Consolidated Financial Statements

Halyk Bank of Kazakhstan and Subsidiaries

December 31, 2002 and 2001
with Report of Independent Auditors

Halyk Bank of Kazakhstan and Subsidiaries

Consolidated Financial Statements

December 31, 2002 and 2001

Contents

Ernst & Young
st. Furmanova 273
Almaty 480099 Kazakhstan
Phone: 7(3272) 585 960
7(3272) 585 969
Fax: 7(3272) 585 961

Эрнст энд Янг
Казахстан, 480099 г.Алматы
Фурманова 273
Телефон: 7(3272) 585 960
7(3272) 585 969
Факс: 7(3272) 585 961

Report of Independent Auditors

To the Board of Directors and Shareholders
OJSC "Halyk Bank of Kazakhstan" and Subsidiaries

We have audited the accompanying consolidated balance sheet of Halyk Bank of Kazakhstan and Subsidiaries (the "Group") as of December 31, 2002 and the related consolidated statements of income, changes in shareholders' equity and cash flows for the year then ended. These financial statements are the responsibility of the Group's management. Our responsibility is to express an opinion on these financial statements based on our audit. The Group's consolidated financial statements for the year ended December 31, 2001 were audited by other auditors, whose report, dated March 26, 2002 expressed an unqualified opinion on those financial statements.

We conducted our audit in accordance with International Standards on Auditing. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the consolidated financial position of the Group at December 31 2002 and the consolidated results of its operations and its cash flows for the year then ended in conformity with International Financial Reporting Standards as published by the International Accounting Standards Board.

Ernst & Young Kazakhstan

March 25, 2003

Halyk Bank of Kazakhstan and Subsidiaries

Consolidated Balance Sheets

December 31, 2002 and 2001

(in thousands of Kazakh Tenge)

	Notes	2002	2001
Assets			
Cash and cash equivalents	4	**17,687,828**	12,554,396
Obligatory reserves	5	**4,525,381**	4,662,961
Due from other banks	6	–	5,036,488
Trading securities	7	**23,506,982**	–
Investment securities:			
-available-for-sale	8	**5,783,439**	14,560,801
-held-to-maturity	8	**2,982,832**	–
Commercial loans and advances, net	9	**125,816,039**	80,517,958
Premises and equipment, net	11	**7,045,844**	6,817,228
Other assets, net		**1,933,832**	2,974,076
Total assets		**189,282,177**	127,123,908
Liabilities and shareholders' equity			
Amounts owed to the Government	12	**449,025**	102,182
Due to other banks and financial institutions	13	**32,106,910**	16,184,017
Amounts owed to customers	14	**135,383,373**	99,126,400
Debt securities issued	15	**4,468,713**	2,356,254
Dividends payable	16	**394,459**	–
Other liabilities		**2,292,578**	2,451,816
Total liabilities		**175,095,058**	120,220,669
Minority interest		**-**	216
Shareholders' equity:			
Share capital:			
Common shares	16	**7,422,600**	5,422,600
Preferred shares	16	**2,261,150**	–
		9,683,750	5,422,600
Additional paid-in-capital		**2,085,600**	956,415
Treasury shares		**(14,043)**	–
Reserves		**544,152**	146,443
Retained earnings		**1,887,660**	377,565
Total shareholders' equity		**14,187,119**	6,903,023
Total liabilities and shareholders' equity		**189,282,177**	127,123,908
Financial commitments and contingencies	28	**50,597,409**	30,471,547

The accompanying notes are an integral part of these consolidated financial statements.

Halyk Bank of Kazakhstan and Subsidiaries

Consolidated Statements of Income

Years ended December 31, 2002 and 2001

(in thousands of Kazakh Tenge, except earnings per share)

	Notes	2002	2001
Interest income:			
Loans		**13,008,226**	8,733,441
Debt securities		**1,860,556**	1,520,145
Deposits with other banks		**454,887**	586,566
		15,323,669	10,840,152
Interest expense:			
Deposits from customers		**(6,189,032)**	(4,153,290)
Deposits and loans from other banks		**(593,662)**	(412,760)
Debt securities		**(406,961)**	(288,472)
Loans from other financial institutions		**(327,276)**	(168,277)
		(7,516,931)	(5,022,799)
Net interest income before provision for losses		**7,806,738**	5,817,353
Provision for losses	10	**(6,199,456)**	(4,460,958)
Net interest income after provision for losses		**1,607,282**	1,356,395
Fee and commission income	17	**5,316,807**	4,570,090
Write-back of dormant customer accounts	18	**3,698,298**	–
Dealing (losses) profits, net	19	**(389,910)**	19,973
Gains less losses from foreign currencies	20	**1,238,221**	1,188,413
Gains less losses from securities	21	**676,942**	326,447
Other operating income	22	**608,092**	1,188,097
		11,148,450	7,293,020
Payroll and other staff costs		**3,726,007**	2,523,186
General and administrative expenses	23	**3,229,505**	2,512,870
Occupancy and equipment		**1,207,001**	1,026,038
Taxes other than income taxes		**875,218**	935,398
Fee and commission expense	17	**1,132,756**	1,411,082
Other provisions	10	**411,837**	167,537
		10,582,324	8,576,111
Income before income tax		**2,173,408**	73,304
Income tax expense	24	**(302,245)**	(42,232)
Net income after income tax		**1,871,163**	31,072
Minority interest		**–**	(10)
Net income		**1,871,163**	31,062
Basic earnings per share (in KZT)	25	**27.22**	0.57

The accompanying notes are an integral part of these consolidated financial statements.

Halyk Bank of Kazakhstan and Subsidiaries

Consolidated Statements of Changes in Shareholders' Equity

Years ended December 31, 2002 and 2001

(in thousands of Kazakh Tenge)

	Share Capital	Additional Paid-in-Capital	Treasury Shares	Securities Revaluation Reserve	Premises and Equipment Revaluation Reserve	Retained Earnings	Total
At January 1, 2001	5,422,600	955,571	(571)	–	384,691	126,831	6,889,122
Sale of treasury shares	–	844	571	–	–	–	1,415
Net income	–	–	–	–	–	31,062	31,062
Revaluation of assets	–	–	–	–	(18,576)	–	(18,576)
Transfers	–	–	–	–	(219,672)	219,672	–
At December 31, 2001	**5,422,600**	**956,415**	**–**	**–**	**146,443**	**377,565**	**6,903,023**
Purchase of treasury shares	**–**	(1,488)	**(14,876)**	**–**	**–**	**–**	**(16,364)**
Sale of treasury shares	**–**	**209**	**833**	**–**	**–**	**–**	**1,042**
Preferred shares issued and paid	**2,261,150**	**1,130,464**	**–**	**–**	**–**	–	**3,391,614**
Common shares issued and paid	**2,000,000**	–	–	**–**	**–**	**–**	**2,000,000**
Dividends on preferred shares	**–**	–	–	–	**–**	**(394,459)**	**(394,459)**
Transfers	**–**	–	–	**–**	**(33,391)**	**33,391**	**–**
Revaluation of securities available for sale	**–**	**–**	**–**	**431,100**	**–**	**–**	**431,100**
Net income	–	–	–	–	**–**	**1,871,163**	**1,871,163**
At December 31, 2002	**9,683,750**	**2,085,600**	**(14,043)**	**431,100**	**113,052**	**1,887,660**	**14,187,119**

The accompanying notes are an integral part of these consolidated financial statements.

Halyk Bank of Kazakhstan and Subsidiaries

Consolidated Statements of Cash Flows

Years ended December 31, 2002 and 2001

(in thousands of Kazakh Tenge)

	2002	2001
Cash flows from operating activities:		
Net income before minority interest and income taxes	**2,173,408**	73,304
Adjustments for:		
Depreciation and amortization	**1,207,001**	1,213,903
Provision for losses	**6,611,293**	4,628,495
Profit on sale of premises and equipment	**(199,415)**	(148,203)
Operating income before changes in net operating assets	**9,792,287**	5,767,499
(Increase)/ decrease in operating assets:		
Obligatory reserves	**137,580**	294,276
Due from other banks	**5,036,488**	(4,004,127)
Trading securities	**(23,506,982)**	-
Commercial loans and advances	**(51,546,520)**	(32,627,602)
Other assets	**481,319**	(875,493)
Increase/ (decrease) in operating liabilities:		
Amounts owed to the Government	**346,843**	-
Due to other banks and financial institutions	**15,922,893**	10,777,586
Amounts owed to customers	**36,256,973**	16,615,604
Other liabilities	**(172,921)**	(3,374,700)
Net cash used in operating activities before income taxes	**(7,252,042)**	(7,426,957)
Income tax paid	**(250,058)**	(64,500)
Net cash used in operating activities	**(7,502,100)**	(7,491,457)
Cash flows from investing activities:		
Sale of available-for-sale securities	**9,093,113**	-
Purchase of held-to-maturity securities	**(2,867,483)**	14,900,872
Purchase of premises and equipment	**(1,466,688)**	(885,355)
Proceeds from sale of premises and equipment	**388,055**	225,822
Net cash provided by investing activities	**5,146,997**	14,241,339
Cash flows from financing activities:		
Proceeds from issue of share capital	**5,391,614**	-
Purchase of treasury shares	**(16,364)**	-
Sale of treasury shares	**1,042**	1,415
Debt securities issued	**2,112,459**	98,956
Minority interest	**(216)**	
Net cash provided by financing activities	**7,488,535**	100,371
Net change in cash and cash equivalents	**5,133,432**	6,850,253
Cash and cash equivalents at the beginning of the year	**12,554,396**	5,704,143
Cash and cash equivalents at the end of the year	**17,687,828**	12,554,396
Supplementary information:		
Interest paid	**6,702,526**	4,447,339
Interest received	**15,259,140**	10,980,484

The accompanying notes are an integral part of these consolidated financial statements.

(Amounts in tables are in thousands of Kazakh Tenge)

1. Description of Business

Halyk Bank of Kazakhstan and Subsidiaries (the "Group") provide retail and corporate banking services in Kazakhstan. The Parent company of the Group, i.e. Halyk Bank of Kazakhstan (the "Bank"), was registered in 1995 and is domiciled in the Republic of Kazakhstan.

The Bank's primary business consists of originating loans and guarantees, attracting deposits from legal entities and individuals, trading with securities, foreign currency and derivative instruments, execution and arrangement of precious metals transactions, conducting credit card operations and sale of state saving bonds. In addition, the Bank is authorized to accept pension fund deposits, acts as agent for the Government of the Republic of Kazakhstan and provide other banking services to its customers. Note 26 lists all of the Bank's subsidiaries whose activities include, leasing, telecommunication services and asset management.

The address of the Bank's registered office is: 97 Rozybakiyev Street, Almaty, 480046, Republic of Kazakhstan.

The Bank has a primary listing in the Kazakhstani Stock Exchange.

The Bank's head office is in Almaty. As of December 31, 2002 the Bank had 20 regional branches, 147 sub-regional offices and 457 cash settlement units (December 31, 2001: 20 regional branches, 157 sub-regional offices and 455 cash settlements units) located throughout Kazakhstan.

The Group had 8,663 and 8,261 employees as of December 31, 2002 and 2001, respectively.

2. Basis of Preparation

General

These consolidated financial statements have been prepared in accordance with International Financial Reporting Standards ("IFRS") issued by the International Accounting Standards Board. These financial statements are presented in thousands of Kazakhstani Tenge ("KZT"). The KZT is utilized as the majority of the Group's transactions are denominated, measured, or funded in KZT. Transactions in other currencies are treated as transactions in foreign currencies.

The Group maintains its records and prepares its consolidated financial statements in Kazakh Tenge ("KZT") in accordance with Kazakh accounting and tax regulations. The accompanying consolidated financial statements differ from the consolidated financial statements issued for statutory purposes in Kazakhstan in that they reflect certain adjustments, not recorded on the Group's books, which are appropriate to present the financial position, results of operations, and cash flows of the Group in accordance with IFRS. The principal adjustments are primarily related to the allowance for losses, deferred taxes and the accrual of dividends on preferred shares:

	2002	2001
Statutory shareholders' equity at December 31	**16,824,703**	8,246,540
Dividends on preferred shares	**(394,459)**	–
Allowance for losses	**(2,220,535)**	(1,320,927)
Deferred taxes	**(9,243)**	(9,243)
Other	**(13,347)**	(13,347)
IFRS shareholders' equity at December 31	**14,187,119**	6,903,023

2. Basis of Preparation (continued)

The KZT is not a fully convertible currency outside the Republic of Kazakhstan. During 2001, transactions denominated in foreign currencies are recorded using the official exchange rates quoted by the National Bank of Kazakhstan (the "NBK"), which closely approximate the market exchange rates quoted by the Kazakhstan Stock Exchange ("KASE"). The Group started to apply the market exchange rates quoted by KASE for all of its transaction from January 1, 2002.

The market exchange rates at December 31, 2002 and December 31, 2001 were KZT 155.85 = US Dollar 1 and KZT 150.94 = US Dollar 1, respectively. The official exchange rates at December 31, 2002 and 2001 were KZT 155.60 = US Dollar 1 and KZT 150.20 = US Dollar 1, respectively.

At March 25, 2003, the market exchange rate was KZT 152.20 = US Dollar 1.

The accompanying consolidated financial statements were authorized for issue by the Bank's Chairman and Deputy Chairman on March 25, 2003.

3. Summary of Significant Accounting Policies

The following is a summary of the significant accounting policies used in preparing the consolidated financial statements.

Basis of Presentation

The accompanying consolidated financial statements have been prepared in accordance with IFRS, and have been prepared under the historical cost convention, modified by fair value accounting for securities as required by IFRS 39 "Financial Instruments: Recognition and Measurement".

The preparation of financial statements requires management to make estimates and assumptions that affect reported amounts. These estimates are based on information available as of the date of the consolidated financial statements. Actual results, therefore, could differ from those estimated.

Subsidiaries and Consolidation

Subsidiaries comprise those companies and other entities in which the Group, directly or indirectly, has power to exercise control over financial and operating policies.

Subsidiaries are consolidated from the date of registration and are no longer consolidated from the date of liquidation. The cost of an acquisition is measured at the fair value of the assets given up or liabilities undertaken at the date of acquisition, plus costs directly attributable to the acquisition. Inter-company transactions, balances, and unrealized surpluses and deficits on transactions between group companies have been eliminated. Where necessary, the accounting policies used by subsidiaries have been changed to ensure consistency with the policies adopted by the Group.

Related Parties

Related parties include the Group's shareholders, key management personnel, investee and affiliated companies.

Cash and Cash Equivalents

Cash and cash equivalents consist of cash on hand, amounts due from the NBK, and amounts due from other financial institutions which mature within ninety days from the date of origination and are free from contractual encumbrances.

3. Summary of Significant Accounting Policies (continued)

Obligatory Reserves

Obligatory Reserves represent mandatory reserve deposits and cash 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 for the purpose of the cash flow statement.

Due From Other Banks

Due from other banks includes amounts due from, and loans to, other financial institutions, which mature within more than ninety days from the date of origination, and amounts which mature within ninety days but are not free of contractual encumbrances.

Trading Securities

Securities purchased principally for the purpose of generating a profit from short-term fluctuations in price or dealers' margin are classified as trading securities. Trading securities are initially recognized under the policy for the recognition of financial instruments and are subsequently measured at fair value, based on market values as of the balance sheet date. Realized and unrealized gains and losses resulting from operations with trading securities are recognized in the consolidated statements of income as dealing gains (losses). Interest earned on trading securities is reported as interest income in the consolidated statements of income. Dividends received are reported as dividend income.

In determining estimated fair value, securities are valued at the last trade price if quoted on an exchange, or the last bid price if traded over-the-counter. When market prices are not available or if liquidating the Group's position would reasonably be expected to impact market prices, fair value is determined by reference to price quotations for similar instruments traded in different markets or management's estimates of the amounts that can be realized from an orderly disposition over a period of time, assuming current market conditions.

Repurchase and Reverse Repurchase Agreements

Repurchase and reverse repurchase agreements are utilized by the Group as an element of its treasury management and trading business. These agreements are accounted for as financing transactions.

Securities sold under repurchase agreements are accounted for as trading or available-for-sale securities and funds received under these agreements are included into amounts due to credit institutions or amounts due to customers. Securities purchased under agreements to resell ('reverse repos') are recorded as amounts due from credit institutions or as loans to customers.

Securities purchased are not recognized in the financial statements, unless these are sold to third parties, in which case the purchase and sale are recorded with the gain or loss included in dealing gains (losses). The obligation to return them is recorded at fair value as a trading liability.

Any related income or expense arising from the pricing spreads of the underlying securities is recognized as interest income or expense, accrued using the effective interest rate method, during the period that the related transactions are open.

3. Summary of Significant Accounting Policies (continued)

Recognition of Financial Instruments

The Group recognizes financial assets and liabilities on its balance sheet when, and only when, it becomes a party to the contractual provisions of the instrument. Financial assets and liabilities are recognized using trade date accounting.

Financial assets and liabilities are initially recognized at cost, which is the fair value of the consideration given or received, respectively, including or net of any transaction costs incurred, respectively. The accounting policies for subsequent re-measurement of these items are disclosed in the respective accounting policies set out in the note.

Derivative Financial Instruments

In the normal course of business, the Group enters into various derivative financial instruments including futures, forwards, and options in the foreign exchange and capital markets. Such financial instruments are primarily held for trading and are initially recognized in the consolidated balance sheets at cost (including transaction costs, if any) and subsequently are measured at their fair value. Their 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 with positive market values (resulted in unrealised gains) are recorded as assets and derivatives with negative market values (resulted in unrealised losses) are reported as liabilities in the consolidated balance sheets. Gains and losses resulting from these instruments are included in the accompanying consolidated statements of income as dealing gains (losses).

Derivative instruments embedded in other financial instruments are treated as separate derivatives as their risks and characteristics are not closely related to the host contracts and the host contracts are not carried at fair value with unrealised gains and losses reported in income. An embedded derivative is a component of a hybrid (combined) financial instrument that includes both the derivative and a host contract with the effect that some of the cash flows of the combined instrument vary in a similar way to a stand-alone derivative. Gains arising from changes in the value of derivatives are included in the consolidated statements of income as dealing gains (losses).

Investment Securities

Following the adoption of IFRS 39 as of January 1, 2001, the Group classified its investment securities into two categories:

- Securities with fixed maturities and fixed or determinable payments that Management has both the positive intent and the ability to hold to maturity are classified as held-to-maturity; and
- Securities that are not classified by the Group as held-to-maturity or trading (see above) are included in the available-for-sale portfolio.

The Group classifies investment securities depending upon the intent of management at the time of the purchase. Shares of associates and subsidiaries held by the Group exclusively with a view to their future disposal are also classified as available-for-sale. Investment securities are initially recognized in accordance with the policy stated above and subsequently re-measured using the following policies:

1. Held-to-maturity investment securities – at amortized cost using the effective yield method. An allowance for impairment is estimated on a case-by-case basis.

3. Summary of Significant Accounting Policies (continued)

Investment Securities (continued)

2. Available-for-sale securities are subsequently measured at fair value, which is equal to the market value as at the balance sheet date. When debt securities with fixed maturities are non-marketable or no information is available on the market of similar instruments, fair value has been estimated as the discounted future cash flows using current interest rates. Non-marketable securities that do not have fixed maturities are stated at cost, less allowance for diminution in value unless there are other appropriate and workable methods of reasonably estimating their fair values.

   Gains and losses arising from changes in the fair value of available-for-sale securities are recognized in shareholders' equity in the period that the change occurs. When the securities are disposed of or impaired, the related accumulated fair value adjustment is included in the statement of income within gains less losses from securities.

Commercial Loans and Advances

Loans and advances are originated by the Group by providing money directly to the borrower and are carried at amortized cost. Loans and advances are recognized when cash is advanced to the borrowers. The accrual of interest income on loans is generally discontinued when a loan becomes 30 days past due as to principal or interest. When a loan is placed on non-accrual status and becomes 60 days past due, interest accrued in the current year but not received is reversed against interest income and interest accrued in prior years and not received is charged off against the allowance for losses. Subsequent payments by borrowers are applied to either principal or delinquent interest based on the estimated collectibility of the loan and delinquent interest at the time of payment. A non-accrual loan may be restored to accrual status when all principal and interest amounts contractually due are reasonably assured of repayment within a reasonable period.

Allowance for Impairment of Financial Assets

The Group establishes an allowance for impairment of financial assets when it is probable that the Group will not be able to collect the principal and interest according to the contractual terms of loans issued, held-to-maturity securities and other financial assets, which are carried at cost and amortized cost. The allowance for impairment of financial assets is defined as the difference between the carrying amounts and the present value of expected future cash flows, including amounts recoverable from guarantees and collateral, discounted at the original effective interest rate of the financial instrument. For instruments that do not have fixed maturities, expected future cash flows are discounted using periods during which the Group expects to realize the financial instrument.

The allowance is based on the Group's own loss experience and management's judgment as to the level of losses that will most likely be recognized from assets in each credit risk category by reference to the debt service capability and repayment history of the borrower. The allowance for impairment of financial assets in the accompanying consolidated financial statements has been determined on the basis of existing economic and political conditions. The Group is not in a position to predict what changes in conditions will take place in Kazakhstan and what effect such changes might have on the adequacy of the allowance for impairment of financial assets in future periods.

Changes in the allowances are reported in the consolidated statements of income of the related period. When a loan is not collectable, it is written off against the related allowance for impairment; if the amount of the impairment subsequently decreases due to an event occurring after the write-down, the reversal of the allowance is credited to the related impairment of financial assets in the statement of income.

3. Summary of Significant Accounting Policies (continued)

3. Summary of Significant Accounting Policies (continued)

Premises and Equipment

Fixed assets are recorded at historical cost adjusted for revaluations made until 1997 using indices provided by the State Committee of Statistics of the Republic of Kazakhstan less accumulated depreciation. Depreciation on assets under construction commences from the date the assets are ready for their intended use. Depreciation is calculated on a straight-line basis over the estimated useful lives of the assets as follows:

Buildings	15-50 years
Furniture, fixtures and equipment	4-10 years
Computers	4 years

Borrowings

Borrowings are recognized initially at ‘cost’, being their issue proceeds net of transaction costs incurred. Subsequently borrowings are stated at amortized cost and any difference between net proceeds and the redemption value is recognized in the income statement over the period of the borrowings using the effective interest method.

If the Group purchases its own debt, it is removed from the consolidated balance sheets and the difference between the carrying amount of a liability and the consideration paid is included in net trading income.

Income Taxes

Income taxes payable on profits, based on the applicable tax laws in Kazakhstan, is recognized as an expense in the period in which profits arise.

Deferred income taxes are accounted for under the balance sheet liability method and reflect the tax effect of all significant temporary differences between the tax base of assets and liabilities and their reported amounts in the accompanying consolidated financial statements. Deferred tax assets and liabilities are measured at tax rates that are expected to apply when the asset is realized or the liability settled, based on tax rates and tax laws that have been enacted or substantially enacted at the balance sheet date. Deferred tax assets are recognized when it is probable that sufficient taxable profits will be available against which the deferred tax assets can be utilized.

Current and deferred tax assets and liabilities are offset when they arise from the same tax reporting group and relate to the same tax authority and when the legal right to offset exists. Current and deferred taxes are recognized as tax benefit or expense except for deferred taxes recognized or disposed of on acquisition or disposal of a subsidiary.

Interest Income and Expense

Interest income and expense are recognized in the consolidated statements of income for interest bearing instruments on an accrual basis using the effective interest method. Interest income is suspended when loans become doubtful of collection. Such income is excluded from interest income until received.

Fee and Commission Income

Fees and commissions are generally recognized on an accrual basis. Commission and fees arising from negotiating, or participating in the negotiation of a transaction for a third party, such as the acquisition or the purchase or sale of businesses, are recognized upon completion of the underlying transaction.

3. Summary of Significant Accounting Policies (continued)

Foreign Currency Translation

Foreign currency transactions are accounted for at the exchange rates prevailing at the date of the transactions. Gains and losses resulting from the settlement of such transactions and from the translation of monetary assets and liabilities denominated in foreign currencies are recognized in the consolidated income statements within gains less losses from foreign currencies.

Translation differences on debt securities measured at fair value are included in the accompanying consolidated statements of income within gains less losses from foreign currencies.

Share Capital and Treasury Stock

Share capital

Share capital is recognized at the fair value of the consideration received net of the cost of the equity transactions, being the incremental external costs directly attributable to the equity

Treasury shares

Where the Group or its subsidiaries repurchase the Group's share capital or obtains rights to repurchase its share capital, the consideration paid including any attributable transaction costs net of income taxes is shown as a deduction from total shareholders' equity. Gains and losses on sales of treasury shares are charged or credited to the treasury share account in equity.

Dividends

Dividends on common shares and non-redeemable preferred shares are recognized as a liability in the period in which they are declared.

Fiduciary Assets

Assets held in trust or in a fiduciary capacity are not treated as assets of the Group and accordingly are not included in these consolidated financial statements.

Acceptances

Acceptances comprise undertakings by the Group to pay bills of exchange drawn on customers. The Group expects most acceptances to be settled simultaneously with the reimbursements from the customers. Acceptances are accounted for and disclosed as liabilities with corresponding contra assets.

Offsetting

Financial assets and financial liabilities are only offset and the net amount reported in the consolidated balance sheets when there is a legally enforceable right to offset the recognized amounts and the Group intends to either settle on a net basis, or to realize the asset and settle the liability simultaneously.

Social Costs

The Group has contributed social tax to the budget of the Republic of Kazakhstan for its employees. Prior to June 30, 2001 the Group contributed 26% of employees' salaries and related staff costs. Starting from July 1, 2001 the Group's social contributions rate was reduced to 21%. These contributions are expensed as incurred.

(Amounts in tables are in thousands of Kazakh Tenge)

3. Summary of Significant Accounting Policies (continued)

Comparative Figures

Certain of the 2001 amounts were reclassified to conform with the presentation of the 2002 consolidated financial statements. These reclassifications are summarized below:

	Amount
Consolidated balance sheet:	
Accrued interest income was reclassified to commercial loans and advances, net	3,289,035
Accrued interest expense was reclassified to amounts owed to customers	1,250,424

None of the above reclassifications impacted net income or shareholders' equity.

4. Cash and Cash Equivalents

Cash and cash equivalents consisted of the following at December 31:

	2002	2001
Interest bearing deposits in Kazakh banks	**11,077,024**	6,186,471
Correspondent accounts with OECD based banks	**3,342,021**	1,700,405
Cash on hand	**2,641,976**	3,667,520
Correspondent accounts with non-OECD based banks	**611,807**	–
Short term loans to other Kazakh banks	**15,000**	1,000,000
	17,687,828	12,554,396

Interest-bearing deposits represent overnight and short-term placements at other banks with annual contractual interest rates ranging as follows at December 31:

	2002		**2001**	
	KZT	**US Dollar**	**KZT**	**US Dollar**
Deposits with Kazakh banks	**9-13%**	**4%**	2-13%	5%
Short term loans to other Kazakh banks	**5%**	–	–	4-6%

Loans to other Kazakh banks are secured by securities held under reverse repurchase agreements in amounts to fully collateralize the deposits. Management regularly reviews the estimated fair value of the collateral to ensure that pledged securities are sufficient to cover the outstanding loans. These loans mature in January 2003 (2001: January 2002).

5. Obligatory Reserves

Obligatory reserves consisted of the following at December 31:

	2002	2001
Due from the NBK	**1,576,240**	2,010,204
Cash on hand allocated to obligatory reserves	**2,949,141**	2,652,757
	4,525,381	4,662,961

Under Kazakh legislation, the Group is required to maintain certain obligatory reserves, which are computed as a percentage of certain liabilities of the Group. Such reserves must be held in either non-interest bearing deposits with the NBK or in physical cash and maintained based on average monthly balances of the aggregate of deposits with NBK and physical cash. The use of such funds is, therefore, subject to certain usage restrictions.

(Amounts in tables are in thousands of Kazakh Tenge)

6. Due from Other Banks

Due from other banks consisted of the following at December 31:

	2002	2001
Time deposits	–	2,077,443
Loans to other Kazakh banks	–	3,008,028
	–	5,085,471
Less allowance for losses	–	(48,983)
	–	5,036,488

At December 31, 2001, the annual interest rates charged by the Group on loans to Kazakh banks ranged from 15% to 16% and matured in 2002.

7. Trading Securities

Trading securities, at estimated fair value, consisted of the following at December 31:

	2002	2001
Notes of the NBK	**10,148,019**	–
Treasury bills of the Ministry of Finance	**6,209,751**	–
Sovereign bonds of the Republic of Kazakhstan	**4,549,879**	–
Eurobonds of Kazakh banks	**2,129,283**	–
Bonds of Kazakh banks	**470,050**	–
	23,506,982	–

Notes of the NBK carry interest at 6% and mature in March 2003.

Treasury bills of the Ministry of Finance carry interest at rates ranging from 7% to 17% and mature between 2003 and 2006.

Sovereign bonds of the Republic of Kazakhstan carry interest at 11.125 % per annum and mature in 2007. Included in sovereign bonds of the Republic of Kazakhstan are securities pledged under repurchase agreements with other financial institutions whose estimated fair value amounted to KZT 3,720,900 thousand (Note 13).

Eurobonds of Kazakh banks carry interest at 7.125% per annum and mature in 2007.

Bonds of Kazakh banks carry interest at 9.1% per annum and mature in 2007.

(Amounts in tables are in thousands of Kazakh Tenge)

8. Investment Securities

Investment securities, at estimated fair value, consisted of the following at December 31:

	2002	2001
Available-for-sale:		
Treasury bills of the Ministry of Finance	**2,902,792**	4,636,791
Sovereign bonds of Kazakhstan	**1,955,666**	3,697,517
Corporate bonds	**592,649**	1,478,608
Bonds of Kazakh banks	**317,353**	–
Notes of the NBK	**14,979**	4,746,283
World Bank bonds	–	1,602
	5,783,439	14,560,801
Held-to-maturity		
Treasury bills of the Ministry of Finance	**1,566,011**	–
Corporate bonds	**1,152,997**	–
Local municipal bonds	**262,222**	–
World Bank bonds	**1,602**	–
	2,982,832	–

Treasury bills of the Ministry of Finance at December 31, 2002 carry interest at rates ranging from 7% to 17% per annum (2001: 7-17%) and mature between 2003 and 2007 (2001: 2002-2007).

Sovereign bonds of the Republic of Kazakhstan at December 31, 2002 carry interest at rates ranging from 11.125 % to 13.625% per annum (December 31, 2001: 8.375% to 13.625%) and mature between 2004 and 2007 (2001: 2002 and 2007). Included in sovereign bonds of the Republic of Kazakhstan are securities pledged under repurchase agreements with other financial institutions whose estimated fair value at December 31, 2002 amounted to KZT 1,955,666 thousands (December 31, 2001: KZT 2,449,682 thousand) (Note 13).

Corporate bonds at December 31, 2002 represent bonds of prime Kazakh corporations that carry interest at rates ranging from 8.5 % to 9% per annum (2001: 10.07%) and mature between 2003 and 2005 (2001: between 2002 and 2005).

At December 31, 2002 bonds of Kazakh banks carry interest at rates ranging from 7% to 11% per annum and mature between 2003 and 2007 (2001: 2002).

9. Commercial Loans and Advances

Commercial loans and advances consisted of the following at December 31:

	2002	2001
Commercial loans portfolio	**132,459,847**	84,220,362
Advances	**1,167,196**	34,195
	133,627,043	84,254,557
Allowance for losses	**(7,811,004)**	(3,736,599)
Total commercial loans and advances, net of allowance	**125,816,039**	80,517,958

(Amounts in tables are in thousands of Kazakh Tenge)

9. Commercial Loans and Advances (continued)

At December 31, 2002, the annual interest rates charged by the Group ranged from 11% to 28% per annum for KZT-denominated loans and advances (2001: 18% - 30%) and from 10% to 23% per annum for US Dollar-denominated loans and advances (2001: 13.5%-20.7%).

Loans and advances to shareholders and related parties, including employees, amounted to KZT 6,545,995 thousand and KZT 5,192,111 thousand at December 31, 2002 and 2001, respectively.

At December 31, 2002, the annual interest rates charged by the Group on loans to shareholders and related parties ranged from 18% to 31% per annum for KZT denominated loans (2001: 19% to 21%), and from 2% to 20% per annum for US Dollar denominated loans (2001: 8% to 11.5%).

Advances represent prepayments related to issued guarantees and letters of credit.

At December 31, 2002 and 2001, loans for which the accrual of interest has been suspended approximated KZT 661,211 thousand and KZT 1,194,525 thousand, respectively.

The Group's gross commercial loan portfolio is concentrated in the following main sectors at December 31:

	2002	**%**	2001	%
Agriculture (grain trading)	**21,962,277**	17%	11,520,135	14%
Wholesale trading	**16,375,035**	12%	17,438,441	21%
Oil and gas	**9,807,910**	7%	10,996,281	13%
Construction	**9,059,167**	7%	5,157,305	6%
Individuals	**7,511,974**	6%	4,414,448	5%
Retail trade	**7,302,901**	6%	3,693,163	4%
Food industry	**8,087,824**	6%	2,500,116	3%
Metallurgy	**6,158,711**	5%	2,073,920	2%
Light industry	**4,241,613**	3%	2,222,507	3%
Transportation	**3,855,444**	3%	7,497,902	9%
Chemical processing	**4,496,945**	3%	969,941	1%
Financial	**1,788,962**	1%	3,132,072	4%
Communication	**1,701,241**	1%	1,630,616	2%
Mining	**1,550,402**	1%	1,506,378	2%
Energy	**1,493,995**	1%	719,389	1%
Entertainment	**1,495,929**	1%	203,405	0%
Machinery and equipment production	**1,309,541**	1%	561,394	1%
Hospitality	**41,016**	0%	665,276	1%
Other	**24,218,960**	18%	7,317,673	9%
	132,459,847		84,220,362	

At December 31, 2002 and 2001, 10 major borrowers accounted for 30% and 27% of the Group's gross commercial loans and advances, respectively.

(Amounts in tables are in thousands of Kazakh Tenge)

10. Allowances for Losses

The movements on the allowance for losses consisted of the following:

	Loans to customers	Loans and advances to banks	Total
At January 1, 2001	2,120,00	15,772	2,135,772
Provision for the year	4,427,74	33,211	4,460,958
Charge offs	(2,811,148	–	(2,811,148)
At December 31, 2001	**3,736,59**	**48,983**	**3,785,582**
Provision (reversal) for the year	**6,248,43**	**(48,983)**	**6,199,456**
Charge offs	**(2,448,218**	**–**	**(2,448,218)**
Recoveries	**274,18**	**–**	**274,184**
At December 31, 2002	**7,811,00**	**–**	**7,811,004**

The allowance for loan losses consisted of the following at December 31:

	2002	2001
Pooled allowance	**2,954,177**	1,171,362
Specific allowance	**4,856,827**	1,565,237
	7,811,004	3,736,599

The movements on the allowance for losses on other transactions were as follows:

	Letters of credit and guarantees	Other assets	Total
At January 1, 2001	201,00	23,81	224,81
Provision for the year	–	167,53	167,53
Charge offs	–	(26,209	(26,20
Recoveries	(102,934	(22,169	(125,10
At December 31, 2001	**98,06**	**142,97**	**241,04**
Provision (reversal) for the year	**(38,503**	**450,34**	**411,83**
Charge offs	**–**	**(22,644**	**(22,64**
Recoveries	**–**	**107**	**107**
At December 31, 2002	**59,56**	**570,77**	**630,34**

(Amounts in tables are in thousands of Kazakh Tenge)

11. Premises and Equipment, net

The movements on the Group's premises and equipment were as follows:

	Buildings	Vehicles	Computers and banking equipment	Furniture and equipment	Total 2002	Total 2001
Cost/Valuation						
At January 1,	3,268,813	350,727	3,490,246	2,193,705	9,303,491	8,718,479
Additions	333,016	124,742	698,208	310,722	1,466,688	885,355
Disposals	(149,858)	(41,213)	(102,844)	(194,763)	(488,678)	(300,343)
At December 31	3,451,971	434,256	4,085,610	2,309,664	10,281,501	9,303,491
Depreciation:						
At January 1,	143,806	203,693	1,474,620	664,144	2,486,263	1,879,583
Charge for the year	293,093	56,788	494,961	204,590	1,049,432	829,404
Disposals	(151,865)	(42,416)	(75,177)	(30,580)	(300,038)	(222,724)
At December 31	285,034	218,065	1,894,404	838,154	3,235,657	2,486,263
Net Carrying Amount:						
At December 31, 2002	**3,166,937**	**216,191**	**2,191,206**	**1,471,510**	**7,045,844**	
					-	
At December 31, 2001	3,125,007	147,034	2,015,626	1,529,561	6,817,228	

12.

12. Amounts Owed to the Government

This amount represents funding for loans to agricultural companies under the EBRD post privatization program. Under this program, the Government provides 50% co-funding for financing provided to agricultural projects in Kazakhstan. These amounts bear interest at 2.8% per annum (2001: 2.8%) and mature between 2003 and 2006 (2001: between 2003 and 2006).

13. Due to Other Banks and Financial Institutions

Due to other banks and financial institutions consisted of the following at December 31:

	2002	2001
Loans from OECD based banks	**16,379,246**	5,296,184
Loans from Kazakh banks	**6,907,706**	2,449,682
Loans from EBRD	**4,204,884**	–
Loans from Small Business Development Fund	**2,401,355**	2,364,333
Overnight deposits	**1,924,748**	–
Correspondent accounts	**228,971**	94,718
Short term deposits from Kazakh banks	**60,000**	5,979,100
	32,106,910	16,184,017

At December 31, 2002 loans from OECD based banks are USD and EUR denominated, bear interest at rates ranging between 2.3% and 7.2% per annum (2001: 2.65% - 4.97%) and mature between 2003 and 2012 (2001: 2002).

(Amounts in tables are in thousands of Kazakh Tenge)

13. Due to Other Banks and Financial Institutions (continued)

At December 31, 2002 loans from Kazakh banks are US$ and KZT denominated, bear interest at rates ranging between 3% and 6.0% per annum (2001: 5.3%), and mature in 2003 (2001: 2003). Included in loans from Kazakh banks as of December 31, 2002 are loans amounting to KZT 5,767,566 thousand (2001: KZT 2,449,682 thousand) that are secured by a pledge over certain of the Group's securities whose fair values as of December 31, 2002 amounted to KZT 5,676,566 thousand (2001: KZT 2,449,682 thousand) (Note 7 and 8).

At December 31, 2002, the Group had several loans from the European Bank for Reconstruction and Development ("EBRD") amounting to USD 23,354 thousand, bearing annual interest at rates ranging from 4% to 6% per annum, (2001:4.1 %) and maturating between 2003 and 2004 (2001: 2003).

At December 31, 2002 loans from the Small Business Development Fund represent a pass-through credit line provided to the Group through the Government of the Republic of Kazakhstan from the European Bank for Reconstruction and Development ("EBRD") amounting to US Dollar 15,340 thousand (2001: US Dollar 15,740 thousand). Loans are granted to borrowers, based on the Group's analysis of their creditworthiness, under terms and conditions comparable to similar credit facilities. The facilities mature between 2003 and 2004 (2001: 2002 and October 2004) and bear contractual interest at rates ranging between 5% and 10.53% per annum. The amounts received under pass-through loans have been advanced to borrowers and included within commercial loans in the accompanying consolidated balance sheets.

Overnight deposits at December 31, 2002 carry interest at rates ranging from 3% to 4% per annum.

At December 31, 2001 the Group had deposits from Kazakh banks bearing annual interest at rates ranging from 1% to 16% and maturing in January 2003.

14. Amounts Owed to Customers

The amounts owed to customers included balances in customer current accounts and term deposits, and were analyzed as follows at December 31:

	2002	2001
Current accounts:		
Individuals	**17,716,805**	20,693,820
Commercial entities	**30,655,123**	19,314,498
Governmental entities	**5,395,910**	3,831,583
Term deposits:		
Individuals	**53,266,594**	34,237,309
Commercial entities	**28,185,486**	17,271,809
Governmental entities	**163,455**	3,777,381
	135,383,373	99,126,400

Term deposits at December 31, 2002 bear annual interest at rates ranging from 1% to 9% per annum (2001: from 1% to 10%) for KZT-denominated balances and from 1% to 7% per annum (2001: from 1% to 8%) for foreign currency-denominated balances.

(Amounts in tables are in thousands of Kazakh Tenge)

15. Debts Securities Issued

At December 31, 2002 and 2001, debt securities issued bear interest at 8% and 11.8% per annum, respectively. The repayment of these securities is indexed to the Tenge/US Dollar exchange rate as at the date of repayment of principal and interest. At December 31, 2002 and 2001, the bonds have a maturity of five and seven years, respectively. These subordinated securities are unsecured obligations of the Group and are subordinated in right of payments to all present and future senior indebtness and certain other obligations of the Group.

16. Shareholders' Equity

Authorized and issued share capital at December 31, 2002 consisted of 74,234,330 common shares (December 31, 2001: 54,226,000) and 22,611,500 preferred shares (December 31, 2001: nil). Each common share is entitled to one vote and shares equally in dividends declared. Preferred shares are not redeemable, carry a cumulative dividend of a minimum of 15.75% per annum and do not have any voting rights. All shares are KZT denominated and have a nominal value of KZT 100 each.

During 2002, the Group purchased 148,671 treasury shares at a total amount of KZT 16,364 thousand and sold 833 treasury shares at a total amount of KZT 1,042 thousand.

In September 2002, the Group issued 20,000,000 common shares with a nominal value of KZT 100 each that were fully paid.

During 2002, the Group accrued for dividends on preferred shares relating to 2002 amounting to KZT 394,459 thousand.

17. Fee and Commission Income and Expense

Fee and commission income and expense comprised the following:

	2002	2001
Commission income:		
Servicing customer accounts	**1,265,857**	1,129,939
Transfer operations	**986,358**	465,556
For services on pension payments	**912,159**	1,179,718
Purchase – sale of currencies	**673,365**	860,350
Letters of credit and guarantees issued	**254,923**	173,490
Debit/credit cards	**168,100**	101,948
Factoring	**114,742**	–
Servicing utility payments	**440,040**	376,154
Other	**501,263**	282,935
	5,316,807	4,570,090
Commission expense:		
Foreign currencies operations	**508,846**	731,752
Cash operations	**242,310**	257,364
Letters of credit and guarantees received	**6,360**	19,467
Debit/credit cards	**142,770**	104,534
Transfer operations	**63,883**	125,331
Servicing nostro and loro accounts	**52,823**	28,493
Other	**115,764**	144,141

(Amounts in tables are in thousands of Kazakh Tenge)

	1,132,756	1,411,082

18. Write Back of Dormant Customer Accounts

As allowed by the banking regulations in Kazakhstan, the Group has written back certain dormant customer accounts taken over from the State Saving Bank of Kazakh SSR (the "Predecessor Bank") amounting to KZT 3,698,298 thousand. Management believes that none of these accounts will be claimed in the future as these accounts have been dormant for more than nine years.

19. Dealing (Losses) Profits, net

Dealing (losses) profits, net comprised the following:

	2002	2001
Dealing profits		
Derivative financial instruments	**214**	4,596
Income from operations with precious metals	**268,954**	225,274
	269,168	229,870
Dealing losses		
Derivative financial instruments	**(658,864)**	(209,897)
Expenses from operations with precious metals	**(214)**	–
	(659,078)	(209,897)
Dealing (losses) profits, net	**(389,910)**	**19,973**

20. Gains less Losses from Foreign Currencies

Gain less losses from foreign currencies comprised the following:

	2002	2001
Net gain on revaluation of foreign currency denominated assets and liabilities	**62,106**	(112,475)
Net income from foreign currency trading	**1,176,115**	1,300,888
	1,238,221	1,188,413

21. Gains less Losses From Securities

Gains less losses from securities comprised the following:

	2002	2001
Change in fair value of trading securities	**541,186**	–
Sale and redemption, net	**135,756**	326,447
	676,942	326,447

(Amounts in tables are in thousands of Kazakh Tenge)

22. Other Operating Income

Other operating income comprised the following:

	2002	2001
Fines and penalties	**205,826**	186,252
Profit on disposal of premises and equipment	**199,415**	148,203
Other	**202,851**	853,642
	608,092	1,188,097

23. General and Administrative Expenses

General and administrative expenses comprised the following:

	2002	2001
Communication	**347,067**	353,322
Repair and maintenance	**206,234**	119,645
Advertisement	**322,703**	152,021
Security	**145,167**	142,465
Insurance of deposits	**355,000**	213,903
Business trip expenses	**213,948**	136,982
Transportation	**105,934**	103,553
Professional services	**53,935**	11,200
Loss from disposal of premises and equipment	**276,047**	–
Fines and penalties	**5,733**	119,472
Rent	**111,831**	161,319
Other	**1,085,906**	998,988
	3,229,505	2,512,870

24. Income Taxes

The Republic of Kazakhstan was the only tax jurisdiction in which the Group's income is taxable. The income tax expenses comprise:

	2002	2001
Current tax	**302,245**	32,989
Deferred tax	**-**	9,243
Provision for income taxes	**302,245**	42,232

(Amounts in tables are in thousands of Kazakh Tenge)

24. Income Taxes (continued)

The reconciliation between the provision for income taxes in the accompanying financial statements and income before taxes multiplied by the statutory tax rate of 30% for the years ended December 31 is as follows:

	2002	2001
Income before tax	**2,173,408**	73,304
Statutory tax rate	**30%**	30%
Income tax computed at the statutory tax rate	**652,022**	21,991
Non taxable income from state securities	**(1,488,745)**	(457,731)
Non taxable income from long term investment projects	**(248,863)**	–
Other non taxable income	**(2,342)**	–
Income of subsidiaries	**(78,547)**	–
Non deductible expenses		
- Interest on deposits	**562,241**	48,790
- Non business expenses	**522,331**	429,182
- Foreign exchange loss	**11,580**	–
- Other	**8307**	–
Change in unrecognized deferred tax assets	**364,261**	–
Provision for income taxes	**302,245**	42,232

Deferred tax balances, calculated by applying the statutory tax rates in effect at the respective balance sheet dates to the temporary differences between the tax base of assets and liabilities and the amounts reported in the consolidated financial statements, comprised the following at December 31:

	2002	2001
Deferred tax assets:		
Allowance for losses	**656,131**	268,973
Other accruals	–	57,763
Deferred tax Liabilities:		
Premises and equipment	**(291,870)**	(335,979)
Net deferred taxes	**364,261**	(9,243)
Unrecognized deferred tax assets	**(364,261)**	–
Net deferred tax liabilities	**–**	(9,243)

(Amounts in tables are in thousands of Kazakh Tenge)

25. Earnings per Share

A basic earnings per share is calculated by dividing the net income for the year attributable to ordinary shareholders by the weighted average number of ordinary shares outstanding during the year. The Group does not have any options or convertible debt or equity instruments. The Group did not declare or pay any dividends during 2002 and 2001.

	2002	2001
Net income attributable to ordinary shareholders and basic earnings per shares (in KZT thousands)	**1,476,704**	31,062
Weighted average number of ordinary shares	**54,241,298**	54,226,000
Earning per share (in KZT)	**27.22**	0.57

26. Subsidiaries

At December 31, 2002 and 2001 the principal subsidiaries of the Bank are as follows:

Subsidiary	*Ownership %*	*Domicile*	*Principal Business*
ZAO “Khalyk Leasing”	100.00%	Almaty	Leasing
ZAO “Kazteleport”	100.00%	Almaty	Telecommunication services
ZAO “KUPA NBK“	100.00%	Almaty	Asset management
HSBK (Europe) BV	100.00%	Amsterdam	Issueance and placement of Euro bonds on international financial markets

27. Commitments and Contingencies

General

The Group’s policy is to accrue contingencies in the accounting period in which a loss is deemed probable and the amount is reasonably determinable. In this regard, because of the uncertainties associated with the Kazakh tax and legal systems, the ultimate taxes as well as penalties and fines, if any, assessed may be in excess of the amounts paid to date and accrued at December 31, 2002. Management believes, based upon its best estimates, that the Group has paid or accrued all taxes that are applicable for the current and prior years, and complied with all essential provisions of laws and regulations of the Republic of Kazakhstan. In management’s opinion, the ultimate determination of the Group’s overall tax liability and potential loss contingencies, to the extent not previously provided, will not have a material effect on the consolidated financial position of the Group.

The Group’s proprietary trading activities involve the execution, settlement, and financing of various securities and financial instrument transactions. The execution of these transactions includes the purchase and sale of securities, and the purchase and sale of forward purchase and sales contracts for foreign currencies. These activities may expose the Group to additional risk in the event the counterparty to the transaction is unable to fulfill its contractual obligations.

In these situations, the Group may be required to purchase or sell financial instruments at prevailing market prices, which may not fully cover the obligations of the counterparty. The Group attempts to limit this risk by identifying and monitoring its individual and aggregate exposures to counterparties and establishing and maintaining procedures for counterparty limit authorization and implementation.

27. Commitments and Contingencies (continued)

General (continued)

Settlement activities involve the Group using securities as collateral in support of various secured financing sources. In the event the counterparty does not meet its contractual obligation to return the collateral, the Group may need to reacquire the securities to satisfy its obligations. The Group controls this risk by evaluating and establishing limits for its counter parties and monitoring the market value of securities pledged on a daily basis.

The Kazakh economy displays emerging market characteristics. These characteristics include lack of liquidity in the capital markets, and the existence of currency controls which causes the KZT to be illiquid outside Kazakhstan.

In addition to the emerging market characteristics mentioned above, the banking system is in a constant state of supervisory reform and additional laws and enforcement actions may be implemented to produce a more sound banking and financial system. The success and stability of the Kazakh economy may be significantly impacted by the government's actions with regard to supervisory, legal, and economic reforms.

28. Financial Instruments with Off-Balance Sheet Risk

General

In the normal course of business, the Group is a party to financial instruments with off-balance sheet risk. These financial instruments include credit-related financial instruments (commitments to extend credit, financial guarantees, commercial letters of credit) and derivative foreign exchange contracts. These instruments involve elements of credit and market risk in excess of the amounts recognized in the consolidated balance sheet.

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

Market risk represents the possibility that the value of financial instruments will change, either positively or negatively, with changes in market prices, such as interest or foreign exchange rates. The Group manages market risk through periodic estimation of potential losses that could arise from adverse changes in market conditions and establishing and maintaining appropriate stop-loss limits and margin and collateral requirements.

Credit-Related Financial Instruments

Commitments are contractual agreements to extend credit, which generally have fixed expiration dates or other termination requirements and require payment of a fee. Substantially all of the Group's commitments to extend credit are revocable as they are contingent upon the prospective borrower maintaining specific credit standards at the time of loan funding.Since many of the commitments are expected to expire without being drawn upon, the total commitment amounts do not necessarily represent future cash requirements.

Financial guarantees are conditional commitments issued by the Group to guarantee the performance of a customer to a third party. The credit risk involved in issuing guarantees is essentially the same as that involved in extending facilities to other customers.

(Amounts in tables are in thousands of Kazakh Tenge)

28. Financial Instruments with Off-Balance Sheet Risk (continued)

Credit-Related Financial Instruments (continued)

The Group applies similar principles as those applied in assessing the required allowance for losses under other credit facilities when assessing the likelihood of loss under a guarantee. Commercial letters of credit represent a financing transaction by a bank to its customer where the customer is usually the buyer/importer of goods and the beneficiary is typically the seller/exporter. Credit risk is limited as the merchandise shipped serves as collateral for the transaction.

The Group's exposure to loss under credit-related financial instruments is limited to the contractual amount and was as follows at December 31:

	2002	2001
Commitments to extend credit:		
Unrelated parties, foreign currency-denominated	**33,436,56**	342,069
Unrelated parties, KZT-denominated	**2,072,74**	131,476
Financial guarantees:		
Unrelated parties, foreign currency-denominated	**31,795,37**	22,070,955
Unrelated parties, KZT-denominated	**13,871,41**	5,622,310
Commercial letters of credit:		
Unrelated parties, foreign currency-denominated	**6,132,09**	2,794,687
Unrelated parties, KZT-denominated	**67,94**	328,967
	51,866,83	30,816,919
Less allowances	**(59,56**	(98,066)
Less cash collateral	**(1,209,86**	(247,306)
	50,597,40	30,471,547

At December 31, 2002, ten guarantees accounted for 28% (2001: 21%) of total financial guarantees and represented 68% (2001: 51%) of the Group's total shareholders' equity at that date.

At December 31, 2002, ten letters of credit accounted for 75% (2001: 21%) of total commercial letters of credit and represented 32% (2001: 51%) of the Group's total shareholders' equity at that date.

29. Maturity Analysis

The maturity of monetary assets and liabilities represents the remaining terms until repayment in accordance with the underlying contractual agreements and terms of issuance of the monetary asset or liability at the respective balance sheet date, except for trading securities which are shown as demand irrespective of their terms of issuance. In practice, the actual maturity of monetary assets and liabilities may differ from the contractual terms based on addenda to the contracts, which already exist.

The following assumptions and conditions have been adopted in the presentation of the Group's maturity analysis:

- Obligatory reserves, held in physical cash or deposits with the NBK, are considered as due after one year; however, their availability is dependent on the composition and maturity of the Group's liabilities in the form of customer accounts and certain other deposits.
- While trading securities are shown as demand, realizing such assets upon demand is dependent upon financial market conditions.
- The maturity of amounts due from other banks and commercial loans and advances is based on the contractual maturity date. The actual maturity may differ as loan agreements are often extended or rolled over to update interest rates and facilitate longer term financing for the borrowers. Amounts due from other banks and commercial loans and advances are shown gross, excluding any deductions with respect to the allowance for losses.
- The maturity of equity investments is considered to be over one year as the Group intends to hold such investments for long-term purposes.
- Amounts due to other banks and owed to customers are shown as having a remaining maturity based on the nature of the amount, which is typically demand for loro accounts, placements, and current accounts, and the contractual maturity date for loans and term deposits. Although the maturity of amounts owed to customers is usually extended beyond the original contractual maturity dates, these expected extensions are not taken into consideration in the maturity analysis.
- Other monetary assets and liabilities are predominantly current claims to and from third parties.

(Amounts in tables are in thousands of Kazakh Tenge)

29. Maturity Analysis (continued)

At December 31, the maturity of monetary assets and liabilities was as follows:

2002: *Monetary assets:*	Demand	Up to 1 month	1 to 3 months	3 to 6 months	6 to 12 months	Over 12 months	Total
Cash and cash equivalents	6,595,804	10,877,099	214,925	–	–	-	17,687,828
Obligatory reserves	–	–	–	–	–	4,525,381	4,525,381
Trading securities	23,506,982	–	–	–	–	–	23,506,982
Investment securities	–	165,666	142,383	-	1,077,033	7,381,189	8,766,271
Commercial loans and advances	–	10,808,832	12,794,461	10,697,265	30,249,229	69,077,256	133,627,043
Other monetary assets	–	1,355,562	–	–	–	204,762	1,560,324
	30,102,786	23,207,159	13,151,769	10,697,265	31,326,262	81,188,588	189,673,829
Monetary liabilities:							
Amounts owed to the Government	–	10,640	–	3,501	57,789	377,095	449,025
Due to other banks and financial institutions	228,971	9,344,324	–	4,701,820	13,112,482	4,719,313	32,106,910
Amounts owed to customers	52,569,810	17,297,083	11,489,645	14,993,155	11,866,163	27,167,517	135,383,373
Debt securities issued	–	–	–	–	–	4,468,713	4,468,713
Dividends payable	–	–	–	394,459	–	–	394,459
Other liabilities	–	2,292,578	–	–	–	–	2,292,578
	52,798,781	28,944,625	11,489,645	20,092,935	25,036,434	36,732,638	175,095,058
Net position	(22,695,995)	(5,737,466)	1,662,124	(9,395,670)	6,289,828	44,455,950	14,578,771
Accumulated gap	(22,695,995)	(28,433,461)	(26,771,337)	(36,167,007)	(29,877,179)	14,578,771	

2001: *Monetary assets:*	Demand	Up to 1 month	1 to 3 months	3 to 6 months	6 to 12 months	Over 12 months	Total
Cash and cash equivalents	5,367,925	5,550,300	1,636,1	–	–	–	12,554,396
Obligatory reserves	–	–	–	–	–	4,662,961	4,662,961
Due from other banks	–	–	–	1,376,292	1,376,292	2,332,887	5,085,471
Investment securities	–	3,342,834	1,246,007	260,644	260,644	9,450,672	14,560,801
Commercial loans and advances	–	8,983,190	5,264,918	14,114,252	14,114,252	41,777,945	84,254,557
Other monetary assets	–	2,348,914	–	–	–	56,376	2,405,290
	5,367,925	20,225,238	8,147,096	15,751,188	15,751,188	58,280,841	123,523,476
Monetary liabilities:							
Amounts owed to the Government	–	27,542	–	–	–	74,640	102,182
Due to other banks and financial institutions	94,718	2,366,313	751,538	3,697,768	5,759,976	3,513,704	16,184,017
Amounts owed to customers	43,716,441	20,963,221	6,500,127	9,633,616	9,633,616	8,679,379	99,126,400
Debt securities issued	–	–	–	–	–	2,356,254	2,356,254
Other liabilities	–	2,451,816	–	–	–	–	2,451,816
	43,811,159	25,808,892	7,251,665	13,331,384	15,393,592	14,623,977	120,220,669
Net position	(38,443,234)	(5,583,654)	895,431	2,419,804	357,596	43,656,864	3,302,807
Accumulated gap	(38,443,234)	(44,026,888)	(43,131,457)	(40,711,653)	(40,354,057)	3,302,807	

(Amounts in tables are in thousands of Kazakh Tenge)

30. Currency Analysis

The following table presents the KZT-equivalent amount of monetary assets and liabilities denominated in different currencies at December 31:

2002:	**KZT**	**Foreign currencies**	**Total**
Monetary assets:			
Cash and cash equivalents	**4,835,057**	**12,852,771**	**17,687,828**
Obligatory reserves	**4,525,381**	–	**4,525,381**
Trading securities	**16,357,771**	**7,149,211**	**23,506,982**
Investment securities	**4,374,523**	**4,391,748**	**8,766,271**
Commercial loans and advances, gross	**42,884,022**	**90,743,021**	**133,627,043**
Other monetary assets	**1,402,626**	**157,698**	**1,560,324**
	74,379,380	**115,294,449**	**189,673,829**
Monetary liabilities:			
Amounts owed to the government	**449,025**	**-**	**449,025**
Due to other banks and financial institutions	**351,750**	**31,755,160**	**32,106,910**
Amounts owed to customers	**53,836,291**	**81,547,082**	**135,383,373**
Debt securities issued	**-**	**4,468,713**	**4,468,713**
Dividends payable	**394,459**		**394,459**
Other liabilities	**2,292,578**		**2,292,578**
	57,324,103	**117,770,955**	**175,095,058**
Net position	**17,055,277**	**(2,476,506)**	**14,578,771**
2001:			
Monetary assets:			
Cash and cash equivalents	6,456,191	6,098,205	12,554,396
Obligatory reserves	4,662,961	–	4,662,961
Due from other banks	–	5,085,472	5,085,472
Trading securities	6,520,252	8,040,549	14,560,801
Commercial loans and advances, gross	33,740,790	50,513,767	84,254,557
Other monetary assets	2,041,889	363,401	2,405,290
	53,422,083	70,101,394	123,523,477
Monetary liabilities:			
Amounts owed to the government	84,932	17,250	102,182
Due to other banks and financial institutions	3,394,645	12,789,372	16,184,017
Amounts owed to customers	45,988,122	53,138,278	99,126,400
Debt securities issued	–	2,356,254	2,356,254
Other liabilities	1,911,861	539,955	2,451,816
	51,379,560	68,841,109	120,220,669
Net position	2,042,523	1,260,285	3,302,808

The above KZT denominated assets and liabilities include assets and liabilities, which are indexed to the US Dollar and revalued, based on changes of market rate as of December 31, 2002 and official NBK rate as of December 31, 2001 to reflect the effect of any change in the KZT against the US Dollar. At December 31, 2002 such assets amounted to KZT 2,926 million (2001: KZT 12,549 million) and such liabilities amounted to KZT 7,637 million (2001: KZT 24,923 million).

31. Financial Instruments

By its nature the Group's activities are principally related to the use of financial instruments. The Group accepts deposits from customers at fixed/floating rates and for various periods and seeks to earn above average interest margins by investing these funds in high quality assets. The Group seeks to increase these margins by consolidating short-term funds and lending for longer periods at higher rates while maintaining sufficient liquidity to meet all claims that might fall due.

The Group also seeks to raise its interest margins by obtaining above average margins, net of provisions, through lending to commercial and retail borrowers with a range of credit standings. Such exposures involve not just on-balance sheet loans and advances but the Group also enters into guarantees and other commitments such as letters of credit and performance, and other bonds.

Credit Risk

The Group takes on exposure to credit risk which is the risk that a counterparty will be unable to pay amounts in full when due. 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, limits on currency types, maturities, collateral types and to geographical and industry segments. Such risks are monitored on a revolving basis and subject to an annual or more frequent review. Limits on the level of credit risk by product, industry sector, and by country are approved quarterly by the Managing Board.

The exposure to any one borrower, including banks and brokers, is further restricted by sub-limits covering on and off-balance sheet exposures and daily delivery risk limits in relation to trading items such as forward foreign exchange contracts. Actual exposures against limits are monitored daily.

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

The Group maintains strict control limits on net open derivative positions, the difference between purchase and sale contracts, by both amount and term. At any one time the amount subject to credit risk is limited to the current fair value of instruments that are favorable to the Group (ie. assets), which in relation to derivatives is only a small fraction of the contract or notional values used to express the volume of instruments outstanding. This credit risk exposure is managed as part of the overall lending limits with customers, together with potential exposures from market movements. Collateral or other security is not usually obtained for credit risk exposures on these instruments, except where the group requires margin deposits from counterparties.

Market Risk

The Group takes on exposure to market risks. Market risks arise from open positions in interest rate and currency products, all of which are exposed to general and specific market movements. The Group manages market risk through periodic estimation of potential losses that could arise from adverse changes in market conditions and establishing and maintaining appropriate stop-loss limits and margin and collateral requirements.

(Amounts in tables are in thousands of Kazakh Tenge)

31. Financial Instruments (continued)

Currency Risk

The Group takes on exposure to the effects of fluctuations in the prevailing foreign currency exchange rates on its financial position and cash flows. The Managing Board sets limits on the level of exposure by currency and in total for overnight positions, which are monitored daily.

Note 29 analyses the assets and liabilities of the Group into relevant currency grouping.

Interest Rate Risk

Interest rate risk arises from the possibility that changes in interest rates will affect the value of the financial instruments. The Group is exposed to interest rate risk as a result of mismatches or gaps in the amounts of assets and liabilities and off balance sheet instruments that mature or reprice in a given period. The Group manages this risk by matching the repricing of assets and liabilities through risk management strategies.

The majority of the Group's assets and liabilities reprice within one year. Accordingly there is a limited exposure to interest rate risk.

The interest rates earned and incurred by the Group on its assets and liabilities are disclosed in the relevant notes to the consolidated financial statements.

Liquidity Risk

The Group is exposed to daily calls on its available cash resources from overnight deposits, current accounts, maturing deposits, loan draw downs, and guarantees. The Group does not maintain cash resources to meet all of these needs as experience shows that a minimum level of reinvestment of maturing funds can be predicted with a high level of certainty. The Board sets limits on the minimum proportion of maturing funds available to meet such calls and on the minimum level on interbank and other borrowing facilities that should be in place to cover withdrawals at unexpected levels of demand.

Note 28 analyses the assets and liabilities of the Group into relevant maturity groupings.

Fair Values of Financial Assets and Liabilities

The following table summarizes the carrying amounts and fair values of those financial assets and liabilities not presented on the Group's consolidated balance sheet at their fair value.

	Carrying Amount		**Fair Value**	
	2002	**2001**	**2002**	**2001**
Financial assets				
Commercial loans and advances	**132,459,847**	77,228,923	**111,624,636**	77,228,923
Financial liabilities				
Amounts owed to the Government	**449,025**	102,182	**375,826**	102,182
Due to other banks and financial institutions	**32,106,910**	16,184,017	**26,628,711**	16,184,017
Amounts owed to customers	**135,383,373**	97,875,976	**127,578,400**	97,875,976

(Amounts in tables are in thousands of Kazakh Tenge)

31. Financial Instruments (continued)

Fair Values of Financial Assets and Liabilities (continued)

Commercial loans and advances

Loans and advances are net of specific and other allowances for impairment. The estimated fair value of loans and advances represents the discounted amount of estimated future cash flows expected to be received. Expected cash flows are discounted at estimated current market rates to determine fair value.

Deposits and borrowings

The estimated fair value of deposits with no stated maturity, which includes non-interest-bearing deposits, is the amount repayable on demand.

The estimated fair value of fixed interest bearing deposits and other borrowings is based on discounted cash flows using interest rates for new debts with similar remaining maturity.

32. Capital Adequacy

To monitor the adequacy of its capital the Group uses ratios established by the Group for International Settlements (BIS). These ratios measure capital adequacy (minimum of 8% for Tier 1 + Tier 2 capital, and minimum of 4% for Tier 1 capital as required by BIS) by comparing the Group's eligible capital with its consolidated balance sheet assets, off-balance-sheet commitments and market and other risk positions at weighted amounts to reflect their relative risk.

The market risk approach covers the general market risk and the risk of open positions in currencies and debt and equity securities. Assets are weighted according to broad categories of notional risk, being assigned a risk weighting according to the amount of capital deemed to be necessary to support them. Four categories of risk weights (0%, 20%, 50%, 100%) are applied; for example cash and money market instruments have a zero risk weighting which means that no capital is required to support the holding of these assets. Property and equipment carries a 100% risk weighing, meaning that it must be supported by capital equal to 8% of the carrying amount.

Off-balance-sheet credit related commitments and forwards based derivative instruments are taken into account by applying different categories of conversion factors, designed to convert these items into balance sheet equivalents. The resulting equivalent amounts are then weighted for risk using the same percentages as for on-balance-sheet assets.

Tier 1 capital consists of shareholders' equity. Tier 2 capital includes the Group's subordinated long-term debt and the pooled allowance.

The Group's capital adequacy level was as follows:

	Balance Sheet Notional Amount		**Risk Weighted Amount**	
	2002	2001	**2002**	2001
Total risk-weighted assets	**241,149,011**	157,595,455	**193,894,879**	114,720,785

BIS Capital Ratios	**Capital**		**BIS%**	
	2002	2001	**2002**	2001
Tier 1 capital	**14,187,119**	6,903,023	**7%**	6%
Tier 2 capital	**5,998,656**	3,943,516	**3%**	3%
Gross available capital	**20,185,775**	10,846,539	**10%**	9%
Less investments	**(204,762)**	(177,506)	**-**	-
Tier 1 + Tier 2 capital	**19,981,013**	10,669,033	**10%**	9%