

R. Poudel & Co.

Chartered Accountants

AUDITOR'S REPORT TO THE SHAREHOLDERS OF MACHHAPUCHCHHRE BANK LIMITED

1. We have audited the accompanying Balance Sheet of Machhapuchchhre Bank Limited as of Ashad 31, 2062 (July 15, 2005), and the related Statement of Income, and Cash Flows for the year then ended. These financial statements are the responsibility of the Bank's management. Our responsibility is to express an opinion on these financial statements based on our audit.
2. We conducted our audit in accordance with Nepal Standards on Auditing or other applicable standards. Those Standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.
3. On the basis of our examination, we would like to report that:
 - i. We have obtained all the information and explanations, which to the best of our knowledge and belief were necessary for the purpose for our audit.
 - ii. The Balance Sheet, Cash Flow Statement, Income Statement and attached Schedules dealt with by this report are in agreement with the books of account maintained by the Bank.
 - iii. In our opinion, proper books of accounts as required by law have been kept by the Bank in so far as it appears from our examination of those books of account.
 - iv. The returns received from branches of the Bank were adequate for the purpose of our audit.
 - v. In our opinion and to the best of our information and according to the explanations given to us and from our examination of the books of account of the Bank, we have not come across the cases where the Board of Directors or any member thereof or any employee of the Bank has acted contrary to the provisions of law or caused loss or damage to the Bank.
4. In our opinion, the financial statements give a true and fair view of the financial position of the Bank as of Ashad 31, 2062(July 15, 2005), and of the results of its operations and its cash flows for the year then ended in accordance with applicable Accounting Standards and comply with Company Act 2053, Bank and Financial Institutional Ordinance, 2062 and Nepal Rastra Bank's Directives.
5. In addition to above report, we further report that:
 - i. The Bank has made provision for possible losses in its investment as per Nepal Rastra Bank's directives,
 - ii. The operations of the Bank were within its jurisdiction,
 - iii. The Bank has acted as per Nepal Rastra Bank's directives, and
 - iv. The operations were carried out in the interest of the Bank and its depositors.

Sd. Rajesh Poudel, FCA
R. Poudel & Co
Chartered Accountants

MACHHAPUCHCHHRE BANK LIMITED

BALANCE SHEET AS AT 31 ASHADH 2062 (JULY 15, 2005)

CAPITAL AND LIABILITIES			
Previous Year Rs.	Particulars	Schedule	This Year Rs.
550,000,000.00	1. Share Capital	1	550,000,000.00
4,221,843.14	2. Reserves and Funds	2	87,739,384.31
102,167,330.15	3. Borrowings	3	154,217,473.95
2,754,632,089.65	4. Deposits	4	5,586,802,644.09
5,135,728.39	5. Bills Payable	5	9,327,537.95
32,477,259.67	6. Other Liabilities	6	68,373,780.29
3,448,634,251.00	Total Capital and Liabilities		6,456,460,820.59

ASSETS			
Previous Year Rs.	Particulars	Schedule	This Year Rs.
65,256,535.68	1. Cash Balance	7	121,550,140.40
345,488,631.64	2. Balance with Banks	8	609,583,135.59
150,000,000.00	3. Money at Call and Short Notice	9	15,000,000.00
274,406,945.26	4. Investments	10	468,612,174.63
2,493,107,931.72	5. Loans, Advances and Bills Purchased	11	5,061,433,055.67
62,412,573.50	6. Fixed Assets	12	86,212,339.78
57,961,633.20	7. Other Assets	13	94,069,974.52
3,448,634,251.00	Total Assets		6,456,460,820.59

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MACHHAPUCHCHHRE BANK LIMITED

**PROFIT AND LOSS ACCOUNT FOR THE PERIOD OF
1st Srawan to 31 Ashadh 2062 (16 JULY 2004 TO 15 JULY 2005)**

EXPENSES			
Previous Year Rs.	Particulars	Schedule	This Year Rs.
113,579,092.57	1. Interest Expenses	15	187,027,981.93
19,872,459.80	2. Employees Expenses	16	29,581,861.23
42,357,601.73	3. Office Overhead Expenses	17	59,973,169.84
-	4. Exchange Loss	20	-
2,259.51	5. Non Operating Expenses	21	-
-	6. Bad Debts Written Off		-
	7. Provision for Non Banking Assets		1,451,250.00
15,980,436.11	7. Provision for Loan Loss	11	21,455,883.28
5,187,771.70	8. Provision for Staff Bonus		12,868,390.67
-	9. Provision for Income Tax		30,945,488.72
46,689,945.30	10. Net Profit Carried Down		84,870,027.30
243,669,566.72	Total		428,174,052.97

INCOMES			
Previous Year Rs.	Particulars	Schedule	This Year Rs.
215,206,843.76	1. Interest Income	18	381,930,447.91
14,840,269.37	2. Commission and Discount	19	21,391,062.43
12,621,092.27	3. Exchange Gain	20	11,359,386.97
-	4. Non Operating Incomes	21	286,968.96
1,001,361.32	5. Other Incomes	22	13,206,186.70
-	6. Net Loss Carried Down		-
243,669,566.72	Total		428,174,052.97

**PROFIT AND LOSS APPROPRIATION ACCOUNT
FISCAL YEAR 2061/62 (2004/05)**

Previous Year Rs.	Particulars	This Year Rs.
45,529,599.32	1. Accumulated Loss up to Last Year	9,530,129.21
-	2. Loss for the Year	-
9,337,989.06	3. General Reserve Fund	16,974,005.46
-	4. Contingent Reserve	-
-	5. Banking Development Fund	-
-	6. Dividend Equalization Fund	-
-	7. Employees Related Fund	-
-	8. Interim and Proposed Dividend	-
-	9. Issue of Bonus Shares	-
-	10. Special Reserve Fund	-
1,352,486.13	11. Exchange Equalization Fund	-
-	12. Paid Up Capital Reserve	55,000,000.00
-	13. Accumulated Profit	3,365,892.63
56,220,074.51	Total	84,870,027.30

Previous Year Rs.	Particulars	This Year Rs.
-	1. Accumulated Profit up to Last Year	
46,689,945.30	2. Profit for the year	84,870,027.30
9,530,129.21	3. Accumulated Loss	
56,220,074.51	Total	84,870,027.30

**STATEMENT OF LOANS AND ADVANCES EXTENDED TO DIRECTORS/CHIEF EXECUTIVE OFFICER/PROMOTERS/EMPLOYEES
AND SHAREHOLDERS HOLDING MORE THAN 1% SHARES**

Name of Promoter/Director/ CEO/Employee	Outstanding up to Last Year		Recovered in Current Year		Additional Lending in this year	Outstanding as of Asadh End 2062	
	Principal	Interest	Principal	Interest		Principal	Interest
A. Directors	-	-	-	-	-	-	-
1.	-	-	-	-	-	-	-
2.	-	-	-	-	-	-	-
3.	-	-	-	-	-	-	-
B. Chief Executive Officer	-	-	-	-	-	-	-
C. Promoters	-	-	-	-	-	-	-
1.	-	-	-	-	-	-	-
2.	-	-	-	-	-	-	-
3.	-	-	-	-	-	-	-
D. Employees	-	-	-	-	-	-	-
1.	-	-	-	-	-	-	-
2.	-	-	-	-	-	-	-
3.	-	-	-	-	-	-	-
E. Shareholder holding more than 1% Shares	-	-	-	-	-	-	-
1.	-	-	-	-	-	-	-
2.	-	-	-	-	-	-	-
3.	-	-	-	-	-	-	-
Total	-	-	-	-	-	-	-

CAPITAL ADEQUACY TABLE
As of Ashadh End 2062 (15 July, 2005)

Rs. '000

Particulars	Previous Year	This Year
A. Core Capital	552,869	637,739
1. Paid Up Capital	550,000	550,000
2. Share Premium	-	-
3. Non-Redeemable Preference Shares	-	-
4. General Reserve Fund	12,399	29,373
5. Accumulated Profit/Loss (Up to previous year)	(45,530)	(9,530)
6. Current Year's Profit/Loss as per Balance Sheet	35,999	67,896
B. Supplementary Capital	26,511	51,104
1. Loan Loss Provision	25,158	51,104
2. Exchange Equalization Fund	1,352	-
3. Asset Revaluation Reserve	-	-
4. Hybrid Capital Instrument	-	-
5. Unsecured Subordinated Term Debt	-	-
6. Interest Spread Reserve Fund	-	-
7 Other Free Reserves	-	-
C. Total Capital Fund (A+B)	579,380	688,843
D. Minimum Capital Fund required to be maintained on the basis of Risk Weighted Assets		
Total Capital Fund (11%)	357,573	666,944
Core Capital (5.5%)	178,786	333,472
Total Capital Fund (Excess/Short) (Excess 6.82%)	221,807	21,899
Core Capital (Excess/Short) (Excess 11.51%)	374,083	304,267

DETAILS OF RISK WEIGHTED ASSETS

Rs. In '000

Particulars	Weight %	Asadh End 2061		Asadh End 2062	
		Amount	Risk Weighted Assets	Amount	Risk Weighted Assets
A Balance -Sheet Item					
1 Cash Balance	-	65,257	-	121,550	-
2 Gold (Tradable)	-	-	-	-	-
3 Balance with Nepal Rastra Bank	-	136,657	-	463,233	-
4 Investments in Government Securities	-	71,320	-	127,336	-
5 Investments in N.R.B. Bonds	-	-	-	-	-
6 Fully secured loan against own Fixed Deposit Receipt	-	600	-	12,722	-
7 Fully secured loan against Government Securities	-	-	-	-	-
8 Balances with Domestic Banks and Financial Institutions	20	54,774	10,955	102,475	20,495
9 Fully secured loan against FDR of other Commercial Banks	20	-	-	-	-
10 Balances with Foreign Banks	20	154,057	30,811	43,875	8,775
11 Money at Call	20	150,000	30,000	15,000	3,000
12 Loan against Guarantees of Internationally Rated Banks	20	-	-	-	-
13 Other Investments in Internationally Rated Banks	20	44,694	8,939	274,317	54,863
14 Investment in Shares, Debentures and Bonds	100	8,943	8,943	9,296	9,296
15 Other Investments	100	149,450	149,450	57,663	57,663
16 Loans, Advances and Bills Purchased/Discounted	100	2,540,188	2,540,188	5,117,501	5,117,501
17 Fixed Assets	100	62,413	62,413	86,212	86,212
18 All Other Assets	100	57,962	57,962	94,070	94,070
Total (A)		3,496,315	2,899,661	6,525,250	5,451,875
B Off -Balance -Sheet Item					
1 Bills Collection	0	1,108	-	85,621	-
2 Forward Foreign Exchange Contract	10	22,335	2,234	-	-
3 Letter of Credit with maturity of less than 6 months (Full Amount)	20	206,361	41,272	257,668	51,534
4 Guarantee issued against counter guarantee of Internationally Rated Foreign Banks	20	-	-	-	-
5 Letter of Credit with maturity of more than 6 months	50	64,845	32,423	102,074	51,037
6 Bid Bond	50	27,886	13,943	5,598	2,799
7 Performance Bond	50	131,072	65,536	302,711	151,356
8 Advance payment Guarantee	100	11,416	11,416	10,802	10,802
9 Financial Guarantee	100	140,900	140,900	267,300	267,300
10 Other Guarantee	100	33,834	33,834	1,999	1,999
11 Irrevocable Loan Commitment	100	-	-	-	-
12 Contingent Liabilities in respect of Income Tax	100	-	-	-	-
13 All Other Contingent Liabilities	100	9,446	9,446	74,429	74,429
Total (B)		649,203	351,003	1,108,202	611,255
Total Risk Weighted Assets (A+B)		4,145,518	3,250,664	7,633,452	6,063,130

KEY INDICATORS OF LAST FIVE YEARS

Particulars	Indicators	F. Y. 2000/01	F. Y. 2001/02	F. Y. 2002/03	F. Y. 2003/04	F. Y. 2004/05
1. Net Profit/Total Income	%	(43.84)	(54.87)	10.13	19.16	19.82
2. Earnings Per Share	Rs.	(18.36)	-	2.81	8.49	15.43
3. Market Value per Share	Rs.	-	-	100.00	125.00	256.00
4. PE Ratio	Ratio	-	-	35.55	14.72	16.59
5. Dividend (Including Bonus Shares)	%	-	-	-	-	-
6. Cash Dividend	%	-	-	-	-	-
7. Interest Income/Loans & Advances	%	6.32	10.70	8.39	7.87	3.84
8. Employee Expenses/Total Operating Expenses	%	35.82	33.75	13.66	11.30	10.70
9. Interest Expenses/Total Deposit and Borrowings	%	3.45	6.48	4.08	3.98	3.26
10. Exchange Fluctuation Gain/Total Income	%	2.87	4.82	-0.25	2.22	2.65
11. Staff Bonus/ Total Employee Expenses	%	-	-	9.76	26.11	43.50
12. Net Profit/Loans & Advances	%	(3.13)	(6.47)	1.02	1.84	1.65
13. Net Profit/ Total Assets	%	(1.97)	(3.83)	0.64	1.35	1.31
14. Credit/Deposit	%	70.47	65.85	84.09	92.24	91.83
15. Total Operating Expenses/Total Assets	%	2.73	3.17	5.32	5.10	4.28
16. Capital Fund/Risk Weightage Assets						
a. Primary Capital	%	7.75	7.99	23.98	17.01	10.52
b. Supplementary Capital	%	0.60	2.69	0.77	0.82	0.84
c. Total Capital Fund	%	8.35	10.68	24.75	17.82	11.36
17. Liquidity (CRR)	%	3.11	3.41	4.98	4.91	8.27
18. Non Performing Loans/Total Loans	%	0.91	10.45	2.08	0.98	0.39
19. Weighted Average Interest Rate Spread	%	3.99	4.36	2.50	3.78	3.97
20. Book Net worth	Rs.	68,722,599	79,544,033	501,705,898	554,221,843	637,739,384
21. Total Shares	Number	840,000	1,362,001	5,441,740	5,500,000	5,500,000
22. Total Employees	Number	52	66	75	85	137
23. Book Value per Share		81.81	58.40	92.20	100.77	115.95

CASH FLOW STATEMENT
Fiscal Year 2061/62 (2004/05)

Previous Year Rs.	Particulars	This Year Rs.
68,401,309.33	A. Cash Flow from Operating Activities	139,052,204.75
<u>236,590,472.52</u>	1. Cash Receipt	<u>411,726,101.16</u>
208,127,749.56	1.1 Interest Income	365,482,496.10
14,840,269.37	1.2 Commission and Discount Income	21,391,062.43
12,621,092.27	1.3 Exchange Income	11,359,386.97
-	1.4 Non-Operating Income	286,968.96
1,001,361.32	1.5 Other Incomes	13,206,186.70
<u>168,189,163.19</u>	2. Cash Payments	<u>272,673,896.41</u>
113,579,092.57	2.1 Interest Expenses	187,027,981.93
19,872,459.80	2.2 Employee Expenses	29,581,861.23
29,549,839.12	2.3 Operating Expenses	43,195,662.58
-	2.4 Exchange Loss	-
-	2.5 Non-Operating Loss	-
5,187,771.70	2.6 Other Expenses	12,868,390.67
<u>(1,057,953,261.83)</u>	B. Cash Flow from Investing Activities	<u>(3,019,837,856.96)</u>
(189,406,264.96)	1. (Increase)/Decrease in Bank Balance	(264,094,503.95)
70,000,000.00	2. (Increase)/Decrease in Money at Call and Short Notice	135,000,000.00
123,949,254.75	3. (Increase)/Decrease in Investment	(194,205,229.37)
(1,044,922,912.24)	4. (Increase)/Decrease in Loans, Advances and Bills Purchased	(2,589,781,007.22)
(10,306,885.71)	5. (Increase)/Decrease in Fixed Assets	(33,702,064.58)
(7,266,453.67)	6. (Increase)/Decrease in Other Assets	(73,055,051.84)
<u>1,009,166,305.79</u>	C. Cash Flow from Financing Activities	<u>2,937,079,256.93</u>
5,826,000.00	1. Increase in Share Capital	-
12,167,330.15	2. Increase/(Decrease) in Borrowings	52,050,143.80
975,845,800.38	3. Increase/(Decrease) in Deposits	2,832,170,554.44
1,178,988.06	4. Increase/(Decrease) in Bills Payable	4,191,809.56
-	5. Increase/(Decrease) in Reserve Funds	(1,352,486.13)
14,148,187.20	6. Increase/(Decrease) in Other Liabilities	50,019,235.26
<u>19,614,353.30</u>	D. Net Cash Flow for the year	<u>56,293,604.72</u>
45,642,182.38	E. Opening Cash Balance	65,256,535.68
65,256,535.68	F. Closing Cash Balance	121,550,140.41

SIGNIFICANT ACCOUNTING POLICIES

The followings are the significant accounting policies adopted by the bank:

1. Basis Of Accounting

The Financial Statements have been prepared in historical cost basis and based on Nepal Accounting Standard and other Generally Accepted Accounting Standards, Company Act - 2062, Bank and Financial Institutions Ordinance - 2062 and Nepal Rastra Bank's Directives.

2. Depreciation On Fixed Assets

Fixed Assets have been accounted on historical cost concept. Fixed Assets are depreciated on diminishing balance method at the rates specified in the Accounting Policy of the Bank, which was approved by the Board.

Type of Property	Depreciation in %
Building	5
Vehicle	15
Wooden Furniture	15
Metal Furniture	10
Office Equipment	15
Computer	20
Generator	15

Depreciation for the purpose of Income Tax is calculated at the rates and manner prescribed by the Income Tax Act, 2058 which comes to Rs.9,902,298.29 whereas the depreciation computed on the above approved rates for the period is Rs. 13,585,026.49. Due to this, the accounting profit has increased by Rs. 3,682,728.20.

3. Provision for Income Tax

Provision for Income Tax is provided on the basis of Income Tax Act, 2058.

4. Investments

Investments made for trading and other purpose has been accounted separately. Investments are valued at Cost or Market Value whichever is lower and has complied with NRB Directives in this regard.

5. Foreign Currency Transactions

Income/Loss from foreign currency transactions have been separately shown as Trading Income/Loss and Foreign Exchange Revaluation Income/Loss. Twenty Five percent of such revaluation gain has been transferred to Exchange Fluctuation Reserve as per the directives of Nepal Rastra Bank through Profit and Loss Appropriation Account.

6. Non Banking Assets

The Bank has the practice of acquiring the properties obtained as security of the loans and advances granted if such assets could not be disposed off due to unsatisfactory bids received at the time of auction.

The Bank has adopted the policy of valuing such assets at the amount equal to the sum of loans and interest due as on the date. Such assets are disposed within 7 years from the date of acquisition or as specified in present Bank and Financial Institution Ordinance, 2061 and if the sale proceeds are different from the value of the asset as acquired, the same is charged to profit and loss account. If in case the market value of the acquired property during the year is less than sum of loans and

interest receivable, such acquired property is valued at the market value and the balance if any of the loans and interest receivable is charged to the profit and loss account during the year.

7. Consumable Items

The Bank has adopted the policy of charging assets costing up to Rs. 2,000.00 to the profit and loss account during the year of acquisition instead of capitalizing the same.

8. Cash Basis of Accounting

Interest Expenses on Deposits and Interest Income on Loans and Advances are computed on the basis of 365 days a year. Similarly, Interest Income in respect of Investment is also computed on the basis of 365 days a year. However, in case of Hire Purchase Loans interest is computed on the basis of 360 days a year.

Interest income on loans and advances are recognized on cash basis. As per the Nepal Rastra Bank's Directive, interest collected during the first month of the following fiscal year.

Interest expenses on interest bearing deposit and liabilities are accounted on accrual basis.

9. Provision for Possible Losses and Write Off Policy

Provision for possible losses has been made as per Nepal Rastra Bank's Directives to cover risk inherent in Bank's Loan Portfolio.

The bank has not written off any loans till date.

10. Contingent Liability in respect of Letter of Credit issued have been shown in full amount as of the year end.

11. Other Policies

a. Commission Income Recognition:

Commission Income is accounted on Cash Basis except in cases of Bank Guarantees issued whose commission income is more than Rs. 50,000.00. In such cases, the commission so earned has been accrued over the period of such Guarantee.

b. Preliminary Expenses, Pre Operating Expenses and Differed Expenses

Preliminary Expenses, Pre Operating Expenses, Computer Software Expenses and Share Issue Expenses are written off during a period of 5 years or where the period is ascertainable, the same is written off during the period so ascertained.

c. Stock and Stationary

Stocks of Stationery have been valued on FIFO (First In First Out) basis and the same has been shown under Other Assets.

d. Provision for Gratuity

Based on policies of the Bank and the no. of qualified staffs Nrs. 1,814,250.00 is provisioned in staff gratuity fund.

e. Provision of bonus to employees

Bonus to staff is provided at 10% of the net profit after loan loss provision before tax.

f. Employees Housing Scheme

As per the practice followed by other financial institutions, provision for employees housing fund as required under the Labor Act 2048 has not been provided.

g. Provision for Staff leave

As per the banking rules payments for employee leave is calculated on accrual basis

h. Previous years figures have been regrouped and rearranged wherever necessary.