	141	–	–	–	–	–	141
Due from other banks	8 085	46	173	–	–	–	8 304
Derivative financial assets	73	96	888	–	–	–	1 057
Loans to customers	13 585	19 022	41 556	54 276	9 371	1 192	139 002
Investment securities available for sale	137	–	–	–	–	–	137
Other assets	59	–	–	–	–	–	59
Total financial assets	40 108	19 164	42 617	54 276	9 371	1 192	166 728
Due to other banks	2 617	12 516	24 659	45 852	15 072	–	100 716
Derivative financial liabilities	97	95	998	22	78	–	1 290
Customer accounts	19 802	4 011	10 171	143	26	–	34 153
Debt securities issued	658	297	5 890	4 274	–	–	11 119
Other liabilities	120	–	–	–	–	–	120
Subordinated debt	114	18	319	1 808	4 485	–	6 744
Total financial liabilities	23 408	16 937	42 037	52 099	19 661	–	154 142
Net liquidity gap	16 700	2 227	580	2 177	(10 290)	1 192	12 586
Cumulative liquidity gap	16 700	18 927	19 507	21 684	11 394	12 586	

31. Related party disclosures

In accordance with IAS 24 “Related Party Disclosures”, parties are considered to be related if one party has the ability to control the other party or exercise significant influence over the other party in making financial or operational decisions. In considering each possible related party relationship, attention is directed to the substance of the relationship, not merely the legal form.

Related parties may enter into transactions which unrelated parties might not, and transactions between related parties may not be effected on the same terms, conditions and amounts as transactions between unrelated parties.

(Millions of Russian Rubles)

31. Related party disclosures (continued)

The volumes of related party transactions, outstanding balances at the year end, and related expense and income for the year are as follows:

	2009				2008			
	Parent	Other significant shareholders	Entities under common control	Key management personnel	Parent	Other significant shareholders	Entities under common control	Key management personnel
Consolidated statement of financial position:								
Cash and cash equivalents (contractual interest rates: 2009: 0.14%; 2008: 0.23%)	273	–	–	–	1 887	–	–	–
Due from other banks (contractual interest rates: 2009: 0.2 – 6.5%; 2008: 23%)	16 168	–	–	–	100	–	–	–
Gross amount of loans and advances to customers (contractual interest rates: 2009: 10 – 17%; 2008: 12 – 18%)	–	–	598	647	–	–	675	624
Allowance for impairment of loans to customers	–	–	(40)	(4)	–	–	(17)	(3)
Other assets	2	–	–	–	–	–	–	–
Due to other banks (contractual interest rates: 2009: 0.32 – 8.75%; 2008: 2.97 – 16%)	51 170	322	3	–	86 148	386	36	–
Customer accounts (contractual interest rates: 2009: 0.7 – 17.5%; 2008: 4.75 – 11.5%)	–	–	105	103	42	–	271	173
Debt securities issued (contractual interest rate: 2009: 9.1%; 2008: 9.1%)	155	–	–	–	693	–	–	–
Other liabilities	14	–	1	–	–	–	–	34
Subordinated debt (contractual interest rate: 2009: 5.8 – 8.0%; 2008: 5.8- 8.0%)	6 333	–	–	–	6 149	–	–	–
Consolidated income statement:								
Interest income	207	–	102	93	108	–	89	19
Interest expense	(4 893)	(32)	(5)	(11)	(5 079)	(27)	(11)	(36)
Allowance for loan impairment	–	–	(23)	(1)	–	–	(6)	(3)
Fee and commission income	–	–	4	6	1	–	2	14
Fee and commission expense	(3)	–	–	–	(7)	–	(1)	(16)
Net (losses)/gains from trading in foreign currencies	296	–	33	(2)	(168)	–	3	–
Net losses from operations with derivatives	(13)	–	(1)	–	–	–	–	–
Other income	–	–	–	–	–	–	10	–
Administrative and other operating expenses	(12)	–	–	–	–	–	–	–
Credit related commitments:								
Undrawn credit lines	500	–	–	6	500	–	–	26

Compensation of key management personnel was comprised of the following:

	2009	2008
Salaries and other short-term benefits	102	108
Social security costs	3	3
Total key management compensation	105	111

(Millions of Russian Rubles)

32. Capital adequacy

The Group maintains an actively managed capital base to cover risks inherent in the business. The adequacy of the Group's capital is monitored using, among other measures, the ratios established by the Basel II Capital Accord and the ratios established by the CBRF in supervising the Group.

During the past year, the Group had complied in full with all its externally imposed capital requirements.

The primary objectives of the Group's capital management are to ensure that the Group complies with externally imposed capital requirements and that the Group maintains strong credit ratings and healthy capital ratios in order to support its business and to maximise shareholders' value.

The Group manages its capital structure and makes adjustments to it in the light of changes in economic conditions and the risk characteristics of its activities. In order to maintain or adjust the capital structure, the Group may adjust the amount of dividend payment to shareholders, return capital to shareholders or issue capital securities. No changes were made in the objectives, policies and processes from the previous years.

Capital adequacy ratio under Basel II Capital Accord

Starting 2008 the Group applies guidelines set out in June 2006 by the Basel Committee of Banking Regulation and Supervision in "International Convergence of Capital Measurement and Capital Standards: a Revised Framework" ("Basel II").

The Group uses following approaches stipulated by the Basel II:

- ▶ The minimum capital requirements for credit risk are calculated based on the standardized approach supported by an external rating assessment;
- ▶ The minimum capital requirements for market risk are calculated under standardized measurement method as combination of interest rate risk, equity position risk and foreign exchange risk according to predefined models. The basic structure of the 1996 Market Risk Amendment regarding the treatment of market risk remains unchangeable. Employable models were adjusted in accordance with methodology used under standardized approach for calculating the minimum capital requirements for credit risk;
- ▶ The minimum capital requirements for operational risk are calculated based on Basic Indicator Approach.

The Group's capital adequacy ratio, computed in accordance with the Basel II Capital Accord as at 31 December 2009 and 2008, comprised:

	31 December 2009	31 December 2008
Tier 1 capital	13 260	17 582
Tier 2 capital	6 658	6 653
Regulatory capital	19 918	24 235
Weighted risks		
Credit risk	94 021	137 042
Market risk	372	142
Operational risk	14 899	20 091
Total weighted risk volume	109 292	157 275
Tier 1 capital ratio	12.13%	11.18%
Total capital ratio	18.22%	15.41%