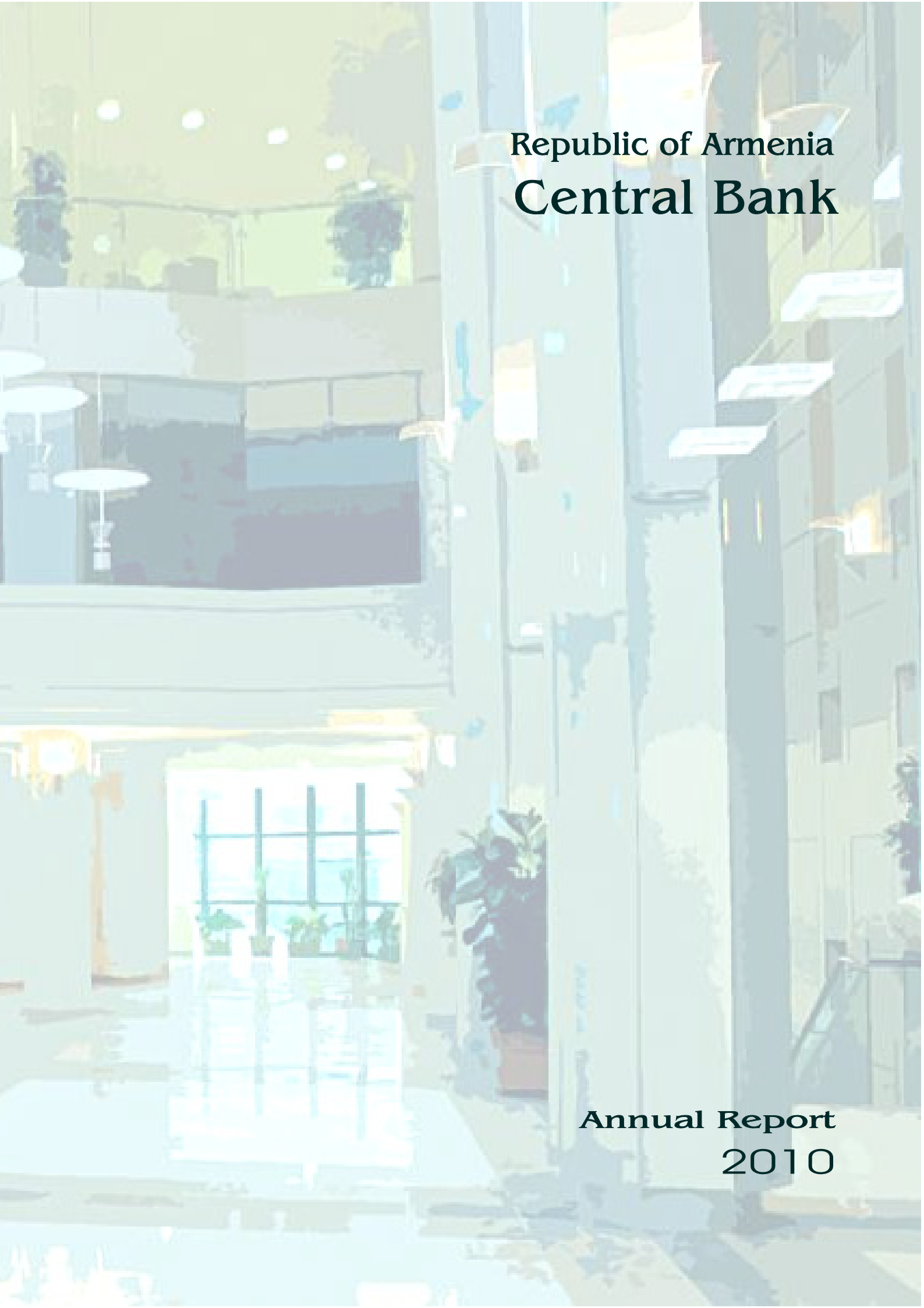

Central Bank of the
Republic of Armenia



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Republic of Armenia

Central Bank

Annual Report

2010



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CHAIRMAN'S MESSAGE

Dear Reader,

The year 2010 was full of challenges and trials but also prominent with achievements and structural reforms.

The world financial and economic crisis in the last two-three years was a test to many governments, central banks and even some renowned scientists in terms of making revision in their approaches and decisions, redefining priorities and goals which were set before them. Armenia's economy, too, could not stay immune to the fallouts of the crisis, and it learned the lessons from it. Strengths and weaknesses of the economy were cleared up, and one thing was certain that preventing negative influence of external shocks and maintaining sustainable growth and low inflation would not be possible without structural changes in the economy and significant productivity growth.

The consequences of the crisis also made themselves felt in implementing a macroeconomic policy in 2010. The anti-crisis measures developed in 2009 in cooperation with the Government helped the Central Bank mitigate, as much as possible, adverse consequences of the global economic downturn. Yet, early in the year, the Central Bank had to face another problem deriving from the crisis – high inflation – which has been predicted by many macroeconomic policy makers worldwide. The main factors determining the formation of an inflationary environment in our country included price increases in world markets as well as expansionary monetary and fiscal policies implemented in the previous year.

The tightening of monetary conditions and the de-dollarization measures since the beginning of the year made it possible to bring the 12-month inflation back to the target band in the first half of the year. Yet, the second half of the year saw new challenges associated, by and large, with steep rise in international prices of food products and a dramatic decline in agricultural output.

Though inflation was attributable to supply shocks, a reason beyond the Central Bank's aptitude, our efforts are continuously spent to cope with such shocks and prevent the importing of inflationary pressures to other segments of the market.

In charge of the development of the financial sector, the Central Bank further carried out a policy for a broader scope of financial market participants, more enhanced accessibility to financial services and diversity of products.

The launching of the compulsory third party motor liability insurance scheme was momentous for the year both in terms of having an insurance culture in place and further developing the financial sector in Armenia.

The passing of the package of laws pertinent to the pension system reforms was an important achievement as well. The voluntary pension component will be introduced since 2011 and the compulsory cumulative pension component, since 2014. These reforms are of great social significance and serve to maintain a proper level of living after retirement.

Work was further done to protect consumer interest as well as large-scale measures were taken up to increase awareness of target groups on financial and economic aspects.

The policy implemented was reflected in the developments of the financial sector. Financial markets bounced back to their pre-crisis levels: competitiveness in the financial sector has improved notably and interest rates of loans have fallen steadily. Nevertheless, much remains to be done for the overall growth of the system.

To sum-up, I would like to note that the year 2011 will also be going to face inflationary pressures and challenges, the Central Bank however will take action to bring inflation back to the target band. We will continue implementing reforms in pension and insurance sectors and in the securities market and non-bank financial institutions.



Chairman

ARTHUR JAVADYAN


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GOVERNANCE AND ACCOUNTABILITY

MISSION AND OBJECTIVES OF THE CENTRAL BANK

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

Objectives of the Central Bank include:

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

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

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

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

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

To achieve its objectives, the Central Bank:

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

b) acts as a lender of last resort;

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

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

e) manages international reserves of the Republic of Armenia;

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

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

Where the other objectives of the Central Bank contradict its primary objective, priority should be given to the ultimate goal of price stability while taking action to attain the aforementioned objective.

GOVERNANCE OF THE CENTRAL BANK

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

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

Chairman of the Central Bank is the highest rank official of the Central Bank. Chairman of the Central Bank is appointed by the Armenian National Assembly upon recommendation of President of the Republic of Armenia, for a 6-year term. Chairman is responsible for fulfillment of the Central Bank objectives. Chairman coordinates and organizes the work and ensures the soundness of activities of the Central Bank; represents the Central Bank in the Republic of Armenia, other states and international organizations; exercises authority not reserved to the competence of the Board. Where Chairman is absent or otherwise unable to act, such powers are to be vested with **Deputy Chairman of the Central Bank**, and where Deputy Chairman is absent or otherwise unable to act, such powers are to be vested with the eldest Board Member of the Central Bank. Deputy Chairman of the Central Bank is appointed by President of the Republic of Armenia, for a

6-year term. Chairman and Deputy Chairman as well as Board members cannot serve as a member of managing body of any party, be involved in activities other than scientific research, pedagogical and creative activities.

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

Board of the Central Bank

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

The Board also approves regular issues of the Central Bank publications as well as the operational administrative and capital investment estimate and annual financial accounts.

Over 2010, the Board has met 61 times and adopted 358 resolutions reflecting the discussion and approval of both conceptual papers on the Central Bank policy and principal activity and drafts to laws and prudential standards for the financial sector.



Board of the Central Bank
(left to right)

front row
- *Nerses Yeritsyan*
- *Arthur Javadyan*
- *Ashot Mkrtchyan*

back row
- *Andranik Norekyan*
- *Aharon Chilingaryan*
- *Vakhtang Abrahamyan*
- *Armenak Darbinyan*

The Board meetings are normally open to the respective field representatives who are invited to take part in the discussion of the issue concerned. For example, a representative of the Government or Ministry of Finance is invited to the discussion of refinancing rate, and representatives of professional unions (of banks, credit organizations, insurance companies, and etc) are invited to discuss issues relating to the financial system policy and engaged in preparation of such issues.

Commissions, committees and other consultative bodies are key pillars of the Central Bank governance, and their structure and competence are defined based on the scope of issues and area of activity. The commissions and committees of the Central Bank hold meetings and draw up minutes which are approved by Chairman of the Central Bank. Where appropriate, Chairman makes decisions and issues orders based on such minutes.

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



The Executive Board discusses items to be presented to the Board of the Central Bank

Executive Board of the Central Bank

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

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

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

Over 2010, the Executive Board has met 22 times.

THE CENTRAL BANK ACCOUNTABILITY

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

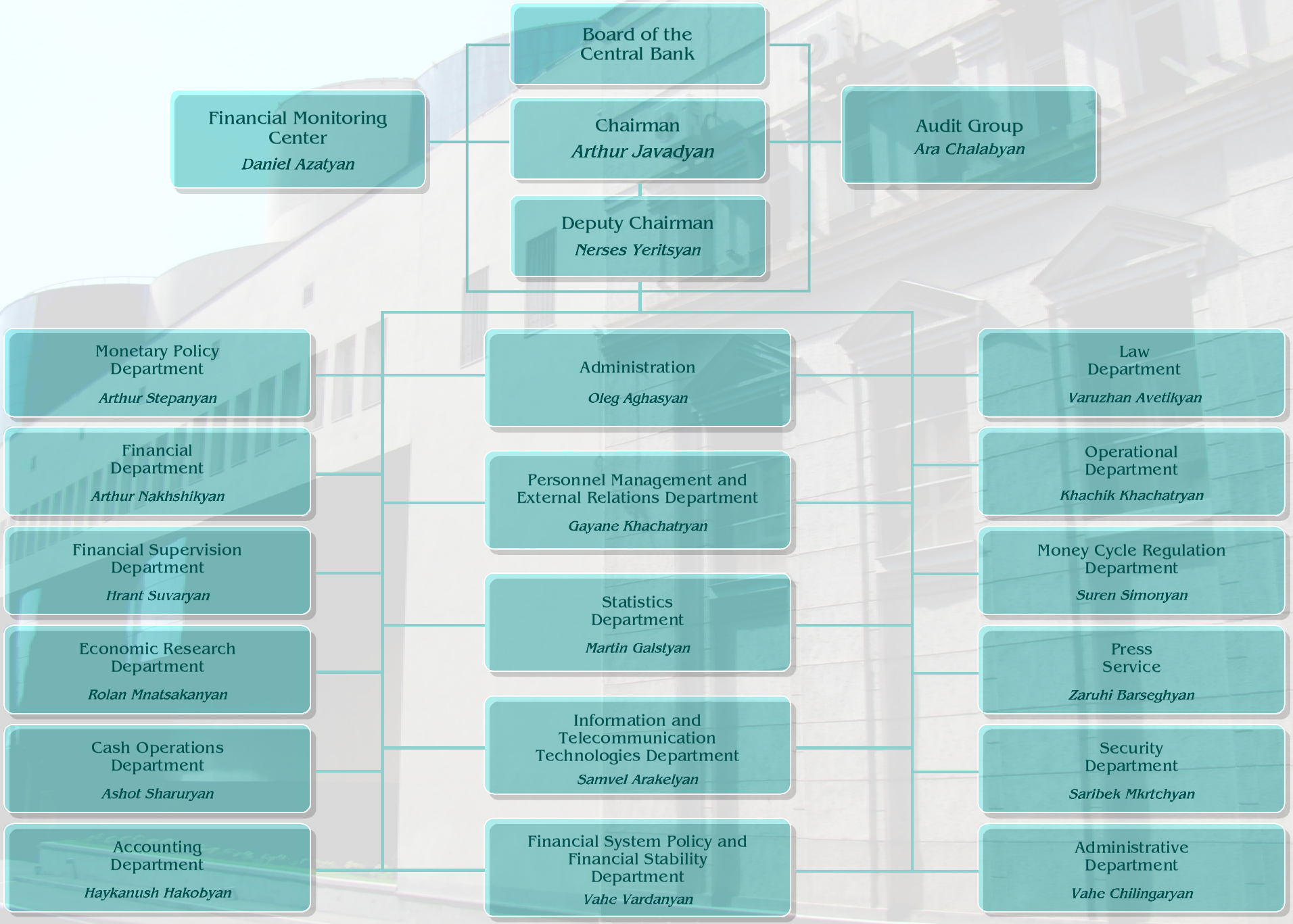
The Central Bank presents the *Monetary Policy Program* and *Status Report on Implementation of Monetary Policy (Inflation Report)* as well as *Expenditures Estimate and Capital Investment Program*, with performance papers, to the National Assembly of the Republic of Armenia.

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

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

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

THE CENTRAL BANK STRUCTURE



STRATEGIC DIRECTIONS

For 2010, the Central Bank prioritized the following objectives:

Maintaining enhanced transparency of the monetary policy; improving the forecasting and policy analyses system by studying the nature of inflation at its core. The central priority of the monetary policy implemented in 2010 was to develop and carry out such monetary and foreign exchange policy which will anchor public expectations in the face of high inflationary environment generated by supply shocks due to increased prices of food products in world markets on the one hand, and reported downfall in agriculture, on the other.

Increasing the stability of the financial system and the regulatory and supervisory framework; eliminating consequences of the crisis, stimulating the sustainable growth of the financial system by focusing on banking system indicators, the level of financial intermediation and development of the insurance and securities markets. Other priorities for 2010 included creating an infrastructure and sub-legislative framework to facilitate the introduction of the Republic of Armenia Law on Compulsory Insurance Against Civil Liability in Respect of the Use of Motor Vehicles and creating a framework for regulation and oversight of investment funds as part of implementation of pension reforms.

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

Improving the payment and settlement system; increasing non-cash payments and services and raising the level of safety and reliability of the payment systems; introducing mechanisms more suitable and state-of-the-art for the use of monetary policy

instruments (repo and reverse repo agreements); commissioning a new cash center of the Central Bank equipped with modern facilities to increase the cash service delivered to the clients.

Setting up a visitor center at the Central Bank in order to increase people's awareness of the Central Bank functions and operations as well as increase the level of financial literacy.

MONETARY POLICY

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

The measures to attain the inflation target set for 2010 (4 $\pm$ 1.5%) were outlined in the monetary policy programs, and its implementation, in the quarterly inflation reports.

The monetary policy implemented during 2010 was characterized by high inflationary environment, which was influenced by such factors as rise in international prices of food and primary goods amid economic recovery, expansionary fiscal and monetary policies implemented in 2009 and increase of gas and water tariffs since April 1 2010. In this situation, the Central Bank implemented a tightened monetary policy since January 2010, keeping on raising the refinancing rate in the first five

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

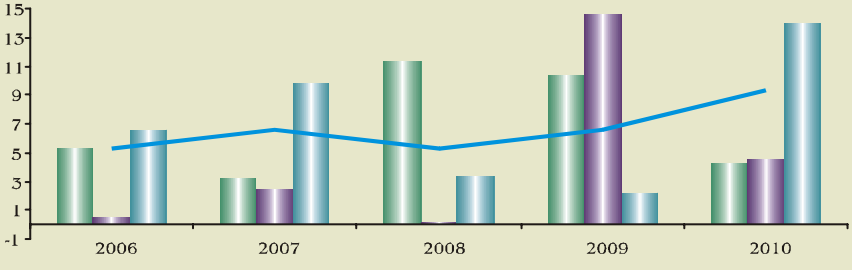


The Central Bank implemented a tightened monetary policy since January 2010.

months for a total of 2.5 pp, while taking on action to reduce dollarization. As a result of the policy implemented, the 12-month inflation of 9.4 percent recorded in February further declined and almost reached the upper border of the target tolerance band in June, making up 5.8 percent. The situation, however, changed drastically as new inflationary impulses driven primarily by supply-side factors appeared.

In the second half of the year inflation has intensified due to a sharp increase in international wheat price, followed by the price increases of food products as well as a reported deep decline in agriculture. As a result, inflation during 2010 was 9.4 percent, 7.5 pp of which alone was due to growth in food prices: the growth of domestic prices of agricultural goods contributed around 5 pp to inflation, and imported food, made over 2 pp of contribution. Average inflation recorded in the period January-December was 8.2 percent in relation to last year's average.

The aforementioned factors point to the fact that inflationary environment was solely due to supply factors, which are not subject to the monetary regulation. In this situation, despite the acceleration of inflation, the Central Bank avoided raising the refinancing rate because all assessments were showing that the slow pace of domestic demand recovery would not create inflationary pressures.

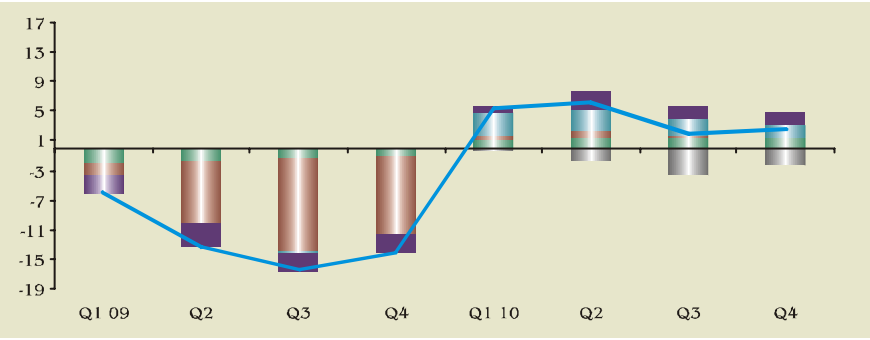


The 12-month inflation by main CPI commodity groups

Services *Non-food products* *Food products* *Headline inflation*

In the fourth quarter of the year, however, the Central Bank began conveying impulses to the economy that tightening the monetary conditions would most likely to happen if supply-side factors and their second round effects proved intensifying.

The year 2010 saw 2.6 percent economic growth, with industry and services having made the largest contribution to the growth. So, industry, services and construction reported growth of value added by 9.5 percent, 4.6 percent and 3.7 percent, respectively, whereas the downfall in agriculture amounted to 13.4 percent.



The Central Bank paid due attention to the research in implementing the monetary policy, the results of which were really instrumental in making decisions on the monetary policy. Research included reviewing developments at macro and micro levels and building models based thereon. These were widely used in monetary forecasts.

Economic research at the Central Bank in 2010 focused on the areas, as follows:

- further development of dynamic stochastic general equilibrium models; assessment of model parameters by the use of modern probability methods and software packages;
- assessment of accumulation of human capital in the Republic of Armenia; assessment of the impact of migration and migrants

making private remittances on the macroeconomic environment and long-term economic growth;

- development of dynamic factor models in order to make short-term forecasts of macroeconomic indicators; probability and econometric assessment of structural forecast models and making forecasts based thereon;
- modeling the development of the Armenian banking system through the import of rigidities existing in the financial system; modeling interbank market risks and formulating a policy to handle such risks;
- building macro-models that describe the labor market imperfections and studying potential impact of existing imperfections on the monetary policy and its channel of transmission.

To increase the effectiveness of research work, the Central Bank intends to expand the research staff, which will then serve a basis for an economic research and education center at the financial and banking complex which is under construction in Dilijan. In addition to economic research, the center is expected to house scientific and educational events through involvement of internationally prestigious scientific and financial institutions and well-known scientists.

MONETARY AND FINANCIAL STATISTICS

During 2010 the Central Bank carried out work to improve the field of statistics. Efforts included drafting a package of legislative amendments and approving the concept paper on Preparation of External Accounts, associated with the moving of the statistics of external accounts on to the Central Bank. A concept paper on Creation of Inflation Expectation Assessment Mechanism at the Central Bank was developed as well as work was done to create an information bank on motor liability insurance contracts.

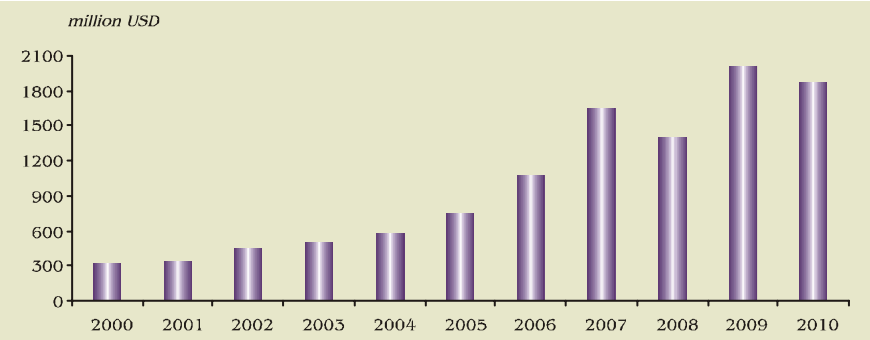
Relations with the rest of the world leave a material impact on domestic prices, aggregate demand, equilibrium in the foreign exchange market and other economic fundamentals. In this context, quality collection of statistics of external accounts while implementing monetary policy is important.

Another important aspect in external account statistics is the development of such statistics, namely the preparation of the statistics in compliance with BPM6 (Balance of Payments and International Investment Position Manual) and revision of historical series. The Central Bank also considers the introduction of the mechanisms of direct data collection from non-financial organizations along with the introduction of the international operations system. The statistics on monetary remittances is improved on an ongoing basis.

Highlighting the role of expectations of economic agents in building macroeconomic models and formulating and implementing monetary policy, the Central Bank will, starting 2011, assess inflation expectations of both households and financial and non-financial organizations. The mechanism of independent expert forecast will be improved further. At the same time, all other sample research will continue to be directed to a more accurate evaluation of the situation and expectations for various economic phenomena and existing problems.

INTERNATIONAL RESERVES MANAGEMENT

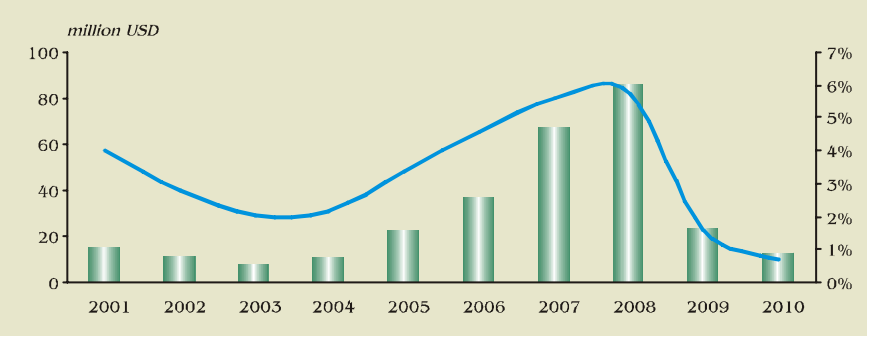
In 2010 international reserves have decreased by about USD 138.2 million in comparison with the previous year and reached USD 1865.5 million at the end of the year.



Armenia's international reserves

In the period under review average annual yield was 0.68 percent (1.61 percent in the previous year) and profit generated USD 12.4 million (USD 23.4 million in the previous year).

Average yield of Armenia's international reserves and generated profit have reduced considerably in relation to the previous year which is explained by overall change in economic and financial landscape.



Income (yield) from management of international reserves

Income Yield (right-hand scale)

Since 2009 interest rates were at low levels, attributable to both a low level of inflation and the US Federal Reserve System and European Central Bank policies to overcome the financial and economic crisis. In developed countries at the end of the year, interest rates tended to rise, which was determined by positive expectations of market participants and an anticipated lifting of monetary policy rates by the US Fed and the ECB during 2010.



Euro and US dollar treasury bills with 2-year maturity

2-year US dollar interest rate *2-year Euro interest rate*

Over 2010, a steadily low level of and lesser volatility in interest rates resulted in limited profitability on reserves and gains from active management. Because interest rates have been at a very low level for a relatively long period of time, bond coupon yields have also fallen compared to the year 2009. To sum up, when compared to the year 2009, returns in 2010 were lower in terms of both capital appreciation and coupon yield.

Reforms in the field of reserve management implemented during the last three years, namely expanded toolkit and advanced active management techniques made it possible to be flexible enough to respond to the European debt crisis of 2010.

The results of the end-year ex-post analyses suggest that the choice of durations and benchmarks for securities was fully justified, as portfolio benchmarks maintained the highest return to

risk ratios and had the best indicators in terms of frequency of positive yield, while symmetric volatility and VaR among other options were considered appropriate for investment by the Central Bank.

Investment Committee

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

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

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

Over 2010, the Investment Committee has met 9 times and made 5 decisions.



FINANCIAL STABILITY, REGULATION, SUPERVISION

The regulatory framework of the financial system[1] is revised and improved on an ongoing basis. In pursuit of consistent development of the banking, insurance and securities markets, a number of reform laws were passed at the National Assembly of the Republic of Armenia in 2010, as follows:[2]

1. The Republic of Armenia Law on Compulsory Insurance Against Civil Liability in Respect of the Use of Motor Vehicles, and relevant changes and supplements to other laws (endorsed in the second quarter of 2010).

The law establishes an obligation of compulsory insurance of the liability of motor vehicle owners and other persons legally possessing motor vehicles used on general purpose roads, arising out of the damage caused to third parties due to the use of the motor vehicles.



There are ongoing efforts to revise and improve the regulatory framework of the financial system.

[2] See details on the financial system in the Armenian Financial System: Development, Regulation and Development, 2010, and the Financial Stability Report, 2010, published by the Central Bank (www.cba.am).

The main goal of the law is the protection of rights of injured parties caused by the use of motor vehicles, particularly through the establishment of efficient mechanisms of damage compensation.

2. The Republic of Armenia Law on amendments and addenda to the law "On Guaranteeing Compensation of Bank Deposits of Individuals" (endorsed in the second quarter of 2010), whereby the guaranteed amount for dram deposits was increased to AMD 4 million, while the guaranteed amount for foreign exchange deposits was increased to AMD 2 million. The Central Bank, as sole founder of the Fund, was given authority to invest into the Fund an amount of up to AMD 5 billion. An amendment was endorsed also to the law "On the Central Bank of Armenia, whereby the Central Bank will be entitled to provide the Deposit Guarantee Fund with loans covered by budgetary guarantee, if at the time of compensation the financial stability (liquidity and/or solvency) of the financial system is undermined. At the same time, amendments to the law "On Budget System of Republic of Armenia" established that the Deposit Guarantee Fund receives budgetary guarantee according to Government decree without any collateral.



Both off-site and on-site inspections were carried out at financial organizations.

3. The Republic of Armenia Law on amendments and addenda to the laws "On Banks and Banking" and "On Joint Stock Companies" (endorsed in the second quarter of 2010). The purpose of these amendments was to give banks, which are joint stock companies, the right to delegate maintenance of their participants' register either to the Central Depository or to the professional company not affiliated to the bank, which is entitled to maintain register (custodians). At the same time, there was clarification made to a provision of the law whereby companies rendering investment services are neither authorized to maintain the register of their participants nor delegate the maintenance of the register to the affiliated custodians.

4. The Republic of Armenia Law on Investment Funds and relevant changes and supplements to other laws (endorsed on December 22, 2010).

5. The changes and amendments to the Republic of Armenia Law on Payment and Settlement Systems and Payment and Settlement Organizations (endorsed on the first hearing in October of 2010), which were aimed to: a) enhance stability and reliability of the financial system through establishing stricter requirements to licensing and oversight of payment and settlement organizations, and b) set a new minimum total capital requirement of AMD 100 million to payment and settlement organizations.

Types of payment and settlement services were given more clarification and the definitions thereof were further aligned with the EU legislative requirements; aspects of holding payment and settlement organizations liable were further regularized and the payment and settlement organizations were offered to use outsourcing services.

6. The changes and amendments to the Republic of Armenia Law on Securities Market and the Republic of Armenia Law on Credit Organizations (endorsed on the first hearing), which were aimed to delineate the scope and functions between investment

companies and credit organizations as the activity of these two segments seemed to have reported an overlap in the absence of distinguished tasks. According to the proposed change, credit organizations will no longer provide investment services except when dealing with securities transactions to their expense and on their behalf, and investment companies will not perform operations pertaining to credit organizations.

7. A draft law to the Republic of Armenia Law on Amendment to the Republic of Armenia Civil Code and other drafts pursuant thereto (endorsed on the second hearing in October of 2010). The main purpose is to eliminate some legislative drawbacks in order to enable legal persons involved in entrepreneurship to attract subordinate borrowings, since these borrowings are the most effective and quickest way to attract extra capital in comparison with, say, the replenishing of statutory capital.

8. In December of 2010, the Central Bank submitted drafts to the Republic of Armenia Law on Bankruptcy and the Republic of Armenia Law on Enforcement of Legal Proceedings to the Government. The proposed changes in the drafts refer to satisfying creditor claims, backed by pledge, surety and guaranty, in the bankruptcy process, without the moratorium in effect. This means that the financial organization or person in question has the right to satisfying its claim without having to wait for the completion of the bankruptcy process.

9. In the fourth quarter of 2010, the Central Bank submitted drafts to the Amendment to Republic of Armenia Law on Income Tax and the Amendment to Republic of Armenia Civil Code to the Government. These drafts were prepared to address a taxation aspect in confiscating the property as pledge. The drafts specify that where, in the event the pledge is marketed extra-judicially, the pledge involved becomes the property of the bank or credit organization, an obligation to pay the income tax shall be postponed until that bank or credit organization has sold the pledge to the third party. The postponement, however, shall not be longer than six months. For income tax calculation purposes, the

pledgor income is the positive amount of difference between selling price of collateral and credit liability.

In the light of the above legislative amendments as well as developments in real and financial sectors of the economy, the Central Bank also introduced some sub-legislative changes in 2010. Further work was done to oversee the financial sector and protect consumer interest.

Licensing and Supervision Committee

The Licensing and Supervision Committee is standing committee at the Central Bank, and is headed by chairman of the Central Bank. In LSC meetings, chairman will make decision or instruct accordingly based on a verbal or written conclusion. The LSC addresses issues on registration and/or licensing of financial system participants; hears the findings of examinations and recommendations in order to offer remedy to the weaknesses identified; gives an opinion on professional integrity of managers of financial organizations.

Over 2010, the Licensing and Supervision Committee has met 66 times.



There were both off-site and on-site inspections carried out at financial organizations. During 2010 the Central Bank carried out 380 on-site inspections, of which:

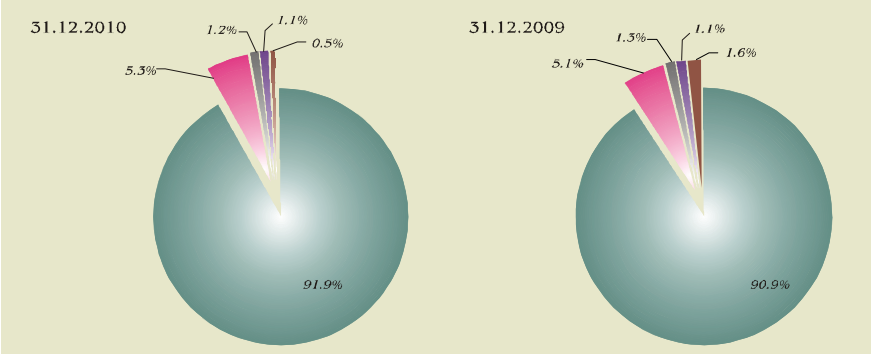
- 7 all-purpose inspections and 24 targeted inspections at banks
- 6 all-purpose inspections and 2 targeted inspections at credit organizations
- 3 all-purpose inspections and 8 targeted inspections at insurance companies
- 4 inspections at investment service providers
- 325 inspections at other financial system participants (exchange offices, pawnshops, payment and settlement organizations and etc.).

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

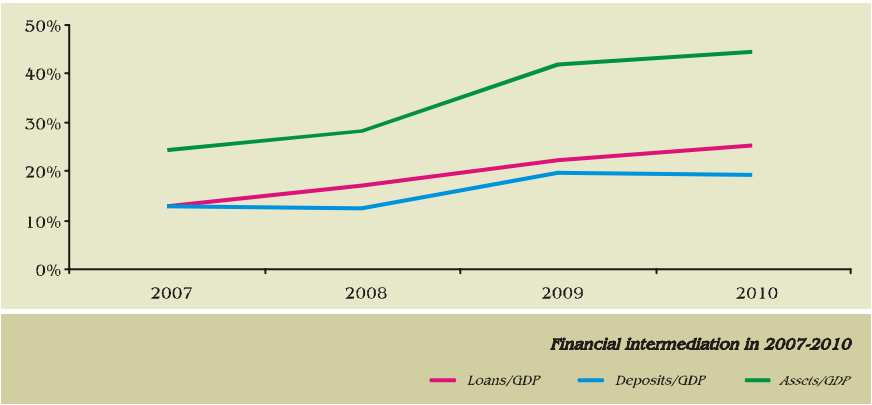
Large-scale awareness campaigns on protection of consumer interest and financial education of target segments of general public continued during 2010. Work was further done to develop a dedicated website "Finance for Everyone" (www.abcfinance.am) and explicate the scheme and use of mandatory motor liability insurance contracts; a guideline "On the Assessment Methodology of Financial and Economic Educational Programs" was developed for senior pupils; a program "On Continuous Delivery of General and Professional Knowledge and Information on Pension System in Armenia" was developed.

In 2010, the Armenian financial system showed highly flexible behavior and overcame crisis challenges of the previous year as lending market bounced back and pre-crisis level of profitability recovered.

The banking sector, the largest participant of the Armenian financial market, accounted for 91 percent of the financial system assets.



In 2010, the banking sector posted 17.7 percent growth of assets and 14.6 percent growth of capital. Return on assets was 2.2 percent and return on equity, 10.7 percent.



In 2010 the level of financial intermediation of the banking sector rose notably, yet it lags behind the same indicator reported for many CIS countries. Growth rate of the banking system assets quickened in relation to the nominal GDP growth rate, thus pushing the ratio of banking system assets to GDP up by 2.6 pp to reach 44.5 percent. The ratio of banking system loans to GDP rose by 3.3 pp and amounted to 25 percent.

Rating Committee

The Rating Committee is standing committee adjunct to chairman of the Central Bank and is set to consider the legal acts and methodology covering the credit rating field, and the ratings of individual companies. Over 2010, the Rating Committee has met 4 times during which decisions on granting credit rating to companies and introducing changes and supplements to the methodology were taken.

RATING OF COMMERCIAL ORGANIZATIONS

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

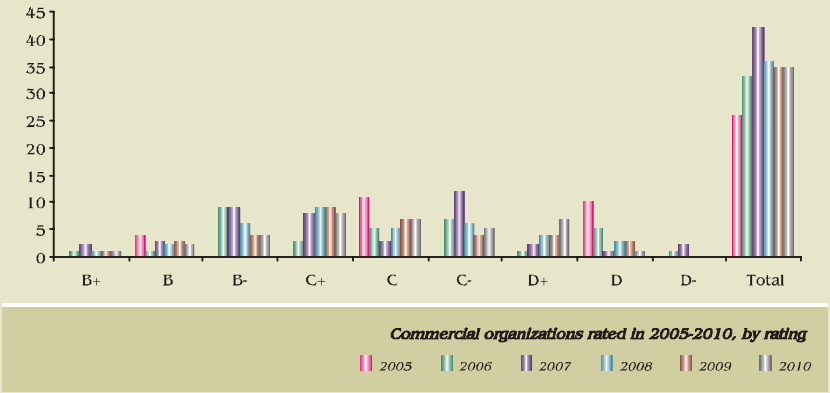
The Central Bank grants credit rating to commercial organizations in order to demonstrate their ability to service (repay) attracted liabilities in a timely manner and in full and provide objective and impartial evaluation of their credibility.

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

At the beginning of 2010, 35 organizations were granted rating. However, the number of rated organizations has not changed at the end of the process.[3]

In 2010 there was a change introduced to the rating methodology as a new component of evaluation of financial and economic performance of airlines was added to the methodology.

Credit ratings granted to 19 commercial organizations remained unchanged after these were re-rated; the ratings of 10 organizations were lowered and the ratings of 6 organizations were raised.



Commercial organizations rated in 2005-2010, by rating

As of yearend 2010, no organization was granted rating from category A. Seven organizations received rating from category B (7 in the previous year); twenty organizations received rating from category C (20 in the previous year); and the number of organizations which received rating from category D was 8 (8 in the previous year).

[3] *The complete list of rated commercial organizations is available on the Central Bank's website at http://www.cba.am.*

PAYMENT AND SETTLEMENT SYSTEM

In 2010, the Armenian payment and settlement system posted a number of positive developments. Work in the payment and settlement area was done in three main directions, pursuant to the Central Bank Development Vision:[4]

1. design, development and input of payment and settlement systems and procedures

2. development of non-cash payments, input of new payment instruments and operations

3. maintenance of payment and settlement system for sustainable development and improvement of legal framework for payment and settlement organizations.

Creating and developing an efficient payment and settlement system is one of key objectives of the Central Bank, according to Article 5 of the Republic of Armenia Law on the Central Bank. In pursuit of this objective, the Central Bank is responsible for regulation and oversight of the payment and settlement system and payment and settlement service providers.

1. During the year the Central Bank worked on creating a new payment system in order to facilitate the usage of the toolkit for a flexible monetary policy implementation.

   The main principles of the system are:

   - more convenient and fresh usage of monetary policy tools for executing repo / reverse repo transactions, and auctions
   - suitable and flexible mechanisms for managing banking system liquidity
   - possibility to execute operations not only with government bonds and the Central Bank securities but also with high-rated corporate securities.

The Central Bank regulates and oversees the activities of payment and settlement system and payment and settlement organizations.



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

To this end, a respective procedure of the exchange of messages was developed and introduced in cooperation with the Central Depositary.

The system will be operated by the Central Bank, with commercial banks operating in Armenia as the only participants of the system. Special accounts established with the Central Bank will be used for settlement needs.

The system will be operational since 2011.

The Armenian Card CJSC, a unified payments system, has a great role in making retail payments on a non-cash basis and thus contributes to the expansion of non-cash payments within Armenia.

In the year under review, driven by the need to meet contemporary trends in payment system management, the Armenian Card's management system has improved considerably thanks to the advice from McKinsey, a consultancy firm, bringing it in compliance with best international practice and current requirements. In 2010 the company realized a number of projects aimed at increasing the level of the system's information security, renewing the system of e-payments, membership to a new international payments system and revising the price policy in order to ensure the comprehensive development of the system in line with the progress of card system and international card payment requirements.

In 2010 the company started servicing AmEx cards, with ACBA-Credit Agricole Bank having acquired a full and exclusive service right.

In 2010 a new payment software of the website was launched for the system, which enabled an increased system capacity and operational continuity.

Starting from 2011, the company will be issuing DDA technology chip cards only. A new price policy was developed to

encourage member banks which are most active. Upgrading the software of the system is planned in the near future, which will be a solution to some key problems.

2. In 2010, 22 commercial banks and 11 payment and settlement organizations provided payment services. The value of non-cash payments executed via the banking system amounted to AMD 17 116 866 million.

It is noteworthy that the demand for financial services has increased in general. At the end of 2010, the accounts opened in the banking sector numbered 1 804 579. The issuance of payment cards has increased by 25.86 percent to amount to 729 298 cards. The value of operations executed with cards has increased by 30.4 percent to make up AMD 558 350 million and the number of transactions has increased by 27.6 percent (a total of 11 292 931 transactions).

The Central Bank works on developing ways to non-cash payments.

3. Further work was done to make pension payments via the banking sector and payment and settlement system on a non-cash basis, and the payment of pensions via bank accounts, as part of pension reforms.

The Board of the Central Bank approved Regulation 16/2 "Procedure and Terms for Issuance and Service (Turnover) of E-Money; and Requirements to Execution of E-Money Transactions" under the Board of the Central Bank Resolution No. 73-N on April 13, 2010. The regulation is aimed to regularize the issuance and circulation of and the transactions with e-money.

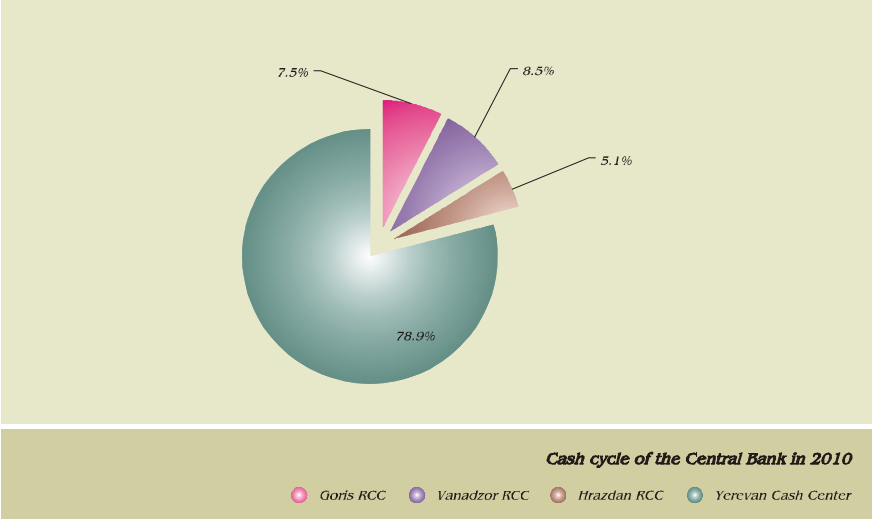
The Board of the Central Bank approved Regulation 16/1 "Procedure and Terms for Permitting, Suspending and Terminating Issuance of E-Money; and Requirements to Issuers of E-Money" under the Board of the Central Bank Resolution No. 74-N on April 13, 2010. The regulation is aimed to regularize the procedure of licensing to the organizations issuing e-money.

Work was further done to draft papers, such as "Rules of Creation of Guaranty Fund and Allocation and Use of Funds", "Clearing and Settlement of Transactions Net of Prior Depositing" and "Agreement on Guaranty Fund Participation".

Developing a sub-legislative framework is expected to follow once the law enters into force in 2011.

CASH MONEY CYCLE

In 2010, relative to 2009, the cash cycle of the Central Bank has increased by 8.3 percent and reached AMD 1200.8 billion. The Central Bank provided cash services to the clients through its central office as well as regional cash centers in Goris, Vanadzor and Hrazdan.



The regional cash centers accounted for 21 percent of the cash cycle of the Central Bank. In 2010, like in previous years, cash outflow remained the main operation carried out by RCC: cash outflow made up 92.1 percent of total RCC cash cycle.

During 2010 the Central Bank opened its new cash center which is equipped with state-of-the-art facilities for client service, cash processing and maintenance. Latest technologies for organizing flow of processes as well as automated systems and other conveniences are in place.

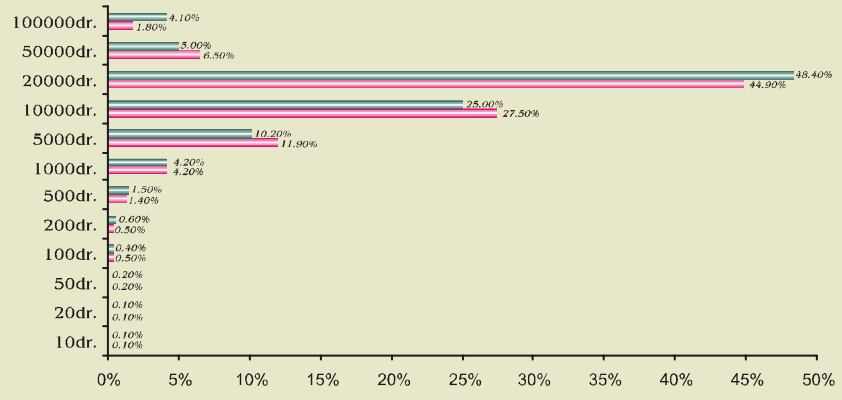
To improve cash service of its clients, the Central Bank continued efforts to further get its operations automated. During the year a new electronic system was in place that facilitates the circulation of documents between the Central Bank and the Ministry of Finance.

In 2010, currency outside the Central Bank grew by 8.6 percent. The cash cycle of notes and coins in selected nominal values changed.

In the type structure of currency outside the Central Bank in recent years, the share of banknotes with nominal value of 20000 drams kept on growing; at the end of 2010 the share of this nominal value in total has increased by 17.0 percent.

The volumes and shares of banknotes with nominal value of 10000 and 50000 drams in cash cycle further trended downward. It should be noted that in the period 2009-2010 the volume of the banknotes with nominal value of 50000 has halved. This was partly attributable to the introduction of the banknote with nominal value of 100000 drams. The volume of this nominal value amounted to AMD 14.2 billion at the end of 2010, representing a 2.4-fold increase relative to the previous yearend.

No essential changes occurred in the type structure of coins.



Type structure of cash outside the Central Bank, 2009-2010

2009 2010

During the year, the banknote with nominal value of 100000 drams earned prizes in the nomination "Banknote of the Year" in the framework of two contests organized by International Association of Currency Affairs and International Banknote Society.



In 2010, currency outside the Central Bank grew by 8.6 percent. The cash cycle of notes and coins in selected nominal values changed.

Financial System Stability and Development Priorities in 2011

- *The Central Bank will develop a concept paper on crisis management. The paper will define the policy goals for prevention and management of crises and main principles for taking up measures to economic recovery.*
- *Efforts to prepare for the introduction of the Basle III will continue and will include internationally accepted principles and requirements to maintain financial stability and prevent banking system risks, specifically in terms of improvement of corporate governance, management of liquidity and capital adequacy and such other risks.*
- *The Central Bank will design, in cooperation with the Government of Armenia, a concept paper for development of medical insurance in the Republic of Armenia. The paper will include the creation of a single electronic database on healthcare which is envisaged to become one of the key pillars in medical insurance in the future. In the meantime, work on raising the effectiveness of the use of mandatory motor liability insurance contracts will carry on.*
- *In 2011 the Central Bank will envisage designing a "hybrid payment system" which will enable commercial banks to manage their correspondent accounts more effectively.*
- *The Central Bank will be proactive in creating a sub-legislative framework for pension and investment funds. Due attention will be paid to maintaining fluent operation of investment funds, managers of investment funds and pension component on a voluntary basis. These measures are believed to largely contribute to the development of capital market in Armenia.*
- *In the context of protection of consumer interest and financial education of target audience, broad-range measures are expected in order to explicate the benefits of mandatory insurance and pension reforms. The World Bank is expected to perform an assessment of the system of protection of consumer interest in Armenia.*



COMBATING MONEY LAUNDERING AND TERRORISM FINANCING

The steps taken since the introduction of the anti-money laundering and combating terrorism financing system in the Republic of Armenia were aimed at improving the system and aligning it with internationally practiced criteria. To this end, the Financial Monitoring Center of the Central Bank of Armenia (hereinafter FMC), the national financial intelligence unit, has coordinated and implemented activities to achieve goals set forth in the 2010-2013 national strategy of combating ML/TF in the Republic of Armenia. Steps included, in particular, introducing legislation broadly complying with FATF recommendations, implementing risk-based principles of the mechanism for combating ML/TF, providing equal compliance with the requirements of anti-money laundering and combating terrorism financing legislation by all reporting entities (financial institutions, non-financial institutions and persons), the strengthening and expansion of cooperation at a domestic and international level.

In 2010, among other steps taken, a strategic analysis of ML/TF risk in Armenia was conducted. The results were introduced in the document entitled "Summary of Conducting a Strategic Analysis of Money Laundering and Terrorism Financing Risk in the Republic of Armenia"[3]. The results of the analysis suggest that potential risks of ML/TF in Armenia are concentrated mainly in the financial sector given the volumes of funds circulated, broad spectrum of financial transactions, the ability of running transnational operations, etc.

Legislative Developments in Combating ML/TF

The Republic of Armenia Law on Combating Money Laundering and Terrorism Financing (hereinafter Law) adopted in 2008 established requirements in compliance with international standards of combating ML/TF. However, the two-year application of the Law and the evaluations by international organizations has, nevertheless, revealed some weaknesses and gaps. Therefore, for the purpose of enhancing the mechanisms of combating ML/TF and having in place AML/CFT legislation broadly complying with international standards, the FMC, in collaboration with other

[3] *See details of risks to ML/TF in Armenia at http://www.cba.am/am/SitePages/fmcregulation.aspx.*

competent parties, drafted a package of amendments to the AML/CTF legislation. Having it agreed with all government departments concerned, the package was submitted to the Government of Armenia.

Besides, in 2010 the Board of the Central Bank adopted a number of methodic guidelines and typologies, and certain changes and supplements were made to other legal acts in the field of combating ML/TF.



The results of the analysis suggest that potential risks of ML/TF in Armenia are concentrated mainly in the financial sector.

ML/TF Analyses and Results

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

The table below presents statistics for the period of 2006-2010 regarding the referrals based on (i) the hypothesis on money laundering made to law enforcement bodies, (ii) the instigated cases and judicial hearing upon the referrals, and (iii) the seized and/or confiscated assets.

	2006	2007	2008	2009	2010	Total
FMC referrals to law enforcement bodies	2	11	11	9	23	56
Criminal cases instigated upon FMC referrals	2	2	2	1	5	12
Information requested from the FMC by law enforcement bodies	-	13	19	39	53	124
Criminal cases instigated at the initiative of law enforcement bodies	2	2	5	9	8	26
Criminal cases instigated, total	4	4	7	10	13	38
Sentences rendered	1	0	0	7	3	10
Funds suspended upon the Central Bank Board decision [5]			USD 802000	USD 1100000	AMD 345000, USD 290000	
Funds subject to confiscation to the budget upon court ruling (AMD)[6]	388000	0	0	53824860	514026500	

The process of analysis of the FMC often necessitates making additional inquiries to and receive information from reporting

[5] *The funds suspended in 2010 were entirely seized.*
[6] *Besides the funds subject to confiscation to the budget as shown in the table, in 2010 a claim of AMD 502240268 was satisfied to the benefit of a third party by a conviction rendered on a money laundering case.*

entities and national law enforcement and supervisory authorities and, when appropriate, foreign counterparts. It is worth mentioning that for the purpose of increasing the effectiveness and efficiency of cooperation between the FMC and national authorities steps were taken towards establishing a single information environment, as part of the Republic of Armenia Anti-Corruption Action Plan for 2009-2010. The single information environment will provide the relevant authorities with the opportunity to exchange information rapidly through secured channels, as well as make any available information accessible to each other.

International Cooperation

In 2010, the FMC staff members took part in plenary meetings of the Council of Europe's MONEYVAL Committee and the Eurasia Group, the joint plenary meeting of FATF and MENAFATF, the joint meeting of FATF and Egmont Group experts, the plenary and working group meetings of the Egmont Group as well as the meeting of the Conference of the Parties established under the Warsaw Convention, where they put forward the interests of the Republic of Armenia and brought their active participation in programs and initiatives of these institutions.

In the reported period, the approval of the Report on Armenia's Progress in the implementation of the recommendations made under the Third Round Evaluation Report of Armenia's Anti-Money Laundering and Combating Financing of Terrorism System by the MONEYVAL Committee was of great importance in the context of international cooperation. The report of the MONEYVAL Secretariat on the core recommendations included in the progress report indicates that a marked progress was recorded in the country.

In the reported period, the FMC signed memoranda of understanding with financial intelligence units of Iran, San Marino, and the Kingdom of Thailand. So, the FMC has agreements signed with FIU of 14 countries[7].

[7] *These countries are Australia, United Arab Emirates, Belarus, the Bermudas, the Kingdom of Thailand, Iran, Poland, Canada, South African Republic, Romania, Russia, San Marino, Georgia, and Ukraine.*

Training and Consultancy

In the year under review, seminars and courses were organized and held for both foreign counterparts and reporting entities.

In May 2010, the Iranian delegation, headed by the chief of the FIU of the Islamic Republic of Iran, visited the Republic of Armenia by the invitation of the FMC.

In November 2010, the delegation of the Financial Intelligence Department of the National Bank of Tajikistan, headed by the chairman of the Bank, visited the Republic of Armenia by invitation of the Central Bank of the Republic of Armenia. During the visit the chairmen of the central banks of the two countries discussed, inter alia, the aspects of cooperation and assistance between the two financial intelligence units as well as issues relating to the technical assistance presented to the FIU of Tajikistan by the FMC. The FMC also arranged seminar-discussions for foreign counterparts, covering legal, institutional, organizational and technical aspects of combating ML/TF.

Over the period April-May 2010, the FMC organized seminar-discussions for the employees of the internal monitoring units of banks, credit organizations, insurance companies and investment companies. As part of technical support provided to the FMC by the US Treasury, seminars were held in Yerevan over the period June-July 2010 with participation of the representatives of non-financial institutions, namely accounting and audit firms, lawyers, the Agency of State Registry of Legal Persons, the Central Depositary, State Committee of Real Estate Cadastre and realtor agencies, the staff members of the Ministry of Finance, employees of casinos and persons organizing lotteries, the representatives of customs and tax bodies of the State Revenue Committee under the Government of the Republic of Armenia.

MANAGEMENT AND ORGANIZATIONAL DEVELOPMENT

IMPROVING MANAGEMENT SYSTEMS

In 2010 there were further efforts to improving management system within the Central Bank. These included the input of the electronic document circulation system which now offers a faster and more effective way of dealing with documents with lesser administrative expenses and better tracking of management assignments.

In 2010 an electronic evaluation of work plans of structural units as well as individual programs and job performance of the staff of the Central Bank was designed and tested.

In the period under review, the Central Bank took measures to develop the Information Security management system and its alignment with international standards (ISO 27001:2005). The certification of the Central Bank's compliance with this standard is planned in 2011.

PERSONNEL MANAGEMENT

In 2010 the personnel policy of the Central Bank was aimed at fulfilling the main tasks and implementing the strategic program set before the Bank. This year too, appropriate resources were used to support professional development and lifelong training of the staff of the Central Bank. As of the end of 2010, the average number of staff of the Central Bank was 743 of which 420 women and 323 men. The average age of employees reached 37.

Professional Knowledge Evaluation Committee of the Central Bank

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

Job Evaluation Committee of the Central Bank

The task of the Committee for evaluation of jobs of the Central Bank is to evaluate and categorize new jobs or changed job positions.

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

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

Over 2010, the Committee has met 6 times.

Vacancies in the Central Bank were filled primarily by competition. During the year, 42 persons joined and 57 persons left the Central Bank.

The Central Bank remained committed to recruiting young specialists, improving qualification and making the best use of their potential. As before, young specialists were selected mostly out of those who had attended a curriculum titled *Central Bank of Armenia: Introductory Course*, which is organized by the "Finance and Banking College" Foundation. In 2010 functional units of the Central Bank employed 54 young specialists on terminal contracts, 15 of who joined the Central Bank.

During the year 61 students from higher academic institutions took their academic and pre-diploma internship in the Central Bank.

Improving Professional Qualification

During 2010 the Central Bank encouraged best students selected out of higher educational establishment of the Republic of Armenia and Nagorny-Karabakh by awarding 3 of them the Isahak Isahakyan Stipend.

Professional development of staff is an integral part of effective personnel management. During 2010 staff members of the Central Bank attended courses to increase professional and managerial skills and learn foreign language.

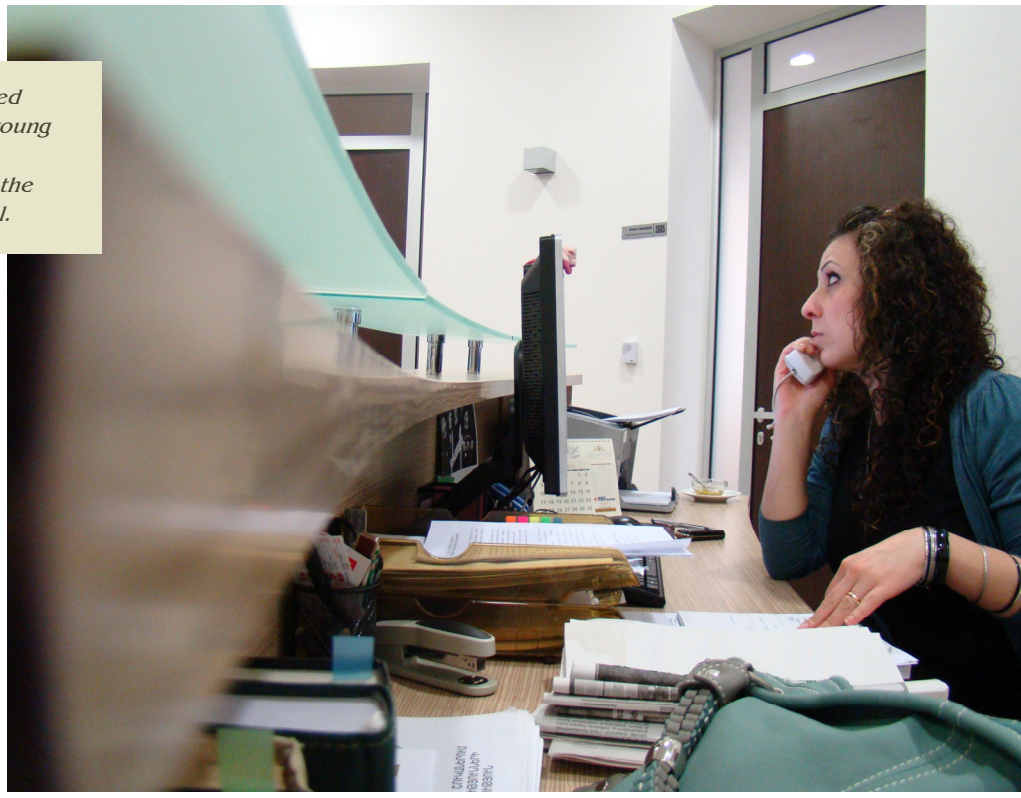
The training programs were organized both within the Central Bank and educational establishments in Armenia and abroad.

The Central Bank continued cooperation with partner central/national banks, the International Monetary Fund, Joint Vienna Institute, among others. During 2010 a total of 245 employees of the Central Bank participated in 162 seminars

abroad. Back from a business trip, employees are required to make account of the results of the training, the knowledge gained as well as to make recommendation on how these can be applied to their work.

Because filling up the gap of the knowledge necessary for performing strategic tasks is vital, the Central Bank has made arrangements with partner central/national banks for "tailor-made" courses within the framework of technical assistance. In 2010 the Central Bank initiated 35 "tailor-made" courses which involved 25 visits to other countries and 10 visits to our country. These courses allowed 238 staff members of the Central Bank to enhance their professional knowledge, in particular, in the field of insurance.

The Central Bank remained committed to recruiting young specialists, improving qualification and making the best use of their potential.



De Nederlandsche Bank (Bank of Netherlands) came in as the most active institution which the Central Bank cooperated with in the area of "tailor-made" courses. During 2010 the Bank has arranged 14 such courses 5 of which in the Republic of Armenia. The results of these courses are communicated in the meeting of Executive Board of the Central Bank and, where necessary, will be used by chairman of the Central Bank for further assignment.

In 2010, the Central Bank hosted two regional conferences: the first with the topic *Credit Risk Analysis* organized jointly with the US Federal Reserve System and the second titled *Crisis Preparedness* organized by the Toronto Center of Canada jointly with the World Bank. Regional attendance covered 40 people (29 participants and 11 experts) plus 26 staff members of the Central Bank. In 2010, the Central Bank continued cooperation with the States of the Eurasia Economic Community in the form of two workshops organized in the Republic of Armenia with an involvement of representatives of member states. The topics of the workshops were *Human Resource Management* and *Monetary Policy*. Mutual business visits for the exchange of experience continued.

Central Bank Staff Assessment Committee

The Committee on Central Bank staff assessment holds its meetings to assess the level of professional and business skills and knowledge of employees of the Central Bank or of persons (applicants) with their intention to work with the Central Bank.

The Committee can assess professional capacity and knowledge of the employees and applicants through both interview and tasks in writing.

Chairman of the Central Bank, who also chairs the Committee, will make a decision based on the conclusion issued by the Committee, determining whether:

- *the employee complies with professional capacities outlined in, and has knowledge appropriate to, the job occupied;*
- *a work contract can be signed with the applicant;*
- *an applicant can be promoted.*

Over 2010, the Committee has met 30 times.

In the period under review, 35 staff members of the Central Bank participated in distant training course (in a real-time regime) on bank and insurance supervision, organized by the Financial Stability Institute. Further, 35 staff members of the Central Bank successfully took exams for international professional qualification in finance, accounting, insurance, and information technologies, and were encouraged accordingly.

Stressing the importance of developing administrative skills of management and employees with a great potential, the Central

Bank organized seminars with the following topics: *Leadership: Resource Mobilization* and *Development of Administrative Skills*.

Staff members of the Central Bank took their active participation in local training courses organized by a great variety of educational establishments in the Republic of Armenia. A total of 76 employees participated in 16 training courses, 46 of which attended the courses of English language.

INTERNATIONAL COOPERATION

In 2010, the Central Bank sustained its multilateral and bilateral cooperation with international organizations and institutions of other countries.

In the period under review, the Central Bank received the International Monetary Fund missions in such areas as banking supervision, financial operations, monetary policy and statistics, as part of the IMF and WB Technical Assistance.

Staff members of the Central Bank attended a great variety of events – annual meetings, forums, international conferences on banking and finance, roundtable meetings, consultations and exhibitions where they made presentations and reports.

In the period under review, the Central Bank received, among others, experts of the IMF mission on statistics in order to strengthen business ties and negotiate on the matter; experts of the GDV, the German insurance association; a group of IMF experts in the framework of technical assistance in the field of fight against money laundering and terrorism financing; a delegation from Islamic Republic of Iran on issues of combating money laundering and terrorism financing; a delegation of the National Bank of Tajikistan, headed by Mr. Sharif Rakhimzoda, chairman of the National Bank; a delegation of the Black Sea Trade and Development Bank, headed by Mr. Andrey Kondakov, president of BSTDB.

In the period under review, the Central Bank arranged a number of meetings, workshops and a conference, including, in particular, an international conference with the following topic *Institute of Financial Ombudsman: Enhancing Public Confidence and Strengthening Financial Intermediation*, jointly organized by the Office of Financial System Mediator of the Republic of Armenia and the Central Bank of the Republic of Armenia (April 7-10 2010, Yerevan).

During 2010, new agreements and memoranda of understating were signed with central banks within the framework of intergovernmental committees.

PUBLIC RELATIONS

In the area of public relations in 2010, the Central Bank appeared with some important undertakings aimed to increase public awareness of new tools in the financial market and its development as a whole. Work was done by the Press Service of the Central Bank to enhance public awareness, including explication of the scheme and use of mandatory motor liability insurance contracts. Popular brochures and booklets were designed, press-conferences organized, educational and informative TV clips developed to explain to the public the said scheme and the use of the insurance contracts. The Central Bank described the use of these contracts through such TV programs as *Perspective*, *Eyewitness*, *Formula*, and *Auto-parade.* Further, 4 TV channels and 6 radio channels were used for advertisement broadcast.

In explicating the scheme and the use of mandatory motor liability insurance contracts, the Central Bank supported the "Bureau of Car Insurers of Armenia", a newly established union of legal persons.

Large-scale awareness campaigns on the activities of the Central Bank as well as financial education of target segments of general public continued during 2010.

In the framework of awareness and educational campaigns, the Central Bank further cooperated with the Union of Armenian Banks, Union of Mortgage Market Participants of Armenia, Association of Insurers and Consumer Interest Protection Organization.

The Central Bank regularly organized meetings with heads of organizations functioning in the financial sector; appeared with explanation of its actions, projects and legislative initiatives in the area of monetary policy, financial supervision and maintenance of financial stability. The next quarter's monetary policy program and steps in implementation of the program were presented to bank managers as well as relevant press releases were communicated.

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

In 2010 the Press Service of the Central Bank organized 14 press-conferences; responded comprehensively to 38 written and verbal queries of reporters; issued 171 press-releases explaining the Central Bank's activities, 47 press-releases about meetings of the Board, and 24 press-releases about interest rate of Repo Operations.

In 2010, the Central Bank made a film titled "Human Capital" which describes work life of Mr. Isahak Isahakyan, the first chairman of the Central Bank.

A video-film presenting the banknote with nominal value of 100000 drams was released during the year.

Another short video-film was made about Armenia which is intended for an international cast.

Work was further done to design and furnish the Visitor Center of the Central Bank; the displays were made ready for final application; work was done to design and update the website of the Central Bank.

During 2010, in-tour visits to the Central Bank were arranged for high graders of schools of Yerevan and regions of Armenia. As part of such tours, pupils were explained of the Central Bank's objectives and functions. They also listened to the history of money and the Dram as well as watched a video material. A total of 3365 pupils and students and 139 accompanying teachers took part in these in-tour visits.

In Shirak region of Armenia, the Central Bank organized, from October 12 through October 22, 2010 an exhibition titled 'History of Money Circulation in Armenia' in cooperation with Peoples'

Architectural and Municipal Life Museum of the city of Gumry. Nearly 2000 people (pupils, teachers and people of other professions) attended the exhibition.

From November 15 through November 27, 2010, in cooperation with the Finance and Banking College, the Central Bank organized in Ashtarak, Armenia, an educational seminar titled 'Economics: Theory and Application' for the teachers of *Economics* in schools of general education. A total of 13 teachers attended the seminar.

RISK MANAGEMENT AND AUDIT

INTERNAL CONTROL

Internal control is an ongoing (continued) process which involves financial and other types of monitoring functions. Internal control is conducted by the Board, heads of structural units and other competent staff of the Central Bank to make sure that:

- goals and objectives of the Bank are fulfilled,
- existing resources are used with care and effectively,
- an appropriate control over various types of risks and maintenance of assets is in place,
- financial information presented to the management of the Bank as well as information subject to public disclosure is complete and accurate,
- activities of the Bank are in compliance with the current legislation as well as the Bank's policies, internal rules and procedures.

During 2010 work was further done to identify, evaluate and classify risks existing in the functions of structural units of the Bank, and relevant efforts were spent by internal controllers and structural units to reduce such risks. Work done by internal controllers was reported to the chairman of the Bank on semi-annual and annual bases.



Internal control is an ongoing (continued) process which involves financial and other types of monitoring functions.

Plans for 2011 include studying the effectiveness of the internal control mechanism and providing solution to further development of that mechanism.

In November of 2010, the Board of the Central Bank approved the Business Continuity Policy within the Bank. The approval of the policy virtually is the first and most important step in implementation of the business continuity process management. The BCP introduction makes it possible to reduce or lessen the threats and consequences thus giving the staff of the Central Bank a sense of comfort and security and, further on, contributing to the financial stability. In addition, the BCP introduction will promote more effective and flexible organization of the business processes within the Central Bank.

The list of key business processes of BCP and the schedule of work to introduce the system are in place.

INTERNAL AUDIT

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

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

In 2010, Audit Group carried out examinations, target and regular, based on the annual audit plan approved by the Board of the Central Bank, to evaluate the effectiveness of risk management, control, and governance processes within the Central Bank as well as to offer possible solution to increased effectiveness.



Examinations carried out offered possible solution to increased risk management, control and governance.

There has been an adequate assurance reached with regard to the evaluation that:

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

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

Audit Committee

The Audit Committee of the Central Bank is one of key components of the Bank's governance. Responsibilities of the Committee include issues and tasks pertinent to financial accounts of the Bank, internal control, external and internal audit.

The Committee consists of three members, including chairman of the Committee. Members of the Committee are board members of the Central Bank.

Over the year, the Committee has met 6 times and during the meetings discussions were held and decisions made in respect of 27 issues. The discussion of issues covered examinations of Audit Group, external audit, internal control and risk management system as well as day-to-day activities of the Group and area-specific issues.

During the year, Audit Group continued actively cooperating with partner central banks (German Bundesbank, Bank of Lithuania, De Nederlandsche Bank) and the International Monetary Fund.

Some changes in personnel took place in the structure of Audit Group in 2010. Specialists of internal audit as well as other professionals with international qualification in accountancy and audit were invited to join the Group.

Republic of Armenia

Central Bank

Annual Financial Statements

2010

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Financial Statements and Independent Auditor's Report
Central Bank of the Republic of Armenia
31 December 2010

INDEPENDENT AUDITOR'S REPORT

To the Board of the Central Bank of the Republic of Armenia:

We have audited the accompanying financial statements of Central Bank of the Republic of Armenia (the "Bank"), which comprise the statement of financial position as at December 31, 2010, and the statement of comprehensive income, statement of changes in equity and statement of cash flows for the year then ended, and a summary of significant accounting policies and other explanatory notes.

Management's responsibility for the financial statements

Management is responsible for the preparation and fair presentation of these 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 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.

Auditor's responsibility

Our responsibility is to express an opinion on these 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 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 auditor's 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 Bank'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 Bank's internal control.

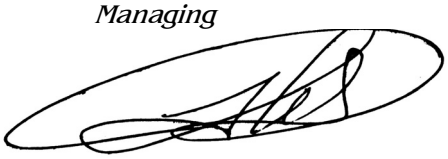
An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

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

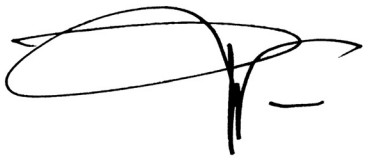
Opinion

In our opinion, the financial statements give a true and fair view of the financial position of the Bank as of December 31, 2010, and of its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards.

Gagik Gyulbudaghyan
Managing



Daniel Hilaire
Head of audit/partner



Grant Thornton CJSC 01
April, 2011
Yerevan

Grant Thornton CJSC
8/1 Vagharshyan Str.
0012 Yerevan, Armenia
T +374 10 260 964
F +374 10 260 961
www.gta.am

Central Bank of the Republic of Armenia

Statement of comprehensive income

AMD thousand

	Note	Year ended December 31, 2010	Year ended December 31, 2009
Interest income	4	9,534,614	8,862,492
Interest expense	5	(16,652,276)	(13,475,140)
Net interest expense		**(7,117,662)**	**(4,612,648)**
Fee and commission income		61,399	116,562
Fee and commission expense		(438,138)	(400,522)
Net fee and commission expense		**(376,739)**	**(283,960)**
Net foreign exchange gain/(loss)	6	(11,962,463)	36,575,523
Net realized gain/(loss) on available-for-sale assets		(21,168)	33
Net gain on financial instruments at fair value through profit or loss	7	2,943,175	5,652,878
Other income	8	1,901,653	709,679
Costs of production of banknotes, coins and numismatics	9	(226,802)	(1,236,314)
Other expenses	10	(13,061,942)	(6,823,054)
Profit/(loss) for the year		**(27,921,948)**	**29,982,137**
Other comprehensive income			
Net unrealized loss from changes in fair value		(600,218)	(1,250,645)
Net losses realized to comp. income statement on disposal of available-for-sale instruments		385,558	-
Total comprehensive income for the year		**(28,136,608)**	**28,731,492**

The statement of comprehensive income is to be read in conjunction with the accompanying notes which are integral part of the financial statements.

Central Bank of the Republic of Armenia

Statement of financial position

AMD thousand

	Note	As of December 31, 2010	As of December 31, 2009
ASSETS			
Foreign currency assets			
Cash		7,552,047	7,776,292
Placements with banks and other financial institutions	11	158,102,101	221,678,070
Financial instruments at fair value through profit or loss	12	404,632,917	459,234,675
Available-for-sale assets	13	917	917
Held-to-maturity assets	13	95,678,521	25,171,087
Placements with the IMF	14	63,670,237	101,621,324
Other assets		874,492	666,956
		730,511,232	816,149,321
Domestic currency assets			
Loans and reverse repurchase agreements	15	70,615,499	70,735,139
Available-for-sale assets	13	88,705,765	121,204,193
Held-to-maturity assets	13	4,132,916	3,862,867
Property and equipment	16	26,312,189	15,762,787
Intangible assets	17	583,179	427,907
Other assets	18	3,752,261	2,451,325
		194,101,809	**214,444,218**
Total Assets		**924,613,041**	**1,030,593,539**
LIABILITIES AND EQUITY			
Foreign currency liabilities			
Deposits and balances from financial and other institutions	19	99,650,034	150,616,174
Due to the Government of the Republic of Armenia	22	3,989,112	1,329,188
Financial instruments at fair value through profit or loss		19,478	36,588
Due to IMF	14	82,284,509	92,263,527
Other borrowed funds	20	27,599,809	28,309,397
Other liabilities		146,096	206,504
		213,689,038	275,761,378

The statement of financial position is to be read in conjunction with the accompanying notes which are integral part of the financial statements.

	Note	As of December 31, 2010	As of December 31, 2009
Domestic currency liabilities			
Notes and coins in circulation		348,164,734	320,669,631
Deposits and balances from financial and other institutions	19	80,825,771	53,204,221
Due to the Government of the Republic of Armenia	22	106,545,573	177,194,796
Due to IMF	14	195,802,721	172,556,583
Other liabilities	21	1,353,894	853,302
		732,692,693	724,478,533
Total Liabilities		**946,381,731**	**1,000,239,911**
Equity			
Issued capital	23	100,000	100,000
General reserve	23	17,389,049	11,392,622
Additional paid in capital	13	85,663,194	85,663,194
Revaluation reserve for available-for-sale assets		(1,628,760)	(1,414,100)
Accumulated losses		(123,292,173)	(65,388,088)
Total equity		**(21,768,690)**	**30,353,62**
Total liabilities and capital		**924,613,041**	**1,030,593,539**

The financial statements from pages 64 to 114 were approved by the Board of the Central Bank of the Republic of Armenia on 1 April 2011 and were signed on its behalf by:

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

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

The statement of financial position is to be read in conjunction with the accompanying notes which are integral part of the financial statements.

Central Bank of the Republic of Armenia

Statement of changes in equity

AMD thousand

	Issued capita	General reserve	Additional paid in capital	Revaluation reserve for available-for-sale assets	Accumulated losses	Total equity
Balance as of January 1, 2009	**100,000**	**9,870,486**	**85,663,194**	**(163,455)**	**(87,814,615)**	**7,655,610**
Distribution to general reserve	-	1,522,136	-	-	(1,522,136)	-
Distribution to the Government of the Republic of Armenia	-	-	-	-	(6,033,474)	(6,033,474)
		1,522,136	-	-	(7,555,610)	(6,033,474)
Profit for the year	-	-	-	-	29,982,137	29,982,137
Other comprehensive income						
Net unrealized loss from changes in fair value	-	-	-	(1,250,645)	-	(1,250,645)
Total comprehensive income for the year	-	-	-	(1,250,645)	29,982,137	28,731,492
Balance as of December 31, 2009	**100,000**	**11,392,622**	**85,663,194**	**(1,414,100)**	**(65,388,088)**	**30,353,628**
Distribution to general reserve	-	5,996,427	-	-	(5,996,427)	-
Distribution to the Government of the Republic of Armenia	-	-	-	-	(23,985,710)	(23,985,710)
		5,996,427			(29,982,137)	(23,985,710)
Loss for the year	-	-	-	-	(27,921,948)	(27,921,948)
Other comprehensive income						
Net unrealized loss from changes in fair value	-	-	-	(600,218)	-	(600,218)
Net losses realized to comp. income statement on disposal of available-for-sale instruments	-	-	-	385,558	-	385,558
Total comprehensive income for the year	-	-	-	(214,660)	(27,921,948)	(28,136,608)
Balance as of December 31, 2010	**100,000**	**17,389,049**	**85,663,194**	**(1,628,760)**	**(123,292,173)**	**(21,768,690)**

Central Bank of the Republic of Armenia

Statement of cash flows

AMD thousand

	Note	Year ended December 31, 2010	Year ended December 31, 2009
CASH FLOWS FROM OPERATING ACTIVITIES			
Profit/(loss) for the year		(27,921,948)	29,982,137
Depreciation and amortization		731,035	437,166
Loss from disposal of PPE		5,302	21,819
Interests receivable		577,853	257,752
Interests payable		657,448	(1,386,963)
Net (gains)/losses from revaluation of monetary assets and liabilities		12,099,588	(22,597,494)
Net loss from remeasurement of financial instruments at fair value		1,939,306	986,939
Other		(32)	4,662
Cash flows from operating activities before changes in operating assets and liabilities		(11,911,448)	7,706,018
(Increase)/decrease in operating assets			
Placements with banks and other financial institutions		882,671	(5,913,005)
Financial instruments at fair value through profit or loss		26,185,644	(105,152,819)
Placements with the IMF		23,797	(131,830)
Available-for-sale assets		8,298,058	(31,438,018)
Held-to-maturity assets		(67,685,078)	(30,139,431)
Loans and reverse repurchase agreements		(30,946)	9,990,494
Other assets		(1,421,373)	(710,326)
Increase/(decrease) in operating liabilities			
Notes and coins in circulation		27,495,103	(23,833,600)
Deposits and balances from financial and other institutions		(16,270,879)	68,023,915
Due to IMF		33,178,784	97,095,654
Due to the Government of the Republic of Armenia		(68,085,395)	74,023,577
Debt securities issued		-	(1,437,498)
Other liabilities		190,940	(5,526,135)
Net cash from/(used in) operating activities		**(69,150,121)**	**52,556,996**
CASH FLOWS FROM INVESTING ACTIVITIES			
Purchase of property, equipment and intangible assets		(11,446,498)	(6,018,475)
Proceeds from sale of property and equipment		5,487	3,340
Net cash used in investing activities		(11,441,011)	(6,015,135)

CASH FLOWS FROM FINANCING ACTIVITIES			
Loans received/ (redeemed) from KFW		1,765,734	11,986,838
Loans received/ (redeemed) from IMF		(7,742,999)	45,291,623
Net cash from/(used in) financing activities		**(5,977,265)**	**57,278,461**
Net increase/(decrease) in cash and cash equivalents		**(86,568,397)**	**103,820,322**
Cash and cash equivalents at the beginning of the year		236,032,987	63,679,345
Exchange differences on cash and cash equivalents		(9,967,062)	68,533,320
Cash and cash equivalents at the end of the year	26	**139,497,528**	**236,032,987**
Supplementary information			
Interest received		8,956,761	8,604,741
Interest paid		(17,309,724)	(14,862,104)

Accompanying notes to the financial statements

1. Background

Principal activities

The Central Bank of the Republic of Armenia (the "Bank") is a legal entity established by the act of the National Assembly of the Republic of Armenia.

The registered address of the Bank is 6 Vazgen Sargsyan Street, Yerevan 0010, Republic of Armenia. The average number of employees of the Bank during 2010 was 728 (2009: 681).

The primary objective of the Bank is price stability in the Republic of Armenia. It is achieved through formulation and implementation of monetary policy. In addition to its primary objective, the Bank is also responsible for:

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

The Bank also:

- issues the national currency of the Republic of Armenia and regulates its circulation;
- organizes and regulates anti money laundering and terrorism financing activities;
- is the fiscal agent and financial consultant of the Government of Republic of Armenia;
- licenses commercial banks and, if so provided by law, other entities, supervises and regulates their activities;
- is the lender of last resort to commercial banks; and,
- possesses, uses and administers international reserves of the Republic of Armenia.

The Bank's subsidiaries are as follows:

Name	Country of incorporation	Principal activity	Controlled %		Date of establishment
			2010	2009	
"Armenian Card" CJSC	Republic of Armenia	Payment and settlement services	66	66	March 2000
"ArmCollection" CJSC	Republic of Armenia	Transportation/delivery of cash	100	100	April 1998
All-Armenian bank	Republic of Armenia	Banking activity	100	100	December 2009
"National mortgage company" UCO CJSC	Republic of Armenia	Mortgage activity	100	100	June 2009
"Home for youth" UCO CJSC	Republic of Armenia	Lending activity	100	-	February 2010
"Small and medium business credit support" CJSC	Republic of Armenia	Lending support	100	-	December 2010

The Bank has also made investments in "Deposit guarantee fund", which was founded by the RA CB decision made on February 4, 2005.

The fund is a non profit legal entity with the purpose of ensuring the stability and reliability of the Banking system of the Republic of Armenia through the guarantee of remuneration of deposits of physical entities and lindividuals.

Bank's action to ensure financial stability

The Bank has an important role in making the effects of the world financial crisis more manageable for the Armenian economy by having a fundamental task and responsibility of maintaining and promoting the stability of the financial system in Armenia. In order to achieve this, the Bank strives to prevent undesirable impacts of the crisis using all the financial instruments at its disposal.

Taking into account the high capitalization and liquidity levels in the Armenian banking system, on 3 March 2009 the Bank of has decided to limit its interventions in the foreign exchange market and to return to floating exchange rate policy. This approach will allow the exchange rates to be formed in line with the current macroeconomic indices, which will considerably improve the external competitiveness of Armenia.

2. Basis of preparation

2.1. Statement of compliance

The accompanying financial statements have been prepared in accordance with International Financial Reporting Standards ("IFRS"), as developed and published by the International Accounting Standards Board (IASB), and Interpretations issued by the International Financial Reporting Interpretations Committee ("IFRIC").

2.2. Basis of measurement

The financial statements have been prepared on a fair value basis for financial assets and liabilities at fair value through profit or loss and available-for-sale assets, except those for which a reliable measure of fair value is not available. Other financial assets and liabilities are stated at amortized cost and non-financial assets and liabilities are stated at historical cost.

2.3. Functional and presentation currency

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

2.4. Use of estimates and judgments

Management has made a number of estimates and assumptions relating to the reporting of assets and liabilities and the disclosure of contingent assets and liabilities to prepare these financial statements in conformity with IFRS. Actual results could differ from those estimates.

The most significant areas of judgments and estimates are presented below:

Consolidation of subsidiaries

The Bank has not consolidated financial statements of subsidiaries due to immateriality of this consolidation on the Bank's financial statements, in accordance with the reviewed policy approved by the Bank.

Investments in subsidiaries are material to the Bank, if any of the following circumstances apply:

a) the Bank's share in net assets of the subsidiary exceeds 1% of total assets of the Bank,

b) the Bank's total share in net assets of all subsidiaries exceeds 5% of total assets of the Bank,

c) in the period under review the Bank's share in income and expense of the subsidiary exceeds, respectively, 3% of income and expense of the Bank,

d) in the period under review the Bank's total share in income and expense of all subsidiaries exceeds, respectively, 5% of total income and expense of the Bank, and

e) other circumstances as determined by the Board of the Bank.

Classification of investment securities

Upon initial recognition, the Bank designates securities as financial assets at fair value through profit or loss, held-to-maturity financial assets or available-for-sale financials assets recognition of changes in fair value through equity.

2.5. Reclassifications

Where needed, comparative figures have been adjusted to provide comparison with the changes of current year.

2.6. Changes in accounting policies

In the current year the Bank has adopted all of the new and revised Standards and Interpretations issued by the International Accounting Standards Board (the "IASB") and International Financial Reporting Interpretations Committee (the "IFRIC") of the IASB that are relevant to its operations and effective for annual reporting periods beginning on January 1, 2010. The standards and interpretations which have had effect on the financial statements are presented below:

IFRS 5 (Amendment) *Non-current Assets Held for Sale and Discontinued Operations*

Clarifies that IFRS 5 and other IFRSs that specifically refer to non-current assets (or disposal groups) classified as held for sale or discontinued operations set out all the disclosures required in respect of those assets or operations. IFRS 5 (Amendment) is applied for annual periods beginning on or after 1 January 2010.

IAS 1 (Amendment) *Presentation of Financial Statements*

Amendment to clarify the classification of a liability that can, at the option of the counterparty, be settled by the issue of the entity's equity instruments. IAS 1 (Amendment) is applied for annual periods beginning on or after 1 January 2010.

IAS 7 (Amendment) *Statement of Cash Flows*

Amends IAS 7 to state explicitly that only an expenditure that results in a recognized asset can be classified as a cash flow

from investing activities. IAS 7 (Amendment) is applied retrospectively for annual periods beginning on or after 1 January 2010.

IAS 36 (Amendment) *Impairment of Assets*

Clarifies that the largest unit permitted by IAS 36 for the purpose of allocating goodwill to cash-generating units is the operating segment level defined in IFRS 8 before aggregation as permitted in that Standard. IAS 36 (Amendment) is applied for annual periods beginning on or after 1 January 2010.

IAS 39 (Amendment) *Financial Instruments: Recognition and Measurement*

- Aims to clarify whether embedded prepayment options, in which the exercise price represented a penalty for early repayment of the loan, are considered closely related to the host debt contract.
- Aims to clarify that the scope exemption in IAS 39.2(g) applies only to binding (forward) contracts between an acquirer and a selling shareholder to buy or sell an acquiree that will result in a business combination at a future acquisition date.
- Clarifies when gains and losses on hedging instruments should be reclassified from equity to profit and loss account as a reclassification adjustment.

IAS 39 (Amendment) is applied prospectively for annual periods beginning on or after 1 January 2010.

2.7. Standards and comments not yet applied by the Bank

At the date of authorization of these financial statements, certain new Standards, amendments and interpretations to the existing Standards have been published but are not yet effective. The Bank has not early adopted any of these pronouncements.

Management anticipates that all of the pronouncements will be adopted in the Bank's accounting policy for the first period beginning after the effect date of the pronouncement. At the moment in management's estimation possible effect of most of the amendments on the Bank's financial statements can not be material.

IAS 32 (Amendment) *Financial instruments: Presentation- Classification of Right Issues*

IFRIC 19 *Extinguishing financial liabilities with equity instruments*

IFRS 7 (Amendment) *Transfer of Financial Assets*

IAS 24 (revised), 'Related party disclosures'

IFRS 9 *Financial Instruments*

2.8. Annual Improvements 2010 (effective from 1 July 2010 and later)

The IASB has issued *Improvements to IFRS 2010* (2010 Improvements). Most of these amendments become effective in annual periods beginning on or after 1 July 2010 or 1 January 2011. The 2010 Improvements amend certain provisions of IFRS 1, IFRS 3R, IFRS 7, IAS 1, IAS 27, IAS 34 and IFRIC 13. The Bank's preliminary assessments indicate that the 2010 Improvements will not have a material impact on the Bank's financial statements, except for disclosure requirements for financial instruments, which eliminated the requirements to disclose:

- the carrying amount of financial assets that would otherwise be past due or impaired whose terms have been renegotiated,
- maximum exposure to credit risk for financial instruments whose carrying amount best represents the maximum exposure to credit risk,
- description and estimate of fair value of collateral held for past due or impaired financial assets.

3. Significant accounting policies

The presented accounting policies have been applied in preparing financial statements. Accounting policies have been applied cosistently, other than consolidation of subsidiaries.

3.1. Foreign currency translation and presentation of foreign currency items

Transactions in foreign currencies are translated to the appropriate functional currency at the foreign exchange rate ruling at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies at the balance sheet date are translated to the functional currency at the foreign exchange rate ruling at that date. Non-monetary assets and liabilities denominated in foreign currencies, which are stated at historical cost, are translated to the functional currency at the foreign exchange rate ruling at the date of the transaction. Non-monetary assets and liabilities that are stated at fair value and whose appraised value is denominated in foreign currencies are translated to the functional currency at the foreign exchange rate ruling at the dates the fair values were determined. Foreign exchange differences arising on translation are recognised in the income statement.

Changes in the fair value of monetary securities denominated in foreign currency classified as available-for-sale are analysed between translation differences resulting from changes in the

amortised cost of the security and other changes in the carrying amount of the security. Translation differences related to changes in the amortised cost are recognised in profit or loss, and other changes in the carrying amount are recognised in equity.

Translation differences on non-monetary items, such as equities classified as available-for-sale financial assets, are included in the revaluation reserve in equity.

The exchange rates at the balance sheet dated used by the Bank in the preparation of the consolidated financial statements are as follows:

	December 31, 2010	December 31, 2009
AMD/1 US Dollar	363.44	377.89
AMD/1 Euro	481.16	542.23
AMD/1 SDR	559.71	592.41

3.2. Cash and cash equivalents

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

3.3. Financial instruments

Classification

Financial instruments at fair value through profit or loss are financial assets or liabilities that are:

- acquired or incurred principally for the purpose of selling or repurchasing in the near term;
- part of a portfolio of identified financial instruments that are managed together and for which there is evidence of a recent actual pattern of short-term profit-taking;
- a derivatives (except for a derivative that is a designated and effective hedging instrument); or,
- upon initial recognition, designated by the entity as at fair value through the profit or loss. Financial instruments are designated at fair value through profit or loss if the Bank manages such investments and makes purchase and sale decisions based on their fair value.

Financial assets and financial liabilities are designated at fair value through profit or loss when:

- Doing so significantly reduces measurement inconsistencies that would arise if the related derivatives were treated as held for trading and the underlying financial instruments were carried at amortised cost, such as loans and advances to customers or banks and debt securities in issue;

- Certain investments that are managed and evaluated on a fair value basis in accordance with a documented risk management or investment strategy and reported to key management personnel on that basis are designated at fair value through profit and loss; and
- Financial instruments, such as debt securities held, containing one or more embedded derivatives significantly modify the cash flows, are designated at fair value through profit and loss.

All trading derivatives in a net receivable position (positive fair value) are reported as assets. All trading derivatives in a net payable position (negative fair value) are reported as liabilities.

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market, other than those that the Bank intends to sell immediately or in the near term, those that the Bank upon initial recognition designates as at fair value through profit or loss, or those which the holder may not recover substantially all of its initial investment, other than because of credit deterioration.

Held-to-maturity investments are non-derivative financial assets with fixed or determinable payments and fixed maturity that the Bank has the positive intention and ability to hold to maturity, other than those that:

- the Bank upon initial recognition designates as at fair value through profit or loss;
- the Bank designates as available-for-sale; or
- meet the definition of loans and receivables.

Available-for-sale assets are financial assets are those financial assets that are designated as available-for-sale or are not classified as loans and receivables, held-to-maturity investments or financial instruments at fair value through profit or loss.

Recognition

Financial assets and liabilities are recognised in the balance sheet when the Bank becomes a party to the contractual provisions of the instrument. All regular way purchases of financial assets are accounted for at the settlement date.

The changes in fair values between the trade and settlement dates are immaterial.

Measurement

A financial asset or liability is initially measured at its fair value plus, in the case of a financial asset or liability not at fair value through profit or loss, transaction costs that are directly attributable to the acquisition or issue of the financial asset or liability.

Subsequent to initial recognition, financial assets, including derivatives that are assets, are measured at their fair values,

without any deduction for transaction costs that may be incurred on sale or other disposal, except for:

- loans and receivables, which are measured at amortized cost using the effective interest rate method;
- Held-to-maturity investments, which are measured at amortized cost using the effective interest method; and
- investments in equity instruments that do not have a quoted market price in an active market and whose fair value cannot be reliably measured, which are measured at cost.

All financial liabilities, other than those designated at fair value through profit or loss and financial liabilities that arise when a transfer of a financial asset carried at fair value does not qualify for derecognition, are measured at amortised cost. Amortised cost is calculated using the effective interest rate method. Premiums and discounts, including initial transaction costs, are included in the carrying amount of the related instrument and amortised based on the effective interest rate of the instrument.

3.4. Fair value measurement principles

The fair value of financial instruments is based on their quoted market price at the balance sheet date without any deduction for transaction costs. If a quoted market price is not available, the fair value of the instrument is estimated using pricing models or discounted cash flow techniques.

Where discounted cash flow techniques are used, estimated future cash flows are based on management's best estimates and the discount rate is a market related rate at the balance sheet date for an instrument with similar terms and conditions. Where pricing models are used, inputs are based on market related measures at the balance sheet date.

The fair value of derivatives that are not exchange-traded is estimated at the amount that the Bank would receive or pay to terminate the contract at the balance sheet date taking into account current market conditions and the current creditworthiness of the counterparties.

3.5. Gains and losses on subsequent measurement

A gain or loss arising from a change in the fair value of a financial asset or liability is recognised as follows:

- a gain or loss on a financial instrument classified as at fair value through profit or loss is recognised in the income statement;
- a gain or loss on an available-for-sale financial asset is recognised directly in equity through the statement of changes in shareholders' equity (except for impairment losses and foreign exchange gains and losses) until the

asset is derecognised, at which time the cumulative gain or loss previously recognised in equity is recognised in the income statement. Interest in relation to an available-for-sale financial asset is recognised as earned in the income statement calculated using the effective interest rate method.

For financial assets and liabilities carried at amortised cost, a gain or loss is recognised in the income statement when the financial asset or liability is derecognised or impaired, and through the amortization process.

3.6. Derecognition

A financial asset is derecognised when the contractual rights to the cash flows from the financial asset expire or when the Bank transfers substantially all the risks and rewards of ownership of the financial asset. Any rights or obligations created or retained in the transfer are recognised separately as assets or liabilities. A financial liability is derecognised when it is extinguished.

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 statement of income.

3.7. Offsetting

Financial assets and liabilities are offset and the net amount reported in the balance sheet when there is a legally enforceable right to set off the recognised amounts and there is an intention to settle on a net basis, or realise the asset and settle the liability simultaneously.

3.8. Repurchase and reverse repurchase agreements

Securities sold under sale and repurchase ("repo") agreements are accounted for as secured financial transactions, with the securities retained in the balance sheet, and, if the transferee has the right by contract or custom to sell or repledge them, they are reclassified as securities pledged under sale and repurchase agreements and faced as the separate balance sheet item. The counterparty liability is included in amounts due to other banks or to financial institutions, as appropriate. The differences between the sale and repurchase price are treated as interest expense and recognised in the income statement over the terms of the repo agreement, using the effective interest rate method.

Securities purchased under agreements to resell ("reverse repo") are recorded as due from banks or financial institutions as appropriate. The differences between the sale and repurchase prices are treated as interest and accrued over the life of the reverse repo agreement using the effective interest method.

3.9. Securities lending and borrowing

Securities lending and borrowing transactions are usually collateralised by securities or cash. The transfer of the securities to counterparties is only reflected in the balance sheet if the risks and rewards of ownership are also transferred. Cash advanced or received as collateral is recorded as an asset or liability.

Securities borrowed are not recognized in the balance sheet, unless they are sold to third parties, in which case the obligation to return the securities is recorded as a trading liability and measured at fair value with any gains or losses included in "Net trading income".

3.10. Notes and coins in circulation

Notes and coins in circulation issued by the Bank are presented in the balance sheet as a liability at nominal value. Printing and production costs of notes and coins are expensed in the year when they incur.

3.11. Numismatic coins

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

3.12. Own assets

Items of property and equipment are stated at cost less accumulated depreciation and impairment losses.

Where an item of property and equipment comprises major components having different useful life, they are accounted for as separate items of property and equipment.

Repairs and maintenance are charged to the income statement during the period in which they are incurred. The cost of major renovations is included in the carrying amount of the

asset when it is probable that future economic benefits in excess of the originally assessed standard of performance of the existing asset will flow to the Bank. Major renovations are depreciated over the remaining useful life of the related asset.

Any gain and loss resulting from the sale of an item of property and equipment, which is the difference between the proceeds from sales and the carrying amount of that asset, is taken to income statement in the period when it is incurred.

Depreciation

Depreciation is charged to the comprehensive income statement on a straight-line basis over the estimated useful life of the individual assets. Depreciation commences on the date of acquisition or, in respect of internally constructed assets, from the time an asset is completed and ready for use. Land is not depreciated. The estimated useful life are as follows:

	2010	2009
Buildings	30 - 50 years	30 - 50 years
Networks, computer and other equipment	5 - 15 years	5 - 8 years
Vehicles	5 years	5 years
Others	2 - 15 years	2 - 10 years

3.13. Intangible assets

Intangible assets, which are acquired by the Bank, are stated at cost less accumulated amortization and impairment losses.

The Bank has revised the estimated useful life of intangible assets in 2009. According to the Bank's estimations, the useful life of software used by the Bank is for an indefinite term. Intangible assets with their indefinite term of useful life shall not be amortized but shall be assessed each year for depreciation, individually or separately for the money creating unit. Intangible assets with their indefinite term of useful life shall be monitored each year to make sure these remain to be accounted within the category defined.

Costs associated with maintaining computer software programmes are recorded as an expense as incurred.

3.14. Impairment

Financial assets carried at amortized cost

Financial assets carried at amortized cost consist principally of placements with banks and other financial institutions, loans, other receivables and unquoted available-for-sale debt securities ("loans and receivables"). The Bank reviews its loans and receivables to assess impairment on a regular basis. A loan

or receivable is impaired and impairment losses are incurred if, and only if, there is objective evidence of impairment as a result of one or more events that occurred after the initial recognition of the loan or receivable and that event (or events) has an impact on the estimated future cash flows of the loan that can be reliably estimated.

Criteria used to determine that there is objective evidence of an impairment loss may include indications that the borrower or a group of borrowers is experiencing significant financial difficulty, default or delinquency in interest or principal payments, breach of loan covenants or conditions.

The Bank first assesses whether objective evidence of impairment exists individually for loans and receivables that are individually significant, and individually or collectively for loans and receivables that are not individually significant. If the Bank determines that no objective evidence of impairment exists for an individually assessed loan or receivable, whether significant or not, it includes the loan in a group of loans and receivables with similar credit risk characteristics and collectively assesses them for impairment. Loans and receivables that are individually assessed for impairment and for which an impairment loss is or continues to be recognised are not included in a collective assessment of impairment.

If there is objective evidence that an impairment loss on a loan or receivable has been incurred, the amount of the loss is measured as the difference between the carrying amount of the loan or receivable and the present value of estimated future cash flows including amounts recoverable from guarantees and collateral discounted at the loan or receivable's original effective interest rate. Contractual cash flows and historical loss experience adjusted on the basis of relevant observable data that reflect current economic conditions provide the basis for estimating expected cash flows.

In some cases the observable data required to estimate the amount of impairment loss on a loan or receivable may be limited or no longer fully relevant to current circumstances. This may be the case when a borrower is in financial difficulties and there are few available historical data relating to similar borrowers. In such cases, the Bank uses its experience and judgment to estimate the amount of any impairment loss.

All impairment losses in respect of loans and receivables are recognised in the income statement and are only reversed if a subsequent increase in recoverable amount can be related objectively to an event occurring after the impairment loss was recognised.

Financial assets carried at cost

Financial assets carried at cost include unquoted equity instruments included in available-for-sale assets that are not carried at fair value because their fair value can not be reliably measured. If there is objective evidence that such investments

are impaired the impairment loss is calculated as the different between the carrying amount of the investment and the present value of the estimated future cash flows discounted at the current market rate of return for a similar financial asset.

All impairment losses in respect of these investments are recognised in the income statement and can not be reversed.

Non financial assets

Other non financial assets are assessed at each reporting date for any indications of impairment. The recoverable amount of non financial assets is the greater of their fair value less costs to sell and value in use. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset. For an asset that does not generate cash inflows largely independent of those from other assets, the recoverable amount is determined for the cash-generating unit to which the asset belongs. An impairment loss is recognised when the carrying amount of an asset or its cash-generating unit exceeds its recoverable amount.

All impairment losses in respect of non financial assets are recognised in the comprehensive income statement and reversed only if there has been a change in the estimates used to determine the recoverable amount. Any impairment loss revered is only reversed to the extent that the asset's carrying amount does not exceed the carrying amount that would have been determined, net of depreciation or amortization, if no impairment loss had been recognised.

3.15. Pensions

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

3.16. Provisions

A provision is recognised in the balance sheet when the Bank has a legal or constructive obligation as a result of a past event, and it is probable that an outflow of economic benefits will be required to settle the obligation. If the effect is material, provisions are determined by discounting the expected future cash flows at a pre-tax rate that reflects current market assessments of the time value of money and, where appropriate, the risks specific to the liability.

3.17. Taxation

The Bank is not subject to any taxes, with the exception of taxes, duties or customs fees collected at the border of the Republic of Armenia for imported goods. At the same time, the Bank acts as a tax agent according to the procedure defined under the Law of the Republic of Armenia.

3.18. Interest income and expense

Interest income and expense are recognised in the comprehensive income statement as they accrue, taking into account the effective interest rate of the asset/liability or an applicable floating rate. Interest income and expense include the amortization of any discount or premium or other differences between the initial carrying amount of an interest bearing instrument and its amount at maturity calculated on an effective interest rate basis.

Interest income on financial instruments at fair value through comprehensive income statement is included in net gain on financial instruments at fair value through profit or loss.

Loan origination fees, loan servicing fees and other fees that are considered to be integral to the overall profitability of a loan, together with the related direct costs, are deferred and amortized to the interest income over the estimated live of the financial instrument using the effective interest rate method.

3.19. Fee and commission income

Other fee and commission income is recognised when the corresponding service is provided.

4. Interest income

AMD thousand

	2010	2009
Interest income from foreign currency assets		
Term deposits	1,834,407	2,342,707
Held to maturity assets	138,829	5,346
Nostro accounts	37,312	101,606
Overnight	211,531	171,419
Placements with the IMF	60,756	47,485
Other	-	191
	2,282,835	**2,668,754**
Interest income from domestic currency assets		
Loans and reverse repurchase agreements	4,632,789	4,147,550
Available-for-sale assets	2,305,423	2,011,754
Held to maturity assets	270,049	12,867
Other	43,518	21,567
	7,251,779	**6,193,738**
	9,534,614	**8,862,492**

5. Interest expense

AMD thousand

	2010	2009
Interest expense on foreign currency liabilities		
Loans from the IMF	2,571,362	1,932,096
Other borrowings	204,348	187,820
Other liabilities	17,320	40,450
	2,793,030	**2,160,366**
Interest income from domestic currency assets		
Debt securities issued	-	4,502
Due to the Government of the Republic of Armenia	13,487,074	11,085,891
Deposits and balances from financial and other institutions	313,078	174,045
Other	59,094	50,336
	13,859,246	**11,314,774**
	16,652,276	**13,475,140**

6. Net foreign exchange gain/(loss)

AMD thousand

	2010	2009
Net gain/(loss) from revaluation of monetary assets and monetary liabilities	(12,099,588)	22,597,494
Net gain on spot transactions	137,125	13,978,029
	(11,962,463)	**36,575,523**

Included in the net loss from revaluation of monetary assets and liabilities is a foreign exchange revaluation loss of AMD 24,501,164 thousand on financial instruments at fair value through profit or loss (2009: AMD 16,312,104, thousand net gain).

On March 3, 2009, the Bank decided to limit intervention in to the foreign exchange market and return to the floating exchange rate policy. This move (when the Armenian dram depreciated vis-a-vis the US dollar by 27.1 percent within a day) affected the Bank's financial position positively for 2009, since the Bank's international reserves are held in foreign currency. After having moved to the floating exchange rate policy, the Bank's net daily gain from revaluation of dram-denominated assets and liabilities amounted to AMD 44,393,817 thousand. In 2010 the Armenian dram revaluated against the US dollar by 4%.

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

AMD thousand

	2010	2009
Net gain on assets under trust management (excluding foreign exchange revaluation*)	236,469	912,737
Net gain on foreign securities under own management (excluding foreign exchange revaluation*)	6,599,921	6,865,918
Net gain on money market instruments under own management	11,126	16,621
Net loss on futures under own management (excluding foreign exchange revaluation*)	(3,772,380)	(2,007,673)
Trust management fees (excluding foreign exchange revaluation*)	(131,961)	(134,725)
	2,943,175	**5,652,878**

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

8. Other income

AMD thousand

	2010	2009
Income from sales of numismatic coins	409,278	439,736
Other income	1,492,375	269,943
	1,901,653	**709,679**

9. Costs of production of banknotes, coins and numismatics

AMD thousand

	2010	2009
Costs of production of banknotes and coins	1,366	989,302
Costs of production of numismatics	225,436	247,012
	226,802	**1,236,314**

10. Other expenses

AMD thousand

	2010	2009
Employee compensation, staff training and related payments	4,139,441	4,013,165
Investments in funds	5,500,000	-
Security and maintenance of reserves	729,718	736,885
Depreciation and amortization	731,035	437,166
Repairs and maintenance	569,417	361,319
Professional services	240,330	181,164
Other	1,152,001	1,093,355
	13,061,942	**6,823,054**

11. Placements with banks and other financial institutions

AMD thousand

	2010	2009
Placements with banks and other financial institutions in foreign currency		
Term deposits	37,385,870	34,009,997
Nostro accounts	119,776,198	181,157,023
Accrued interest on deposits and nostro accounts	36,169	57,280
Cash included in assets under trust management	89,668	259,484
Receivables	814,196	6,194,286
	158,102,101	**221,678,070**

Concentration of placements with banks and other financial institutions

As at 31 December 2010 and 2009 the Bank had placements in 3 banks, whose individual balances exceeded 10% of total placements. The gross value of these balances as of 31 December 2010 and 2009 amounted to AMD 135,063,346 thousand and AMD 211,234,506 thousand, respectively.

During 2009 the Bank has placed short-term FX deposits with, and received the ones from, Armenian commercial banks (these amounts have been included in Item 'Receivables'). As of December 31, 2009, the Bank has placed deposit of USD 10 000 thousand and the dram-denominated deposit from the mentioned commercial bank has been included in Note 19.

12. Financial instruments at fair value through profit or loss recognized in the statement of comprehensive income

AMD thousand

	2010	2009
Assets		
Debt and other fixed-income instruments-Quoted		
Foreign government securities under own management	358,460,805	415,401,592
Securities under trust management	42,465,054	43,758,444
Money market instruments under own management	3,645,519	-
	404,571,378	**459,160,036**
Derivative financial instruments-Quoted		
Foreign exchange futures contracts under own management	61,539	74,639
	404,632,917	**459,234,675**

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

As at 31 December 2010 foreign securities at fair value under own management include:

AMD thousand

	2010	2009
Government securities	249,225,131	225,002,788
Securities directly/indirectly backed by the State	40,569,775	148,010,416
Other securities	68,665,899	42,388,388
Total	**358,460,805**	**415,401,592**

Securities under trust management include:

AMD thousand

	2010	2009
Securities of foreign governments	32,032,674	26,607,627
Securities of foreign financial institution	10,432,380	17,150,817
Total	**42,465,054**	**43,758,444**

Securities and derivative financial instruments under trust management represent financial instruments under discretionary asset management at foreign financial institutions. Risk exposure limits and investment guidance are set by the Bank.

Derivative financial instruments

AMD thousand

	2010	2009	2010		2009	
	Nominal value		Asset	Liability	Asset	Liability
Foreign exchange futures contracts under trust management	12,263,252	14,806,747	-	19,478	-	36,588
Foreign exchange futures contracts under own management	467,176,740	1,136,105,882	61,539	-	74,639	-
Total	**479,439,992**	**1,150,912,629**	**61,539**	**19,478**	**74,639**	**36,588**

13. Investment securities

AMD thousand

	2010	2009
Available-for-sale investments in foreign currency		
Equity investments at cost – Unquoted		
SWIFT	917	917
Available-for-sale investments in domestic currency		
Debt and other fixed-income instruments		
Treasury securities of the Government of the Republic of Armenia	12,124,141	25,936,859
Promissory note of the Government of the Republic of Armenia	55,644,010	79,629,720
	67,768,151	**105,566,579**
Equity investments at cost – Unquoted		
Investments in unconsolidated subsidiaries	20,894,923	15,594,923
Other equity investments	42,691	42,691
	20,937,614	**15,637,614**
Total available-for-sale investments in domestic currency	**88,705,765**	**121,204,193**
Total available-for-sale investments	**88,706,682**	**121,205,110**
Held-to-maturity investments in foreign currency		
Foreign securities under own management	95,678,521	25,171,087
	95,678,521	**25,171,087**
Held-to-maturity investments in domestic currency		
Discount bond	4,132,916	3,862,867
	4,132,916	**3,862,867**
Total held-to-maturity investments	**99,811,437**	**29,033,954**

In 2008 a non-interest demand bond at par value of AMD 85,663,194 thousand was issued by the Government of the Republic of Armenia as a gratis investment in the Bank. The bond was issued according to the Republic of Armenia law on the Central Bank to cover the negative equity reserves of the Bank. According to the same law AMD 23,985,710 thousand was directed to the redemption of the bond from the profit of 2009 (from profit of 2008: AMD 6,033,474 thousand).

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

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

Available-for-sale equity instruments in local currency are stated at cost, since there is no market for these investments and there have not been any recent transactions that provide evidence of the current fair value. In addition, discounted cash flow techniques yield a wide range of fair values due to uncertainty regarding future cash flows.

14. International Monetary Fund

Assets related to IMF — *AMD thousand*

	2010	2009
Placements with the IMF in foreign currency		
SDR holdings in the IMF	12,169,283	47,099,672
Quota in IMF (subscription)	51,493,341	54,502,140
Accrued interest	7,613	19,512
	63,670,237	**101,621,324**

The Bank maintains an SDR-denominated current account with the IMF used for processing and settling transactions with the IMF. This current account bears interest based on the SDR interest rate, obtained weekly, as a weighted average of selected rates of three-month instruments on the money market of the four currencies which constitute the SDR basket. In 2010, the interest rate ranged from 0.22% to 0.32% (2009: 0.82% to 0.25%).

According to the IMF Statute, the Bank acts as a fiscal agent of the Republic of Armenia and simultaneously behaves as a depositary of the IMF in the Republic of Armenia. As such, the Bank keeps records of the quota of the Republic of Armenia for membership with the IMF and the promissory note related to the membership of the Republic of Armenia in the IMF. The positions are as follows:

The quota of the Republic of Armenia for membership with the IMF amounts to SDR 92,000,000 as of 31 December 2010 (2009: SDR 92,000,000).

Liabilities to IMF in domestic currency

AMD thousand

	2010	2009
Securities account	140,663,079	140,663,079
Adjustment account for AMD liabilities to the IMF	(6,677,555)	8,523,264
Account 1	61,814,443	23,367,610
Account 2	2,754	2,630
	195,802,721	**172,556,583**

The IMF's Account 1 is used to carry out operations with the IMF, including the payment of membership fee, purchase and repurchase of assets, carrying of Stand-by loan, repayment of loans, as well as the sale of national currency of the Republic of Armenia.

The IMF's Account 2 is used to reflect the IMF's administrative expenditures and entries in national currency of the Republic of Armenia and within the territory of the Republic of Armenia.

As of 31 December 2010, loans of AMD 140,6 billion (31 December 2009: 140,6 billion) disbursed from the IMF are backed by the Government of the Republic of Armenia through an issuance of securities for these loans.

Liabilities to IMF in SDR

AMD thousand

	2010	2009
Credit	32,565,060	42,837,498
SDR allocation	49,248,152	52,125,764
Interest accrued	471,297	300,265
	82,284,509	**95,263,527**

The Poverty Reduction and Growth Facility was disbursed in SDR from the IMF to the Republic of Armenia for a period of 15 years, with 0% interest rate per annum (2009: 0.5%).

The disbursement of SDR to SDR Member States by the IMF without any conditions is the disbursement of SDR in proportion to the States' quotas. The disbursed SDR can be used to carry out transactions at rather a broad spectrum, including the purchase of currency of other Members, regulation of financial liabilities, donations, loan origination, and etc. As of 31 December 2010 the interest rate was 0.32% (0.23% in 2009).

In the reported periods the Bank had no violation of non-payment of principal and interest, or any other violations whatsoever.

As of 31 December 2010 and 2009, the carrying amounts of claims and liabilities to the IMF approximated their fair values.

15. Loans and reverse repurchase agreements

AMD thousand

	2010	2009
Loans to resident banks under arrangement with the KFW and World banks	29,643,307	25,619,315
Loans on subordinated terms	24,536,382	13,467,606
Other loans to resident banks	7,325,216	-
Amounts receivable under reverse repurchase agreements	8,022,812	30,782,396
Other loans	1,087,782	865,822
	70,615,499	**70,735,139**

Loans to resident banks under the agreement with the KFW and World bank are provided to 14 domestic banks and 2 financial institutions and bear interest at rates from 5.5% to 8% p.a.

In consideration of Armenia's banking sector reliability and long-term stability, the Bank has provided loans on subordinated terms to 8 banks for 7.5 percent interest rate p.a. and 5 years of maturity, aimed to build sufficient capacity in the system to absorb potential crisis-derived risks.

A loan for a 3-year period of maturity has been made for bank mergers in the banking sector.

The Bank accepted securities on reverse repurchase agreements as collateral for commercial loans, which are permitted to sell or repledge. As of 31 December 2010 amounts receivable under reverse repurchase agreements are with 5 resident banks (2009: 14 banks) and are collateralised by the following securities.

AMD thousand

	2010	2009
Treasury bonds of The Government of the Republic of Armenia	8,131,931	30,495,653
	8,131,931	**30,495,653**

16. Property and equipment

AMD thousand

	Land and buildings	Networks, computer and other equipment	Vehicles	Other	Total
Cost					
Balance at 1 January 2009	10,499,985	3,694,409	302,675	1,881,628	16,378,697
Additions	3,996,009	1,440,939	51,589	357,854	5,846,391
Disposals	(19,586)	(115,881)	(41,018)	(228,687)	(405,172)
Balance at 31 December 2009	14,476,408	5,019,467	313,246	2,010,795	21,819,916
Additions	9,782,376	968,262	10,268	530,320	11,291,226
Disposals	-	(499,688)	-	(69,904)	(569,592)
Reclassification	(489,133)	32,935	(6,453)	462,651	-
Balance at 31 December 2010	23,769,651	5,520,976	317,061	2,933,862	32,541,550
Depreciation					
Balance at 1 January 2009	1,724,054	2,659,909	172,173	1,443,845	5,999,981
Addition	47,926	234,390	39,516	115,334	437,166
Disposals	-	(114,020)	(38,967)	(227,031)	(380,018)
Balance at 31 December 2009	1,771,980	2,780,279	172,722	1,332,148	6,057,129
Addition	116,632	382,426	40,413	191,564	731,035
Disposals	-	(492,938)	-	(65,865)	(558,803)
Reclassification	-	-	(6,130)	6,130	-
Balance at 31 December 2010	1,888,612	2,669,767	207,005	1,463,977	6,229,361
Carrying amount					
At 31 December 2008	8,775,931	1,034,500	130,502	437,783	10,378,716
At 31 December 2009	12,704,428	2,239,188	140,524	678,647	15,762,787
At 31 December 2010	21,881,039	2,851,209	110,056	1,469,885	26,312,189

17. Intangible assets

AMD thousand

	Computer software
Cost	
Balance at 1 January 2009	462,200
Additions	172,085
Disposals	(1,063)
Balance at 31 December 2009	633,222
Additions	155,272
Disposals	-
Balance at 31 December 2010	788,494
Amortization	
Balance at 1 January 2009	206,373
Additions	-
Disposals	(1,058)
Balance at 31 December 2009	205,315
Additions	-
Disposals	-
Balance at 31 December 2010	205,315
Carrying amount	
At 31 December 2008	255,827
At 31 December 2009	427,907
At 31 December 2010	**583,179**

Intangible assets have been valued individually for depreciation, and no features of depreciation have been identified.

18. Other assets

AMD thousand

	2010	2009
Numismatic coins	739,624	735,712
Receivables	2,836,231	1,538,413
Other	176,406	177,200
	3,752,261	**2,451,325**

19. Deposits and balances from financial and other institutions

AMD thousand

	2010	2009
Foreign currency liabilities		
Vostro accounts and deposits of domestic banks	88,236,533	148,673,237
Current accounts of other legal entities	9,729,221	39,699
Term deposit of Deposit Insurance fund	1,684,280	1,903,238
	99,650,034	**150,616,174**
Domestic currency liabilities		
Vostro accounts and deposits of domestic banks	77,124,832	47,978,778
Term deposit and current accounts of Deposit Insurance fund	254,710	7,996
Current accounts of other legal entities	3,446,229	1,460,677
Other liabilities	-	3,756,770
	80,825,771	**53,204,221**

Concentration of deposits and balances from banks

As of 31 December 2010, no bank had been identified to have balances exceeding 10% of total amount allocated with the Bank by commercial banks. As of 31 December 2009, only one bank had a balance individually exceeding 10% of that amount, which amounted to AMD 27,452,156 thousand.

During 2009 the Bank has placed short-term deposits in different currency with, and received the ones from, Armenian commercial banks (these amounts have been included in Item 'Other liabilities'). As of December 31, 2009, the Bank has received deposit of AMD 3,751,400 thousand and the US dollar-denominated deposit placed with that commercial bank has been included in Note 11.

20. Other borrowed funds

AMD thousand

	2010	2009
Loans from KFW and World bank	27,560,279	28,266,861
Accrued interest	39,530	42,536
	27,599,809	**28,309,397**

The loans are provided under an intergovernmental agreement on financial cooperation between the Government of the Republic of Armenia and the Federal Republic of Germany

to finance special loan programs placed through domestic commercial banks (Note 15). The loans mature from 2010 through 2048, and bear interest of 0.75% p.a. for the used part of the loan, and 0.25% for the unused part of the loan. The repayment of loans to KFW is guaranteed by the Government of the Republic of Armenia.

The loans are provided by World Bank for financing small and medium enterprises through domestic commercial banks (Note 15). The loans mature from 2010 through 2035, and bear interest of 0.81%.

As of the reporting periods the Bank has not had any defaults of principal, interest or other breaches with respect to its liabilities during the period (2009: either).

21. Other liabilities

AMD thousand

	2010	2009
Demand deposits of employees	531,068	428,266
Other	822,826	425,036
	1,353,894	**853,302**

22. Due to the Government of the Republic of Armenia

AMD thousand

	2010	2009
Foreign currency liabilities		
Balances of the Government of the Republic of Armenia	1,187,537	1,225,249
Payables	2,801,575	103,939
	3,989,112	**1,329,188**
Domestic currency liabilities		
Balances of the Government of the Republic of Armenia	27,315,188	46,143,142
Deposits	79,230,385	131,051,654
	106,545,573	**177,194,796**

As the financial agent to the RA Government, the Central Bank of Armenia is entitled to attract free funds from the RA Government, based on the principles of cooperation adopted in the framework of the Agreement signed between the Ministry of Finance and Economy of the RA and the Central Bank of

Armenia on 13/10/2006. In consideration of the significance of the influence that these Parties have on the market in terms of their transactions, the Ministry of Finance shall allocate the Government's funds by adhering to the market rules, and the CBA shall provide services that are adequate by their market price and quality. The actions of the Parties cannot be charged by the private sector and result in ineffective performance of market mechanisms.

23. Equity

Issued capital

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

Additional paid in capital

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

General reserve

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

24. Commitments

Capital commitments

The capital commitments outstanding at 31 December 2010 related to the construction of the Bank's premises is AMD 14,541,725 thousand (2009: AMD 4,543,029 thousand).

Litigation

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

Guarantees

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

25. Related party transactions

Transactions with members the key management

Total remuneration is included in employee compensation (Note 10).

AMD thousand

	2010	2009
Key management including the Bank's board members	209,580	196,427

The outstanding balances and average effective interest rates as of 31 December 2010 with members of the key management are as follows:

AMD thousand

	2010	Average effective Interest Rate	2009	Average effective Interest Rate
Balance Sheet				
Assets				
Loans	65,640	3-5%	76,776	3-5%
Deposits	59,725	14%	42,858	13.5%
Receivables on business trip	-	-	2,956	0.00%
Salary payable	-	-	2,102	0.00%

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

AMD thousand

	2010	2009
Statement of comprehensive income		
Interest expense	6,142	2,042
Interest income	3,294	2,900

Transactions with subsidiaries

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

AMD thousand

	2010	2009
Statement of comprehensive income		
Other expenses		
Money collection expenses	556,708	601,552

Transactions with the Government of the Republic of Armenia

The outstanding balances and average effective interest rates as of 31 December 2010 with government are as follows:

AMD thousand

	2010	Average effecttive Inte-rest Rate	2009	Average effecttive Inte-rest Rate
Balance Sheet				
Assets				
The Government of Republic of Armenia treasury securities (Note 13)	12,124,141	11%	25,936,859	8.6%
The Government of Republic of Armenia promissory note issued to the Bank as additional paid in capital (Note 13)	55,644,010	0.00%	79,629,720	0.00%
Liabilities				
Due to the Government of the Republic of Armenia (local currency, Note 22)	106,545,573	10%	177,194,796	9%
Due to the Government of the Republic of Armenia (other currency, Note 22)	3,989,112	0.00%	1,329,188	0.00%

The flow of deposits included in liabilities to the Government of the Republic of Armenia, in domestic currency

AMD thousand

	2010	2009
Balance at 1 January	131,051,654	-
Additions	688,363,583	471,312,429
Disposal	(740,184,852)	(340,260,775)
Balance at 31 December	79,230,385	131,051,654

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

AMD thousand

	2010	2009
Statement of comprehensive income		
Interest income from treasury securities of the Government of the Republic of Armenia	2,305,423	2,011,754
Net gain/(loss) on spot transactions	782,980	(499,005)
Interest paid on other amounts due to the Government of the Republic of Armenia	13,487,074	11,085,891

26. Cash and cash equivalents

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

AMD thousand

	2010	2009
Cash	7,552,047	7,776,292
Nostro accounts (Note 11)	119,776,198	181,157,023
SDR holdings in IMF (Note 14)	12,169,283	47,099,672
	139,497,528	**236,032,987**

27. Fair value of financial instruments

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

As disclosed in Note 13 the fair value of unquoted equity securities with a carrying value of AMD 20,937,614 thousand (2009: AMD 15,637,614 thousand) could not be determined.

Held-to-maturity foreign securities under own management as of December 31, 2010, represent government securities of other countries, amounting to AMD 95,678,521 thousand (2009: 25,171,087 thousand); these are listed securities, and as of December 31, 2010, their fair value has amounted to AMD 95,671,630 thousand (2009: 25,171,160 thousand).

The estimates of fair value are intended to approximate the amount for which a financial instrument could be exchanged between knowledgeable, willing parties in an arm's length transaction. However given the uncertainties and the use of

subjective judgment, the fair value should not be interpreted as being realisable in an immediate sale of the assets or settlement of liabilities.

Fair value hierarchy

Financial assets and liabilities measured at fair value in the statement of financial standing are presented according to the fair value hierarchy. The hierarchy divides the financial assets and liabilities into three levels based on the materiality of instruments used when measuring their fair value. The fair value hierarchy has the following there levels:

Level 1: price determination on active markets for the same assets and liabilities (non-adjusted);

Level 2: baseline data, other than price determination specified in Level 1, which are considered for the asset and liability directly (i.e. as prices) and indirectly (i.e. available based on prices);

Level 3: baseline data on the asset or liability, which are not based on market data in consideration (non-considered baseline data).

AMD thousand

	2010			
	Level 1	Level 2	Level 3	Total
Financial assets				
Quoted securities and bonds	404,571,378	-	-	404,571,378
Unquoted securities and bonds	-	12,124,141	-	12,124,141
Derivative financial assets	61,539	-	-	61,539
Total	404,632,917	12,124,141	-	416,757,058
Financial liabilities				
Financial liabilities at fair value through profit or loss	19,478	-	-	19,478
Total	19,478	-	-	19,478
Net fair value	**404,613,439**	**12,124,141**	**-**	**416,737,580**

AMD thousand

	2009			
	Level 1	Level 2	Level 3	Total
Financial assets				
Quoted securities and bonds	459,160,036	-	-	459,160,036
Unquoted securities and bonds	-	25,936,860	-	25,936,860
Derivative financial assets	74,639	-	-	74,639
Total	459,234,675	25,936,860	-	485,171,535
Financial liabilities				
Financial liabilities at fair value through profit or loss	36,588	-	-	36,588
Total	36,588	-	-	36,588
Net fair value	**459,198,087**	**25,936,860**	**-**	**485,134,947**

28. Risk management

Institutional Framework

International reserves of the Republic of Armenia are Central Bank claims on non-residents in freely convertible foreign currencies. The reserves are reflected in the Balance Sheet of the Central Bank of Armenia (CBA). The CBA manages the reserves in accordance with the principles laid down in article 52 of the "Law of Republic of Armenia on the Central Bank of Armenia", by investing the reserves within the Investment framework set by the Board of the CBA.

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

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

Administration and Control

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

Investment Committee as a rule meets once a month to discuss issues related to reserves management. The Committee includes heads of structural units involved in the entire process of reserves management, as well as the Bank's Chairman and

Deputy Chairman. Formerly, the Committee was totally a consultative body but, after the introduction of the three level system for management, it has been granted executive power. Financial Department reports on the performance of reserves management to Investment Committee on a quarterly basis and to the Bank's Board on a semiannual basis. Each quarter the Bank presents information on condition and composition of international reserves to the Government and the National Assembly, and makes that information publicly available.

Reserve management process is under the control of the Bank's Audit Group, which reports directly to the Board. The reserves management function is audited once a year by an internationally recognized audit firm.

Asset Allocation and Risk Management

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

Credit risk management

Reserve management process entails credit risk exposure, defined as default on obligations by an issuer of the securities or counterparty. The Central Bank of the RA evaluates the counterparty creditworthiness based on the credit ratings assigned by leading internationally recognized credit rating agencies.

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

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

each rating group, maturity, individual counterparties, and asset classes. The matrix is the mail tool for the credit risk management.

Maximum credit risk without guaranty or other credit security

The table below presents the worst scenario of the Bank's exposure to credit risk, as of 31 December 2010, and 31 December 2009, without consideration of security. For balance sheet assets, credit risks have been based on net carrying value.

AMD thousand

	Note	Gross maximum risk, as of 31 December 2010	Gross maximum risk, as of 31 December 2009
Placements with banks and other financial institutions	11	158,102,101	221,678,070
Financial instruments fair value through profit or loss recognized in the statement of comprehensive income	12	404,632,917	459,234,675
Loans and reverse repurchase agreements	15	70,615,499	70,735,139
Available-for-sale assets	13	88,706,682	121,205,110
Held-to-maturity investments	13	99,811,437	29,033,954
International Monetary Fund	14	63,670,237	101,621,324
Credit risk, total		885,538,873	1,003,508,272

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

Liquidity risk

Liquidity risk management: as a fiscal agent of the Government and the monetary authority of the RA, the Bank is responsible for public debt service, the Government's foreign payments service and for smoothing out sharp fluctuations in national currency in the domestic market. From this perspective proper cash and liquidity management is crucial.

Based on the reserves' management objectives and grouping liquidity needs based liabilities' term structure, Armenia's international reserves have been divided into three tranches – working capital, liquidity and investment tranches. While the first two are designed to meet short-term/instant and mid-term liquidity requirements, the purpose of investment tranche is the accumulation of wealth.

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

Below we present the distribution of the Bank's non-discounted financial liabilities, as of December 31, 2010 and 2009 in accordance with the period spanning from the balance sheet date to the expiration date specified in contracts.

AMD thousand

2010							
	Demand or less than 1 month	1 to 3 months	3 months to 1 year	1 year to 5 years	More than 5 years	No maturity	Total
Financial liabilities							
Notes and coins in circulation	-	-	-	-	-	348,164,734	348,164,734
Deposits and balances from financial and other institutions	180,489,100	-	-	-	-	-	180,489,100
Due to the Government of the Republic of Armenia	83,771,724	27,156,571	-				110,928,295
Due to IMF	120,364,074	-	8,523,491	148,181,976	1,487,336	-	278,556,877
Other borrowings	-	-	238,146	1,585,982	30,393,480	-	32,217,608
Total non-discounted financial liabilities	**384,624,898**	**27,156,571**	**8,761,637**	**149,767,958**	**31,880,816**	**348,164,734**	**950,356,614**

AMD thousand

2009							
	Demand or less than 1 month	1 to 3 months	3 months to 1 year	1 year to 5 years	More than 5 years	No maturity	Total
Financial liabilities							
Notes and coins in circulation	-	-	-	-		320,669,631	320,669,631
Deposits and balances from financial and other institutions	198,160,386	3,793,770	1,908,238	-	-	-	203,862,394
Due to the Government of the Republic of Armenia	72,568,670	-	110,955,766	-	-	-	183,524,436
Due to IMF	106,651,903	-	8,846,564	149,538,921	3,411,701	-	268,449,089
Other borrowings	-	-	236,077	1,811,255	31,219,870	-	33,267,202
Total non-discounted financial liabilities	**377,380,959**	**3,793,770**	**121,946,645**	**151,350,176**	**34,631,571**	**320,669,631**	**1,009,772,752**

Market risk

Market risk is defined as possible loss of the value of the assets due to adverse exchange rate and interest rate fluctuations.

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

As to *interest rate risk*, within the three level management structure the Board defines the overall *risk tolerance,* which is the acceptable level of interest rate risk in the long run. It also outlines portfolio optimization principles. The risk tolerance is defined as a minimum acceptable return over certain period of time (now 3 years) with 95 percent confidence level. The authority to set tactical benchmarks is delegated to Investment Committee.

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

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

The following table shows the currencies which can affect the Bank's non-commercial dram-denominated assets and liabilities and projected flows thereon, as of December 31, 2010. The analysis measures the impact of possible foreign currency fluctuations vis-a-vis the Armenian dram (provided that other variables remain constant) on the statement of financial results, determined by the change in fair value of non-commercial dram-denominated assets and liabilities sensitive to the foreign currency. In the Table, the negative value denotes net potential decrease while the positive value denotes net potential increase, in the statement of financial results or in equity.

AMD thousand

Currency	Change in currency rate in %	2010		2009	
		Effect on profit before tax	Effect on equity	Effect on profit before tax	Effect on equity
USD	+20%	53,997,794	53,977,794	69,619,854	69,619,854
USD	-20%	(53,997,794)	(53,977,794)	(69,619,854)	(69,619,854)

The following table demonstrates the sensitivity of the Bank's equity, which is calculated by revaluating fixed rate available-for-sale financial assets at 31 December 2010 for the effects of the assumed changes in interest rates. The sensitivity of equity is analysed by maturity of the asset. The sensitivity of equity is based on the assumption that there are parallel shifts in the yield curve.

AMD thousand

Currency	Change in basis points	2010		2009	
		Up to 1 year	More than 1 year	Up to 1 year	More than 1 year
AMD	+20%	(959)	(141,668)	(7,385)	(167,873)
AMD	-20%	729	136,647	5,120	171,489

The following table demonstrates the sensitivity to profit of the Bank, which is calcuated by revaluating financial instruments at fair value through profit and loss as of 31 December 2010, based on the assumption of changing interest rates.

AMD thousand

Currency	Change, basis points	2010	2009
		Impact on profit before tax	Impact on profit before tax
Foreign currency	+25	(914,599)	(893,533)
Foreign currency	-25	914,599	893,553

29. Average effective interest rate

The table below displays the Bank's interest bearing assets and liabilities as at 31 December 2010 and as at December 2009 and their corresponding average effective interest rates as at that date. These interest rates are an approximation of the yields to maturity of these assets and liabilities.

AMD thousand

	2010		2009	
	Value	Average Effective Interest Rate	Value	Average Effective Interest Rate
INTEREST BEARING ASSETS				
Placements with banks and other financial institutions				
Nostro accounts				
- USD	90,353,330	0.16%	143,848,833	0.08%
- EUR	28,253,122	0.36%	36,195,576	0.56%
- GBP	1,053,146	0.00%	1,249,523	0.11%
- Other currencies	210,537	0.00%	127,318	0.00%
Deposits and other balances in foreign banks				
- USD	32,739,803	4.14%	34,062,534	7.3%
- GBP	4,677,966	0.69%	-	-
Other balances				
- USD	499,399	0.00%	5,921,977	4.95%
- EUR	314,798	0.00%	272,309	0.00%
	158,102,101		**221,678,070**	
Financial instruments at fair value through profit or loss				
Foreign government securities under own management				
- USD	179,843,535	1.30%	241,852,660	1.6%
- EUR	178,617,270	1.90%	173,548,932	2.5%
Assets under trust management				
- USD	42,465,054	1.20%	43,758,444	2.5%
Contracts under own management				
- USD	45,335	0.00%	22,589	0.00%
- EUR	16,204	0.00%	52,050	0.00%
Money market instruments				
- USD	3,645,519	0.27%	-	-
	404,632,917		**459,234,675**	
Loans and reverse repurchase agreements				
- AMD	70,615,499	7.84%	70,735,139	7.7%

Available-for-sale assets				
- AMD	55,644,010	0.00%	79,629,720	0.00%
- AMD	12,124,141	11.00%	25,936,859	8.6%
- AMD (Equity investments)	20,937,614	0.00%	15,637,614	0.00%
- EUR (Equity investments)	917	0.0%	917	0.0%
Held to maturity				
- AMD	4,132,916	6.47%	3,862,867	5.8%
- GBP	19,083,251	0.44%	25,171,087	0.40%
- JPY	76,595,270	0.12%	-	-
	188,518,119		150,239,064	
Placements with the IMF				
- SDR (SDR holdings)	63,670,237	0.29%	101,621,324	0.37%
INTEREST BEARING LIABILITIES				
Deposits and balances from financial and other institutions				
Current accounts of domestic banks				
- AMD	57,515,911	0.00%	40,449,703	0.00%
- Other currencies	88,236,533	0.00%	148,673,237	0.00%
Other term deposits				
- EUR	1,684,280	1.13%	1,903,238	1.3%
- AMD	254,710	0.00%	7,995	-
Other accounts				
- AMD	23,055,151	4.25%	8,989,753	0.00%
- Other currencies	9,729,220	0.00%	39,699	0.00%
- AMD	-	-	3,756,770	4.75%
	180,475,805		203,820,395	
Due to the Government of the Republic of Armenia				
- AMD	106,545,573	10.00%	177,194,796	9.00%
- Other currencies	3,989,112	0.00%	1,329,188	0.00%
	110,534,685		178,523,984	
Liabilities to IMF				
- SDR	82,284,509	0.00%	95,263,527	0.50%
- AMD	195,802,721	0.00%	172,556,583	0.00%
	278,087,230		267,820,110	
Other borrowed funds				
- EUR	27,599,809	0.78%	28,309,397	0.60%
Other liabilities				
Demand deposits				
- AMD	531,068	14%	428,266	13.5%
Other liabilities				
- AMD	822,826	0.00%	425,036	0.00%
- Other currencies	146,096	0.00%	206,504	0.00%
	1,499,990		1,059,806	

30. Maturity analysis

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

AMD thousand

	2010						
	Less than 1 month	1 to 3 months	3 months to 1 year	1 year to 5 years	More than 5 years	No maturity	Total
Assets							
Cash	7,552,047	-	-	-	-	-	7,552,047
Placements with banks and financial institutions	119,902,034	32,748,474	5,451,593	-	-	-	158,102,101
Financial instruments at fair value through profit or loss	-	25,870,081	206,465,046	171,383,803	913,987	-	404,632,917
Loans and reverse repurchase agreements	6,704,810	3,201,300	2,179,257	56,109,584	2,420,548	-	70,615,499
Available-for-sale assets	-	-	56,636,853	1,533,497	9,597,802	20,938,530	88,706,682
Held-to-maturity investments	-	53,178,981	43,321,077	3,311,379	-	-	99,811,437
Placements with the IMF	12,176,896	-	-	-	51,493,341	-	63,670,237
Other assets	4,626,753	-	-	-	-	-	4,626,753
Total assets	**150,962,540**	**114,998,836**	**314,053,826**	**232,338,263**	**64,425,678**	**20,938,530**	**897,717,673**
Liabilities							
Notes and coins in circulation	-	-	-	-	-	348,164,734	348,164,734
Deposits and balances from financial and other institutions	180,475,805	-	-	-	-	-	180,475,805
Financial instruments at fair value through profit or loss	-	19,478	-	-	-	-	19,478
Due to the Government of the Republic of Armenia	56,421,717	54,112,968	-	-	-	-	110,534,685
Liabilities to IMF	120,364,074	-	8,523,491	147,798,146	1,401,519	-	278,087,230
Other borrowed funds	-	-	153,187	1,512,203	25,934,419	-	27,599,809
Other liabilities	1,499,990	-	-	-	-	-	1,499,990
Total liabilities	**358,761,586**	**54,132,446**	**8,676,678**	**149,310,349**	**27,335,938**	**348,164,734**	**946,381,731**
Net position as at 31 December 2010	**(207,799,046)**	**60,866,390**	**305,377,148**	**83,027,914**	**37,089,740**	**(327,226,204)**	**(48,664,058)**
Net position as at 31 December 2009	**(105,472,474)**	**57,931,511**	**135,008,730**	**188,812,602**	**42,913,665**	**(305,031,100)**	**14,162,934**

31. Currency analysis

The following table shows the currency structure of assets and liabilities at 31 December 2010:

AMD thousand

	AMD	USD	EUR	GBP
Assets				
Cash	-	7,504,401	47,562	15
Placements with banks and financial institutions	-	123,592,532	28,567,920	5,731,112
Financial instruments at fair value through profit or loss	-	225,999,443	178,633,474	-
Loans and other claims	70,615,499	-	-	-
Available-for-sale investments	88,705,765	-	917	-
Held-to-maturity investments	4,132,916	-	-	19,083,251
Placements with the IMF	-	-	-	-
Property and equipment	26,312,189	-	-	-
Intangible assets	583,179	-	-	-
Other assets	3,752,261	18	874,474	-
Total assets	**194,101,809**	**357,096,394**	**208,124,347**	**24,814,378**
Liabilities				
Notes and coins in circulation	348,164,734	-	-	-
Deposits and balances from banks and other financial institutions	80,825,771	74,409,429	25,240,577	26
Financial instruments at fair value through profit or loss	-	19,478	-	-
Due to the Government of the Republic of Armenia	106,545,573	1,533,121	2,455,991	-
Debt securities issued	-	-	-	-
Liabilities to IMF	195,802,721	-	-	-
Other borrowed funds	-	10,989,520	16,610,289	-
Other liabilities	1,353,894	143,076	2,983	-
Total liabilities	**732,692,693**	**87,094,624**	**44,309,840**	**26**
Net on balance sheet position as of 31 December 2010	**(538,590,884)**	**270,001,770**	**163,814,507**	**24,814,352**
Net on balance sheet position as of 31 December 2009	**(510,034,315)**	**344,311,158**	**159,392,138**	**26,420,598**

AMD thousand

	JPY	SDR	RUR	Other	Total
Assets					
Cash	-	-	-	69	7,552,047
Placements with banks and financial institutions	31.138	-	58,346	121,053	158,102,101
Financial instruments at fair value through profit or loss	-	-	-	-	404,632,917
Loans and other claims	-	-	-	-	70,615,499
Available-for-sale investments	-	-	-	-	88,706,682
Held-to-maturity investments	76,595,270	-	-	-	99,811,437
Placements with the IMF	-	63,670,237	-	-	63,670,237
Property and equipment	-		-	-	26,312,189
Intangible assets	-		-	-	583,179
Other assets	-		-	-	4,626,753
Total assets	**76,626,408**	**63,670,237**	**58,346**	**121,122**	**924,613,041**
Liabilities					
Notes and coins in circulation	-	-	-	-	348,164,734
Deposits and balances from banks and other financial institutions	-	-	2	-	180,475,805
Financial instruments at fair value through profit or loss	-	-	-	-	19,478
Due to the Government of the Republic of Armenia	-	-	-	-	110,534,685
Debt securities issued	-	-	-	-	-
Liabilities to IMF	-	82,284,509	-	-	278,087,230
Other borrowed funds	-	-	-	-	27,599,809
Other liabilities	-	-	37	-	1,499,990
Total liabilities	**-**	**82,284,509**	**39**	**-**	**946,381,731**
Net on balance sheet position as of 31 December 2010	**76,626,408**	**(18,614,272)**	**58,307**	**121,122**	**(21,768,690)**
Net on balance sheet position as of 31 December 2009	**2,489**	**6,357,797**	**32,728**	**3,871,035**	**30,353,628**

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