

EXTERNAL ENVIRONMENT

Macroeconomic Prerequisites

In recent years the Republic of Armenia demonstrated stable economic growth and expansion of external economic activity, as well as underpinning and development of the financial sector. Meanwhile, the year 2008 was marked by a slowdown in the pace of development, which was a consequence of the processes taking place in the world.

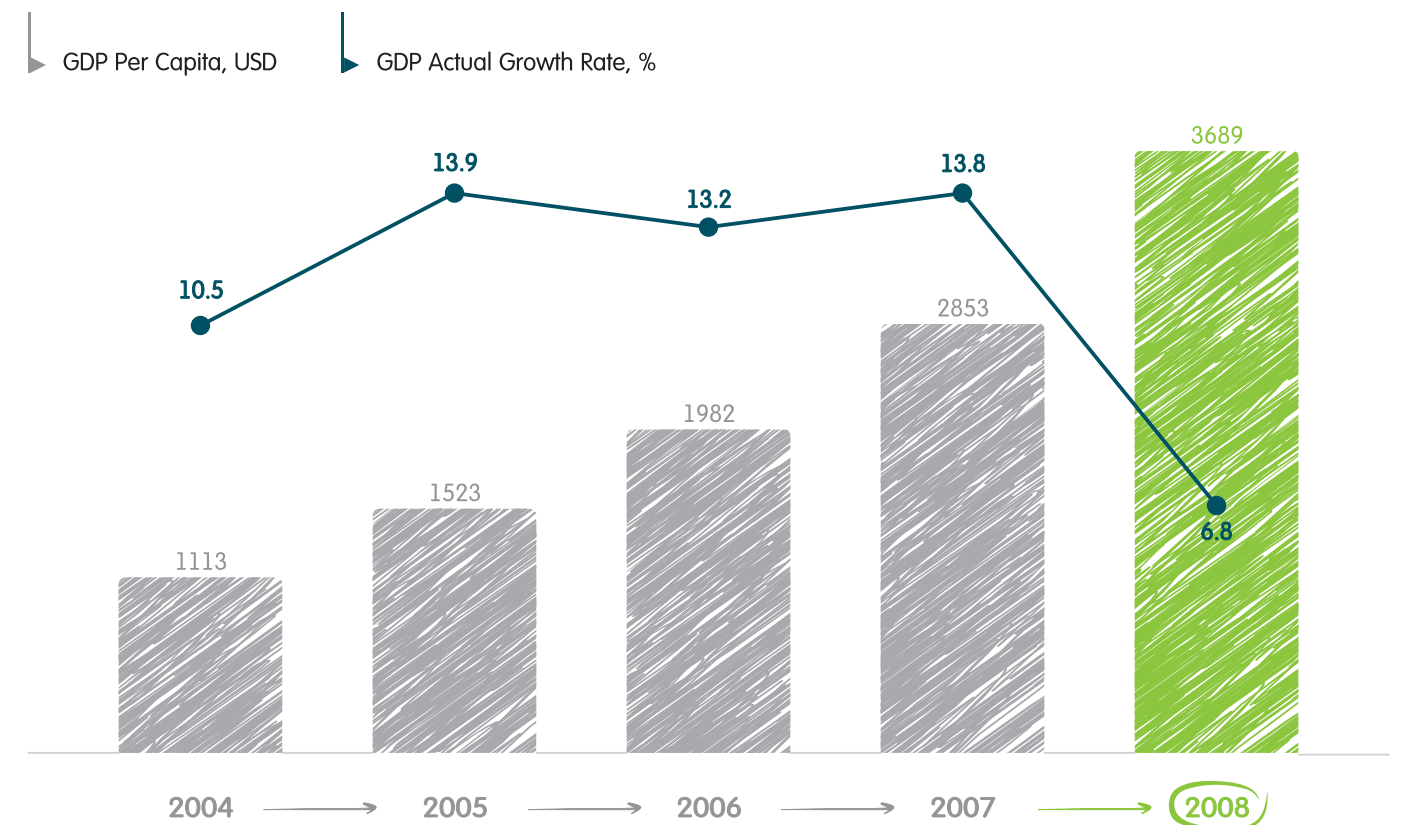
The key external factors, which substantially influenced the economic situation in Armenia in 2008 were:

- ▶ decrease in demand and drop of global prices for products constituting the major part of the commodity composition of Armenian export, specifically: copper, molybdenum, aluminum, gold, caoutchouc, precious metals, stones and jewelry
- ▶ floating interest rates in international markets
- ▶ volatility of exchange rates
- ▶ uncertainty of further developments

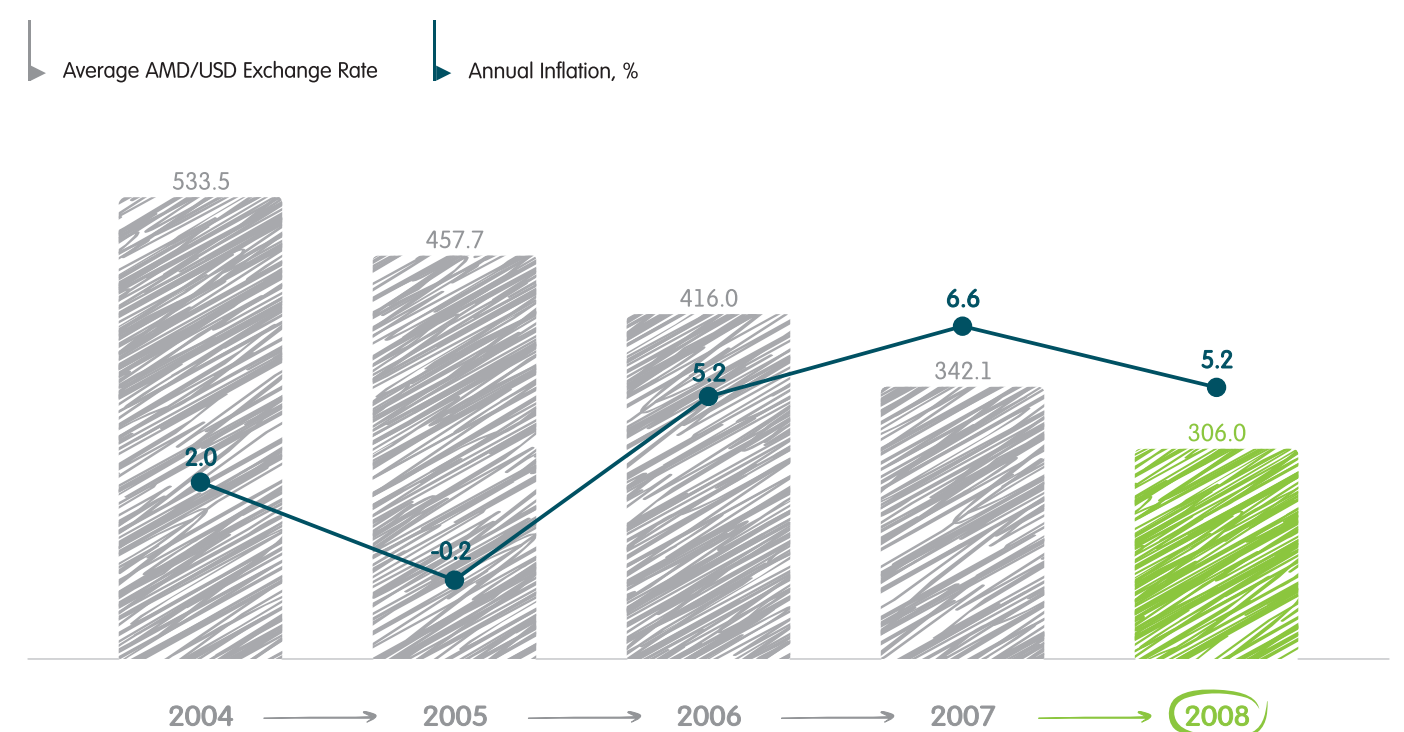
The impact of the global crisis on Armenia's economy became more apparent during the last months of 2008. It mostly affected the export industries.

- ▶ Not only metal mining industries but companies chiefly exporting their production found themselves in a difficult situation.
- ▶ In view of current global economic processes, a considerable slowdown of economic growth in Armenia was registered. The economic growth, previously reaching two-digit figures, amounted to only 6.8%, as to the real growth of industrial manufacturing, it was 5.4%.
- ▶ The current balance of payments deficit increased to account for 11.4% of GDP as compared with 6.4% in 2007. The increase of this indicator was chiefly due to a growth in the negative external trade balance, which in 2008 totaled USD 3.3 bln.
- ▶ Against this background the average AMD/USD rate in 2008 rose by almost 12% as compared with 2007.

Economic Growth and GDP per Capita



Inflation and AMD Value



Legislation, Monetary Policy, Financial Infrastructure

Armenia's banking system is to a considerable extent ahead of the other countries in the region in terms of supervision and corporate governance. The banking legislation of Armenia is considered to be one of the most perfect sets of legislation throughout the post Soviet territory.

As early as in the beginning of 2005, the CBA adopted a conceptual decision on gradual transition to "Basel II". An important precondition for this shift was the implementation of the corporate governance concept in the banking system starting from July 1, 2006. Starting from January 1, 2008, the banking capital benchmark was aligned with the new Basel standards.

Amendments to the financial legislation, which took effect in 2008, were targeted not only at further development of the banking system and economy of the country on the whole, but at strengthening the protection of rights of commercial banks' clients.

Three fundamental laws enacted by the parliament of Armenia should be highlighted: the Law "On Financial Ombudsman", the Law "On Consumer Loans" and the Law "On Attraction of Bank Deposits".

In 2008 the new Law "On Securities Market" enacted on October 11, 2007 triggered activation in the Stock Market of Armenia. Amendments incorporated as per the new law enabled banks and credit organizations to operate in the securities market directly, without a special license. Furthermore, the Central Depository and the Stock Exchange were granted the status of commercial organizations.

Along with this, the new law created prerequisites, due to which the Swedish Stock Exchange operator OMX Group acquired 100% interest in the Armenian Stock Exchange (ASE) and the Central Depository (CDA) in January 2008. After NASDAQ merged with OMX in March, 2008, NASDAQ OMX Group, Inc. became the sole shareholder of ASE and CDA. The latter were reorganized through integration into the global NASDAQ OMX structure.

During 2008 all rules of ASE and CDA were reviewed and aligned with those effective in stock exchanges and depositories operating under NASDAQ OMX Group.

Due to radical changes in the stock market, in 2008 11 emissions of corporate bonds took place in Armenia, most of which were listed in the Stock Exchange. On the whole, it may be stated that the Legislation of Armenia is rather favorable in regard to the securities market. Currently amendments are being incorporated, which may to a great extent promote the capital market in Armenia. These amendments are implemented through granting tax benefits to companies listed in the Stock Exchange and through pension reforms, etc.

During 2008 definite steps were taken towards establishment of a mortgage company and fund. The Central Bank of the Republic of Armenia provided AMD 5 bln (USD 16.3 mln) to create a mortgage fund in 2009.

In 2008 the Insurance Market of Armenia also underwent serious reforms. Availability of a modern insurance system is one of the preconditions to ensure efficient social security for the population.

- ▶ motor vehicle liability insurance against third parties
- ▶ medical insurance

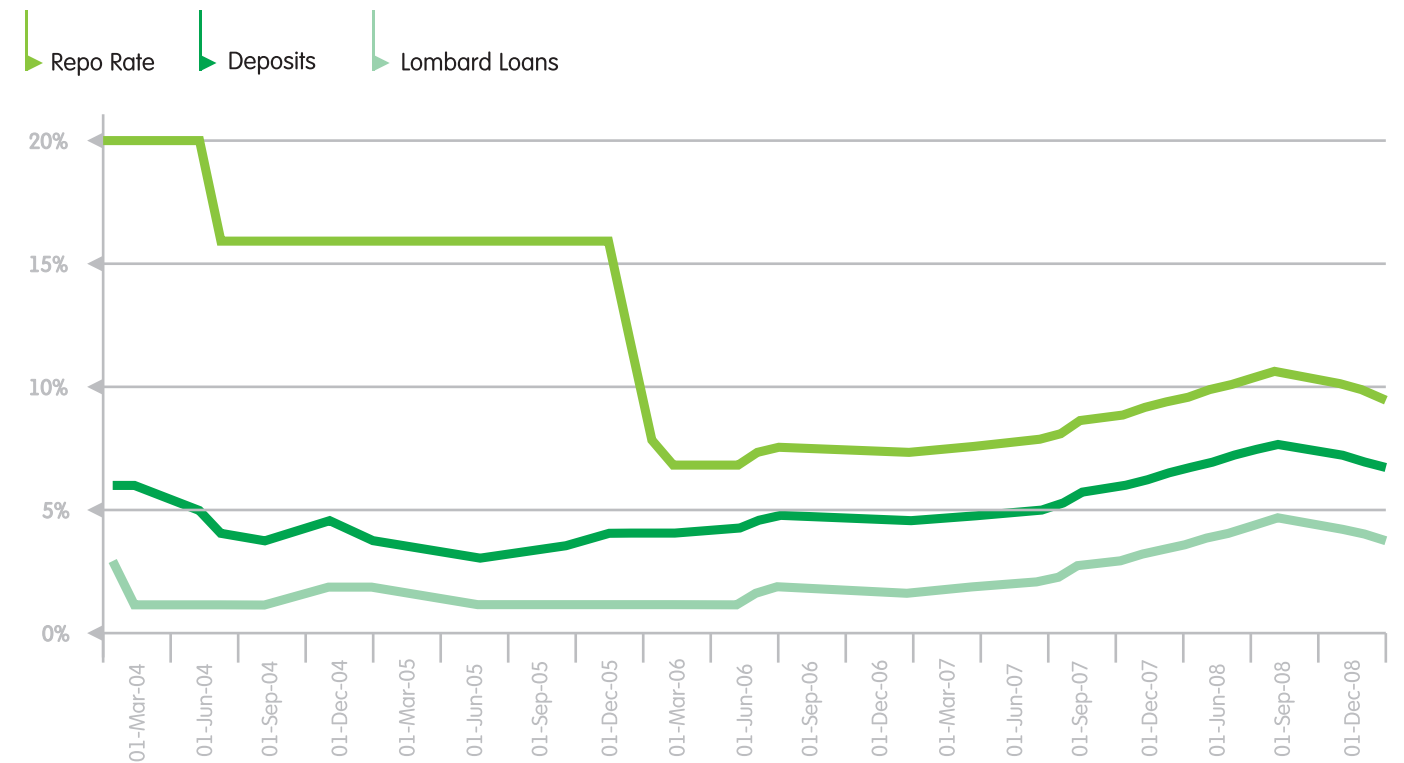
In 2008 the newly enacted Law "On Insurance" triggered activation in the insurance market. Pursuant to the new law, the restrictions on foreign investor participation in the statutory funds of domestic insurance companies were removed (restrictions on foreign participation in resident insurance companies were removed a year earlier). As per the previous law, foreign participation in insurance companies of Armenia should not exceed 49%.

On the whole, the insurance market in the country progressed to a great extent.

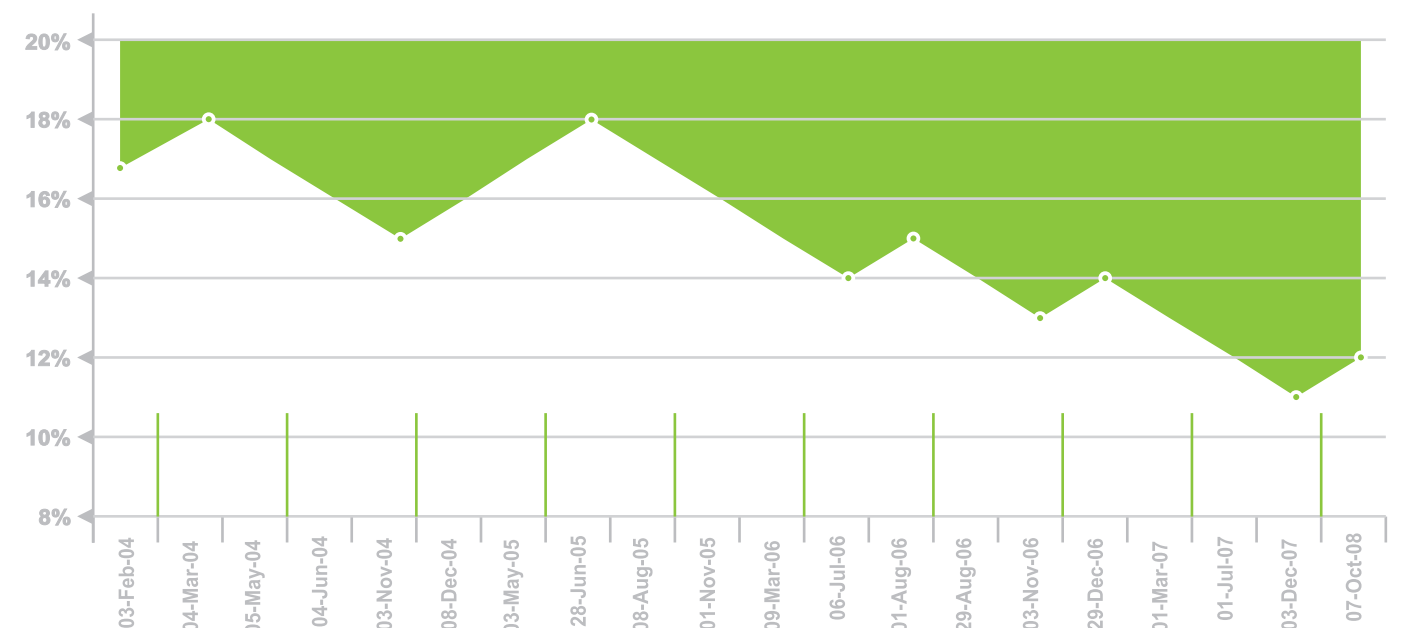
The main objective of all economic reforms implemented by the Government of Armenia is ensuring stable economic growth. A constituent part of the economic policy, the monetary policy of the Central Bank in its turn contributes to accomplishment of this end through attaining its own main objective, i.e. ensuring price stability in the economy of the country. For this purpose in 2008, the CBA proceeded with the strategy of shifting to full inflation targeting. It should be pointed out that Armenia is the first CIS country the Central Bank of which since January 2006 has switched to a new inflation control policy, i.e. targeting, where interest rates, particularly the refinancing rate, are the main tools.

In the sphere of regulation and control of the financial system the Central Bank persisted with the strategy of shifting from institute-based supervision over the financial system to functional control.

Dynamics of Interest Rates as per CBA Instruments



Banking Rate



The Financial Sector and Ameriabank's Position in the Banking System of the RA

The financial sector of Armenia appears to be one of the most stable in the country's economy. Weak integration of financial organizations in international processes on the one hand and positive economic growth, large-scale foreign investments on the other are indicative of strong potential for development. In this regard the role of the banking system should not be underestimated.

- ▶ The surging development of Armenia's banking sector carried through the previous year.
- ▶ The total assets of the banking system as of yearend increased by 34% to pass the USD 3.3 bln threshold. The capital increased by 37% to reach USD 769 mln.
- ▶ The volume of lending to the economy increased by 48% in 2008. Loans to organizations comprise 28.3% and those to individuals are 30.1% of the banks' assets.
- ▶ Despite the rather low level of financial intermediation in the banking system, in recent years a trend was registered of stable and smooth growth of the banking sector's role in the country's economy.

It should be noted that along with the change of the shareholder, review of the main development scenarios, enhancement of product mix and new tariff policy, the attitude of the population towards the Bank has changed too. This is evidenced by a tangible upsurge in lending and augmentation of the resource base of Ameriabank due to not only capitalization growth, but also a substantial increase in funds attracted from individuals and legal entities as time and demand deposits.

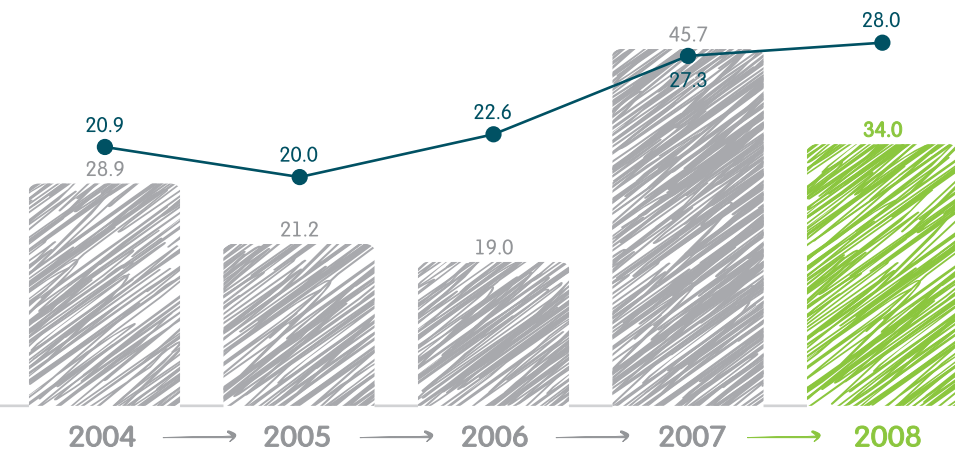
This is indicative of growth of the Bank's recognition as an upgraded modern financial institution and of increase of trust to the Bank.

Against the favorable macroeconomic background, the banking sector of Armenia demonstrated not only a high level of financial stability in the first half of 2008 but also rather high profitability. Profit and ROA, ROE indicators were on a high level. Profit of the banks as of the end of 2008 (less profit/loss of the previous years) increased by 30.5% as compared with the same benchmarks of the previous year. Only three out of 22 banks in Armenia have been operating at a loss. ROE in 2008 accounted for about 14%, and ROA – 3.1%.

In light of the global financial crisis in the second half of 2008, all Armenian commercial banks reviewed their lending policies, as new risks which needed to be taken into account emerged under the new conditions. In particular, banks have toughened the lending terms, giving preference mainly to large taxpayers, and started not only paying more attention to the financial position of enterprises to which loans are advanced, but also thoroughly monitoring the relationship of borrowers with the government.

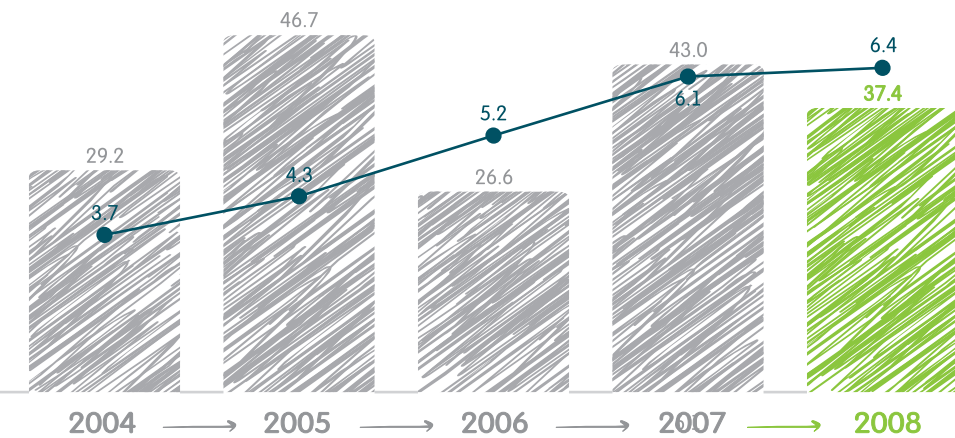
Assets of Armenia's Banking System

- ▶ Assets, % of GDP
- ▶ Growth of Assets, Y-o-Y, %



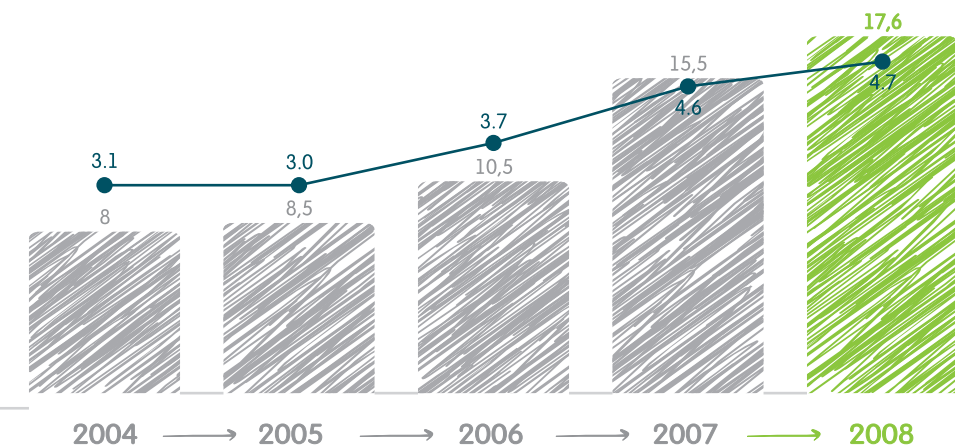
Growth Rates of the Total Capital of Armenia's Banking System

- ▶ Capital, % of GDP
- ▶ Growth of Capital, Y-o-Y, %

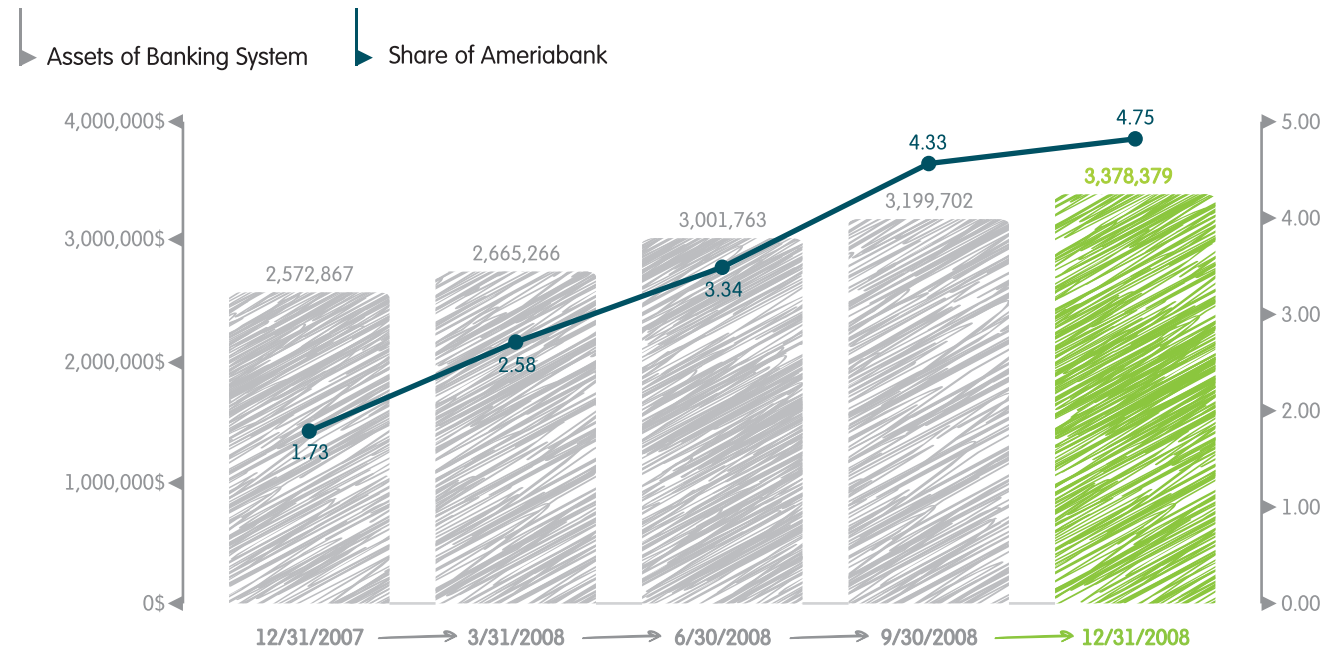


Lending to Economy and Deposits of Population

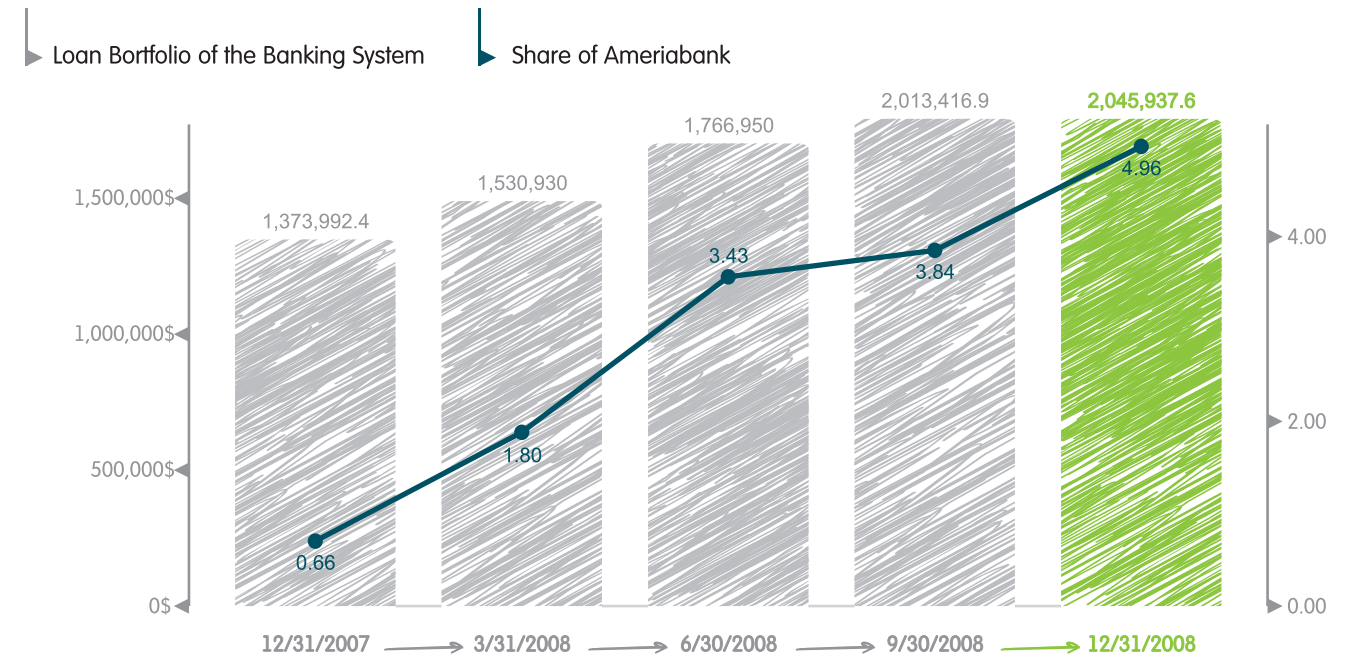
- ▶ Loans to Economy, % of GDP
- ▶ Growth of Deposits, Y-o-Y, %



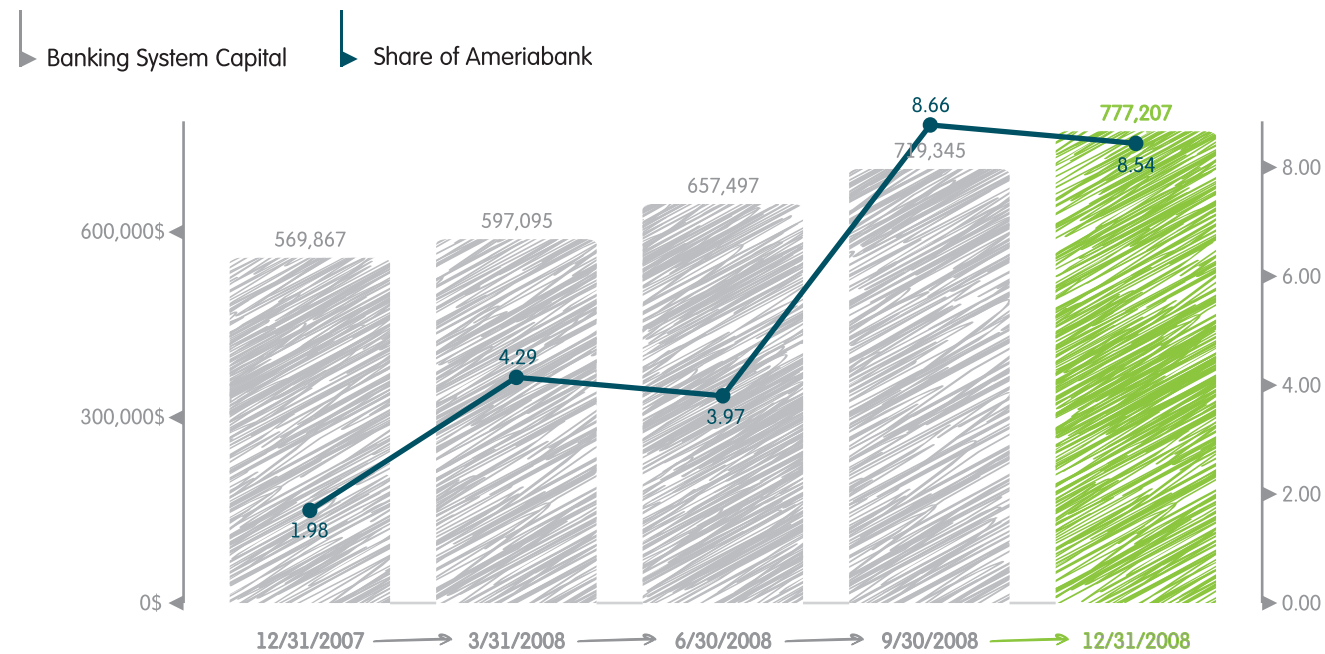
Dynamics of Ameriabank's Share in the Banking System by Assets in 2008



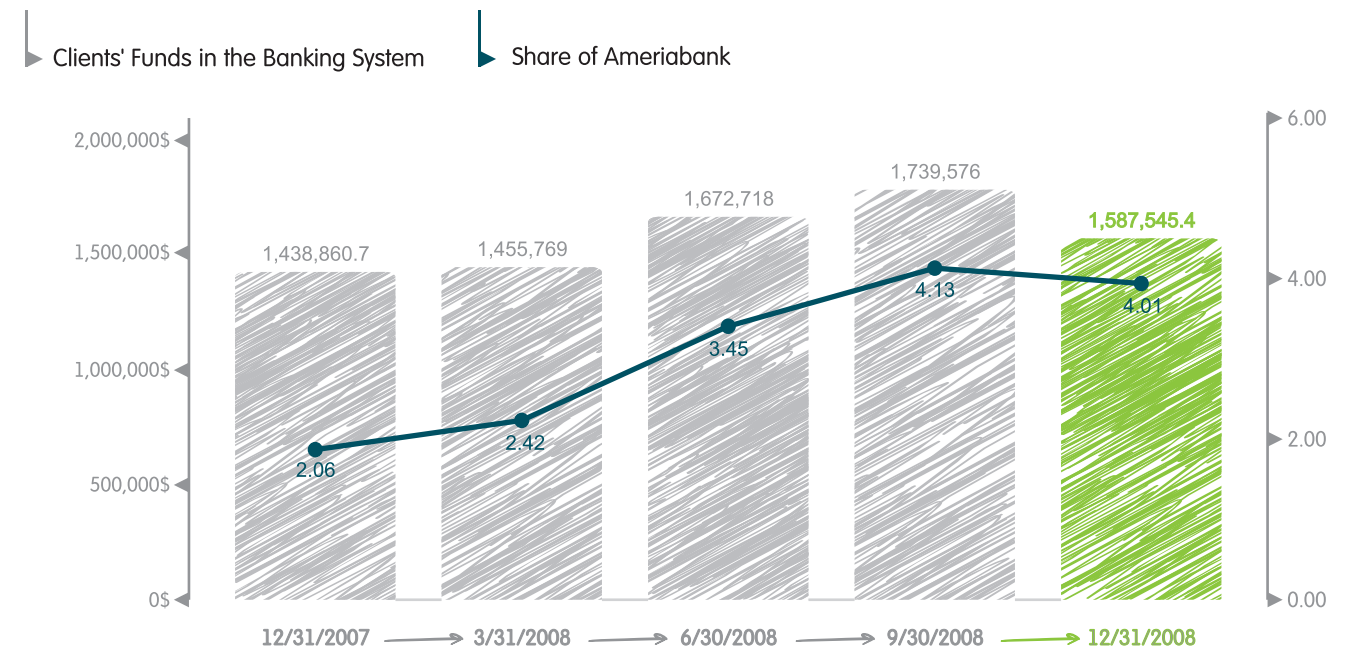
Dynamics of Ameriabank's Share by Lending in 2008



Dynamics of Ameriabank's Share by Capital in 2008



Dynamics of Ameriabank's Share by Deposits in 2008



- ▶ In view of the continuous development of Armenia's banking sector, rapid growth of key indicators of Ameriabank was registered during the last year. This was due to the change of the shareholder and the designing of an essentially new development strategy,, which is indicative of development potential and the Bank's target of attaining leadership in the market. The comparative dynamics of the Bank's development during 2008 are the evidence of the above.
- ▶ In 2008 the assets of Armenia's banking system increased by 34%, while those of Ameriabank increased by 3.64 times. As a result of this the Bank's share in the banking system increased from 1.7% to 4.7% within a year.
- ▶ In 2008 the total capital of Armenia's banking system increased by 37.4%, and that of Ameriabank increased by 5.9 times. As a result of this the Bank's share in the banking system by total capital increased from 2% to 8.5% within a year.

- ▶ In 2008 the loan portfolio of Armenia's banking system increased by almost 50%, while the volumes of lending to the economy by Ameriabank increased by 11.3 times. As a result of this the Bank's share in the banking system by loan portfolio increased from 0.7% to 5% within a year.
- ▶ In 2008 total deposits of Armenia's banking system increased by 11.2%, while the volumes of deposits attracted by Ameriabank increased by 2.2 times. As a result of this the Bank's share in the market by funds attracted from clients increased from 2.1% to 4% within a year.