

**JSC Microfinance Organization
“CRYSTAL”**

*Financial Statements for the year ended 31 December 2007
and Independent Auditors' Report*

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საქართველოს აუდიტორული და საკონსულტაციო კომპანია
Georgian Audit & Consulting Company

A Horwarth Business Alliance Association

INDEPENDENT AUDITOR'S REPORT

To the Supervisory Board of the JSC Microfinance Organization "CRYSTAL"

We have audited the accompanying balance sheet of the **JSC Microfinance Organization "Crystal"** ("The Company") as of 31 December 2007, and related statements of income and cash flow for the year then ended. These financial statements are the responsibility of the Company's management. 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 and Georgian Legislation. Those Standards require that we plan and perform the audit in order to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the financial statements of the Company present fairly, in all material respects, the financial position of the Company as of December 31, 2007 and the results of its operations for the year then ended, in accordance with International Accounting Standards and requirements of Georgian legislation.

*Georgian Audit and Consulting Company
A Horwarth Business Alliance Associate*

February 12, 2008

GACC



**Joint Stock Company
Microfinance Organization “CRYSTAL”**

BALANCE SHEET

for the year ended December 31, 2007 (In GEL)

	notes	2007
ASSETS		
Current assets		
Cash	1	214,130
Gross loan portfolio	2	7,469,985
Loan loss reserve		(105,562)
Net loan portfolio		7,364,423
Interest receivable	3	107,624
Other current assets		45,012
Net current assets		<u>7,731,189</u>
Long-term assets		
Fixed assets, net	4	312,489
Intangible fixed assets, net	4	30,681
Participation in Other Organization	5	39,690
Deferred tax asset		89,266
Net long-term assets		<u>472,125</u>
TOTAL ASSETS		<u>8,203,314</u>
LIABILITIES & CAPITAL		
Current liabilities		
Accounts payable to suppliers		10,987
Short-term loan	6	1,196,455
Current portion of long-term loan	7	775,070
Accounts payable to founders	8	98,559
Tax payable	9	46,224
Interest payable		49,182
Total current liabilities		<u>2,176,477</u>
Long-term liabilities		
Long-term loan	10	4,405,483
Total long-term liabilities		<u>4,405,483</u>
Total liabilities		<u>6,581,960</u>
Equity		
Owner's equity	11	1,530,898
Current year's profit		90,456
Total equity		<u>1,621,354</u>
Total liabilities and equity		<u>8,203,314</u>

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

**Joint Stock Company
Microfinance Organization “CRYSTAL”**

INCOME STATEMENT

For the year ended December 31, 2007 (in GEL)

	Notes	2007
Revenues	12	
Interest revenue		708,228
Financial service fee		56,004
Penalties		36,650
Other revenues		11,380
Total revenues		<u>812,261</u>
Expenses	13	
General and administrative expenses		400,076
Interest expense		199,439
Taxes		15,872
Depreciation and amortization		33,220
Interest expense from written off loans		205
Exchange rate difference expense		17,540
Loan loss provision expenses		27,984
Audit and consulting		4,856
Total expenses		<u>699,192</u>
PROFIT/LOSS BEFORE TAXATION		<u>113,070</u>
Profit tax	14	<u>22,614</u>
NET PROFIT		<u>90,456</u>

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

**Joint Stock Company
Microfinance Organization “CRYSTAL”**

CASH FLOW STATEMENT

For the year ended December 31, 2007 (in GEL)

CASH FLOW FROM OPERATING ACTIVITIES	2007
Net profit	90,456
Adjustments:	
Cash investment	622,997
Depreciation and amortization	23,905
Net profit after Adjustments	<u>737,357</u>
Short-term accounts receivable	(3,030,165)
Paid advances	(3,952)
Interest receivable	(39,711)
Deffered tax asset	(7,738)
Short-term liability	188,412
Tax liability	46,224
Net cash flow from operating activities	<u><u>(2,109,573)</u></u>
CASH FLOW FROM INVESTMENT ACTIVITIES	
Changes in fixed assets	(6,996)
Changes in intangible fixed assets	(6,691)
Net cash flow from investing activities	<u><u>(13,687)</u></u>
CASH FLOW FROM FINANCIAL ACTIVITIES	
Sort-term loan	1,207,921
Long-term loan	1,129,469
Net cash flow from financial activities	<u><u>2,337,390</u></u>
Net cash flow	214,130
Cash balance at the beginning of the year	-
Cash balance at the end of the year	214,130

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

**Joint Stock Company
Microfinance Organization “CRYSTAL”**

CHANGES IN SHAREHOLDERS' EQUITY (In GEL)

	2007
Shareholders' equity at the beginning of the period	-
Emission of stocks	1,530,898
Net profit	90,456
Shareholders' equity at the end of the period	1,621,354

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

JSC Microfinance Organization “Crystal”
Notes to Financial Statements

NOTES TO FINANCIAL STATEMENTS

GENERAL INFORMATION

JSC Microfinance Organization “Crystal” (JSC MFO Crystal) was founded on August 23, 2007 on the basis of the decision of the “CRYSTAL” Fund (Board’s Resolution #20, August 21, 2007) according to the Georgian Law on Microfinance Organizations from July 18, 2006.

Company’s statutory capital is 1,530,898 GEL.

Statutory capital is divided into 1,530,898 ordinary shares with principal value of 1 GEL. Each Ordinary share entitles one vote to its owner at the General Meeting of Shareholders of the Joint Stock Company.

The legal address of the company is: # 72 Tamar Mepe St. Kutaisi, Georgia.

The supreme management body of the company is the General Meeting of Shareholders. Supervision of the company’s operations is conducted by the Supervisory Board, members of which are appointed by the General Meeting of Shareholders. Daily management of the company is carried out by the Director General appointed by the Supervisory Board.

The company is established with the purpose of making a profit on the basis of independent entrepreneurial activity. The company objects are to support and develop micro, small and medium businesses in Georgia, to improve the social and economic conditions of clients by providing them fast, easy and high-quality financial services.

Main activity of the Microfinance Organization “Crystal” is micro lending. Company’s financial products are: individual business loans, group loans, consumer loans, housing loans and long-term credit lines. In 2007 company conducted lending operation through its own loan capital and external lending.

The loan agreements with borrowers were made according to the loan products both in a foreign and national currency. Loan disbursements and repayments were made in national currency at the rate fixed by the National Bank of Georgia for the date of disbursement and repayment. Lending operation was fully conducted using bank accounts.

Company has a head office (Kutaisi), four branches (Kutaisi, Zugdidi, Poti, Tbilisi) and ten service centers (Kutaisi (3), Ozurgeti, Samtredia, Senaki, Khoni, Mestia, Chkhorotsku, Lanchkhuti). The lending operations are conducted through 4 partner banks and using 12 bank accounts.

**JSC Microfinance Organization “Crystal”
Notes to Financial Statements**

SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of presentation

The financial statements as of 31 December 2007 consist of JSC “Crystal” balance sheet and related statements of income, cash flows and changes in equity.

The financial statements have been prepared in accordance with International Accounting Standards (IAS) on the historical cost basis of accounting. The principal accounting policies adopted are set out below.

The accompanying financial statements have been prepared in the national currency of Georgia, Lari (GEL), which is the Company’s functional currency.

Cash

Cash includes cash on premises as well as cash on bank accounts.

Foreign currencies

Transactions denominated in foreign currency are translated into GEL at the official exchange rate of National Bank of Georgia on the date of transaction. The official exchange rate for the principal currency as of 31 December 2007 was:

	USD	EUR
GEL	1.5916	2.3315

Fixed assets

Tangible fixed assets are stated at historical cost less accumulated depreciation. An asset is considered a fixed asset when its useful life exceeds one year. Original historical cost of a fixed asset consists of purchase price, non-recoverable taxes and other expenses directly related to putting a fixed asset into use.

Fixed assets are considered on purchase value with deduction of depreciation. Cost of fixed assets purchase includes all charges which are related to putting an asset to use and achieving necessary condition. Charges connected to reparations are recognized as expense upon they have been incurred.

Value of liquidated and sold fixed assets and corresponding amount of depreciation is written off and reflected in the profit and loss account.

Depreciation is charged on the annual basis according to the historical cost for all fixed assets using the straight-line method. Rates for the main fixed asset groups are the following:

JSC Microfinance Organization “Crystal”
Notes to Financial Statements

Buildings	4 %
Vehicles	33 %
Furniture and equipments	33 %
Office equipments	25 %

The organization timely conducted inventory of goods according to the financial and administrative regulations and all fixed assets are appropriately marked.

Revenue and expense recognition

Revenues and expenses are recognized on the accrual basis.

Revenue consists of loan interest, fees for loan services (revenue from financial service), penalties and other revenue. Revenue also includes grants received from donor organizations and other revenues.

Recognition of revenues and expenses is made according to the requirements of IFAS.

Taxation

Social security contributions are recognized in the period, in which they arise. Under national tax regulations the company has to pay 20% of social tax on salaries.

The company pays property tax and a corporate profit tax of 20% is charged on the profit received from economic activities.

LOANS

Basis of presentation

Loans are presented as disbursed loans and provision for loan losses.

The loan loss provision in the balance sheet represents an estimate of possible loan losses based on the CGAP (Consultative Group to Assist the Poor) standards, which is one of the best in micro finance industry worldwide, as well as the historic analysis of loan losses conducted by the Company’s management.

Loans reserve policy

The provision for loan losses depends on delinquencies and the level of risk. Actual losses on loans may differ from the current estimate.

Considering the absence of reliable information on borrowers’ solvency, it is almost impossible to determine expected losses precisely. Despite these circumstances, the management of the company believes that it made the best possible estimate on possible losses on loans, and that the present amount of reserve is adequate.

**JSC Microfinance Organization “Crystal”
Notes to Financial Statements**

	Provisions rate
Net portfolio	1 %
Deferred loans	25 %
<i>overdue</i>	
1-30 days	25 %
31-90 days	50 %
91-180 days	75 %
181 days and more	100 %

Generally, calculation of loan loss provision is conducted on a monthly, quarterly and annual basis.

Loans write-off policy

JSC MFO „Crystal“ writes off loans only in the following cases:

- Owner of business dies and business stops functioning.
- Court receives appropriate decision.
- Delinquent loans for more then 180 days.

Loan prolongation policy

Loan prolongation is regulated by the Crystal’s Loan Methodology. According to the procedure, sometimes it is possible to make prolongation of loans within the repayment schedule (mainly before next payment). Any type of loan restructuring and refinancing is forbidden.

Prolonged loans are accounted in organization’s monthly program and financial accounts as a separate figure and the amount influences credit officers’ bonus and organization’s loan reserves.

Loan portfolio quality

a) Portfolio in Arrears as of December 31, 2007 (in GEL)

Delinquencies days	Kutaisi branch	Zugdidi branch	Poti branch	Tbilisi branch	All Total
1-30 days	5,481.22	518.85	219.13	42.40	6,261.59
31-60 days	1,908.47	223.60	941.91	-	3,073.98
61-90 days	1,416.36	31.27	177.67	-	1,625.31
91-180 days	1,889.99	471.80	1371.35	-	3,733.15
181 days and more	-	-	-	-	0.00
Total:	10,696.05	1,245.52	2,710.07	42.40	14,694.03

JSC Microfinance Organization “Crystal”
Notes to Financial Statements

b) Portfolio at risk as of December 31, 2007 (in GEL)

Delinquencies days	Kutaisi branch	Zugdidi branch	Poti branch	Tbilisi branch	All Total
1-30 days	54,036.94	2,799.86	6,004.23	1,166.48	64,007.52
31-60 days	11,841.22	1,259.04	4,978.64	-	18,078.89
61-90 days	5,143.94	31.27	422.71	-	5,597.93
91-180 days	2,757.37	471.80	1,882.83	-	5,112.00
181 days and more	-	-	-	-	0.00
Total:	73,779.46	4,561.97	13,288.41	1,166.48	92,796.33

c) Loan write-offs during the year as of December 31, 2007 years (in GEL)

	Kutaisi branch	Zugdidi branch	Poti branch	Tbilisi branch	All Total
Write off loans	11,221.64	37,609.28	91,008.60	-	139,839.52
Restored loans	4,041.61	50,788.16	12,279.89	-	67,109.66
Loan write-offs	7,180.03	(13,178.88)	78,728.71	-	72,729.86

* In Zugdidi branch there is an excess of returned previously written off loans to current year write-offs.

Insider loans

From October of 2005 “Crystal“ started issuing loans to “insiders”. Insider loans are made according to policy which strictly defines the limit of borrowing

Interest accrual on overdue loans

Interest is accrued on overdue loans for the loan repayment period defined by loan agreement. After expiration of this period the interest is not accrued.

Risk management policies

Management of risk is fundamental to the microfinance organization and is an essential element of the operations. The main risks inherent to the company’s operations are related to credit, liquidity and market changes (interests and foreign exchange rates). Risk management policies of the company are tailored to unpredictable financial market and the main goal of the policy is to reduce impact to the minimal level. Risk management is accomplished by the senior management under the supervision of the Supervisory Board.

Liquidity risk

Liquidity risk is controlled by the company’s management. As of December 31, 2007 management believes, there is no substantial liquidity risk, because of high liquidity of current assets.

JSC Microfinance Organization “Crystal”
Notes to Financial Statements

Credit risk

Organization is exposed to credit risk which occurs if the borrower is unable to repay the loan amount within the agreed schedule. The management regularly conducts an analysis of borrowers and market opportunities. Large part of loan portfolio is held in hard currency (appropriate USD rate in GEL). Also, important part of loans is secured by different types of collateral, which significantly reduces credit risk.

Market risk

Company is exposed to market risk related to currency exchange and interest rate fluctuation. Management with the Supervisory Board establishes the risk limit, which is monitored on the regular basis. Despite, company cannot fully avoid such risks in case of significant changes on the market.

1. Cash

Cash of the JSC for the year ended December 31 2007

	2007
	(GEL)
Cash in hand	697
Cash in bank	213,433
Total:	<u>214,130</u>

2. Loans

Loan portfolio by types of loans in GEL:

	2007
	(GEL)
Loan portfolio total	
Individual Loans	3,733,966
Group loans	15,112
Credit line	84,565
Housing Loans	467,991
Consumer loans	<u>3,168,351</u>
Total loan portfolio	<u>7,469,985</u>
Loan loss reserve	<u>(105,562)</u>
Net loan portfolio	<u>7,364,423</u>

**JSC Microfinance Organization “Crystal”
Notes to Financial Statements**

3. *Interests receivable*

In the balance sheet the interest receivable (107,624GEL) is presented as an amount, which was accrued as of December 31, 2007 but not then received.

4. *Fixed and Intangible Assets*

Schedule below represents changes in fixed assets during 2007 and their structure as of December 31:

	Buildings	Office equipment	Furniture	Vehicles	Property Improvement	Total	Intangible assets
Historical value							
31 December, 2006	-	-	-	-	-	-	
Acquisition	131,091	198,055	49,773	48,615	10,713	438,247	43,331
Liquidation and write off		(2,751)	(740)	(14,801)		(18,292)	
31 December, 2007	131,091	195,304	49,033	33,814	10,713	419,955	43,331
Accumulated depreciation at time of transfer							10,382
Accrued during the period	8,679	46,799	15,177	14,562	612	85,829	
Liquidation and write off	1,413	20,737	4,964	2,581	1,258	30,953	2,268
31 December, 2007	10,092	64,835	19,407	11,263	1,870	107,466	12,650
Net balance value							
31 December, 2007	120,999	130,469	29,627	22,551	8,843	312,489	30,681

5. *Participation in other Organization*

The amount represents company’s investment in tea enterprises: 25% share with the value of 18,290 GEL (10,000 USD) in the „Georgian Teruar Tea LLC” which was made in February of 2006, and 45% share with the value of 21,400 GEL in “Thernali Tea LLC” accomplished in 2007.

JSC Microfinance Organization “Crystal”
Notes to Financial Statements

6. Short-term loans

Short-term loans include:

- a) Loan from the Charity Humanitarian Center „Abkhazeti”, in amount of 58,715 GEL as of December 31, 2007;
- b) Credit from TBC BANK – 1,137,740 GEL, which itself includes 300,000 GEL as an overdraft facility and 837,740 GEL one year loan. Payment is made in the monthly basis.

7. Current portion of long-term loan

Current portion of the long-term liabilities 775,070 GEL comprises the following:

- 1. Part of the loan received from Dutch organization ”CordAid” in 2004-2005 (84,000 USD), which should be repaid in 2008 (133,694 GEL). Loan period is 4 years. Payments of principal and interest are made every 6 months;
- 2. Part of a long-term loan of 100,000 USD (159,160 GEL) received in 2006 from Dutch organization ”Oikocredit”. This loan should be covered in 2008. Credit is received for 3.5 years. Payments are made semi-annually;
- 3. Loan received in 2006 from Dutch organization ”Novib” in amount of 466,300 GEL, for 2 years. The loan has been fully repaid in January 2008;
- 4. Interest free loan (10,000 USD – 15,916 GEL) received from Mr. Keith Young, UK citizen purposefully to support investment in Georgian tea business.

8. Liabilities to founders

It should be noted that according to Georgian tax legislation transfer of existing tax liability or tax credit to other entities is prohibited. Founder company at the moment of establishment of JSC ”CRYSTAL” had such a liability, which could not be transferred to the subsidiary. Therefore, the liability to the founder makes up 98,558 GEL.

9. Tax liabilities

Tax liabilities in 31 December, 2007 include:

	2007
	(GEL)
Income tax	30,352
Personal income tax	14,711
Property tax	1,161
Total:	<u>46,224</u>

**JSC Microfinance Organization “Crystal”
Notes to Financial Statements**

10. Long-term loans

Long-term loans comprises:

1. Part of loan from Dutch organization ”CordAid” which will be repaid in next period of 2008 (267,322.70 GEL).
2. Part of loan of Dutch organization ”Oikocredit” which will be repaid in 2008 (159,160 – 100,000 USD).
3. In 2006-2007 organization received credit line of 2 million USD from the US-based financial organization „Deutsche Bank Micro Finance Consortium”. Duration of the credit line is 4,5 years. Interest payment is made every year, twice a year. Principle amount will be repaid in 2010. Liability as of December 31, 2007 amounts 3,183,200 GEL (2 million USD).
4. In 2007 the loan was received from Dutch Public limited company ”Pettelaar Effectenbewaarbedrijf N.V.” in amount of 500,000 USD for 3 yaers. Interest payment is made twice in a year, while principal payment is made at the end of the period.

11. Owner’s Equity

In result of reorganization of “Crystal” Fund, in August 23 of 2007 the JSC ”Crystal” was established which acquired all assets and liabilities of the founder organization. the statutory capital was evaluated as of August 13, 2007 and its value was 1,530,898 GEL, including:

Loans	4,174,874	GEL
Minus loans loss reserve	(75,983)	GEL
Net loans	4,098,891	GEL
Interest receivable	82,835	GEL
Other current assets	42,706	GEL
Fixed assets	331,197	GEL
Intangible assets	26,790	GEL
Other long-term assets	121,612	GEL
<hr/>		
Total assets	4,704,031	GEL
Credit liabilities	3,461,476	GEL
Interest liabilities	50,619	GEL
Other short-term liabilities	5,560	GEL
<hr/>		
Total liabilities	3,517,655	GEL
Total contribution to the statutory Capital taking account of liabilities	1,530,898	GEL

JSC Microfinance Organization “Crystal”
Notes to Financial Statements

12. Revenues

Interest Revenue

Interest revenue is recognized in income statement on the accrual basis. Interest revenue represents interests on disbursed loans. Depending on the type and the amount of loan the Interest rates can be fixed (flat) or declining from 18% to 36% per annum. Customers taking flat interest rate loans receive the benefit in case of earlier repayment of the loan (20% of total interest).

Revenue from financial services

Revenue from financial services (56,004 GEL) comprises: commission fees paid by borrowers (1-2% of disbursed loan), except group loan recipients for the loan disbursement procedures and commission fee paid by partner trading organizations for the financial services, which is paid every month on basis of presented invoices.

Revenue from penalties

Revenue from penalties (36,650.11 GEL) includes amount, which is paid by borrowers in case of violating the loan agreement. The penalty is paid only for the principal amount and makes up 2% on every overdue day. Penalty payment from borrower goes to company's bank account. If client informs company in advance in writing concerning the possible delay in payment he/she may receive a privilege not to pay the penalty, but this is strictly limited for each borrower and credit officer.

Other revenues

Other revenues (11,279.60 GEL) include the revenue received from internships. Organization offers 3 month education services for interns. Each intern pays 50 GEL per month. Other revenues also include the revenue from sale of fixed assets. Sale of two company vehicles was carried out on basis of tender in accordance to policies and procedures.

JSC Microfinance Organization “Crystal”
Notes to Financial Statements

13. Expenses

General and Administrative expenses for the year ended 2007

	2007
	(GEL)
Salary	214,710
Interest expenses	199,439
Social benefits	42,942
Other tax expenses	38,669
Depreciation and amortization	33,220
Other general expenses	27,984
Bank fees	18,400
Currency difference expense	17,540
Office Rent	16,900
Taxes	15,872
Petrol and Oil expenses	14,808
Advertisement	10,255
Car rent	9,088
Commission fees for taking loans	8,894
Communication	8,292
Audit and consulting services fees	4,856
Stationery	4,680
Business trips	3,973
Reparation expenses	2,918
Operational expenses	2,405
Electricity	1,309
Utilities (natural gas, recycling, water)	702
Insurance expense	573
Representative expense	558
Interest expenses from written off loans	205
Total :	<u>699,192</u>

14. Profit tax

The organization pays the profit tax at 20% rate. In 2007 profit before taxation was 151.762 GEL.

Calculation of 2007 profit tax:

**JSC Microfinance Organization “Crystal”
Notes to Financial Statements**

Profit before taxation	151,762
	<u>20%</u>
	30,352
<i>Temporary differences</i>	
Revenue from soft loans and sale of fixed assets	8,230
Depreciation and amortization	(19,814)
Loan loss provision expense	(27,984)
Fixed assets expenses up to 1000 GEL	10,588
Other general expenses	<u>(9,711)</u>
Total:	(38,692)
Deferred tax asset (liability)	(7,738)
Profit tax	<u><u>22,614</u></u>

Deferred tax asset

Deferred tax liability - 7,738 GEL occurred on basis of difference in recognition of expenses and revenues by tax legislation and financial accounting standards.

15. Legal Environment

Since 2008 amendments were introduced to the Tax Code of Georgia. In result, the social tax was abolished (20%), while personal income tax was increased from 12% to 25%. Income tax was reduced from 20% to 15%. Physical persons have been freed from the property tax related to rented property, but legal person are obliged to pay the property tax for property rented from physical person.

According to the amendments made in February 25, 2005 in the Civil Code of Georgia the status of microfinance organization was defined.

On July 18, 2006 a new Law on Micro Finance Organizations was adopted which allowed organizations operating micro-lending activities to register as microfinance organizations and conduct their activities in frames of the established law and regulations.

16. Organization’s functionality

JSC “Crystal” was established on August 23, 2007 in Kutaisi (registration # 212896570) according to the Georgian Civil Code, company laws and Georgian law on Micro Finance Organizations. On September 18, 2007 “Crystal” was registered by the National Bank of Georgia. At the end 2007 there is no any risk, which will make doubtful company’s future functionality.
