



Veles International

VELES INTERNATIONAL LIMITED

Pillar 3 disclosures for the year ended 31 December 2010

CONTENTS

1.	Introduction	3
2.	Risk Management Objectives and Policies	3
2.1.	Risk Management Organisation	3
	Risk Management Framework	3
	Risk Management Process	4
2.2.	Credit Risk Management	5
	Measurement and Assessment	5
	Creditworthiness Assessment of Clients and Counterparties	5
	Efficient Monitoring and Control	6
2.3.	Market Risk Management	6
2.4.	Operational risk management	7
3.	Own funds	7
3.1.	Original Own Funds	7
4.	Minimum Required Own Funds for Credit, Market and Operational Risk	7
4.1.	Company's Approach to Assessing the Adequacy of its Internal Capital	7
	Standardised Approach for Credit Risk	7
	Minimum Capital Requirements in Relation to Operational Risk	8
	Position, Foreign Exchange and Commodity Risks Own Funds Requirements	8
5.	Counterparty Credit Risk	8
6.	Company's Exposure to Credit Risk and Dilution Risk	8
6.1.	Total Amount of Exposures	8
6.2.	Geographic Distribution of the Exposures	9
6.3.	Distribution of the Exposures by Industry or Counterparty Type	9
6.4.	Residual Maturity Breakdown of the Exposures	9
6.5.	Impaired Exposures and Past Due Exposures	9
7.	The Standardised Approach	10
7.1.	Exposure Classes for which External Credit Assessment Institutions ('ECAI') or Export Credit Agencies ('ECA') are Used	10
7.2.	Transfer of Credit Assessments onto Items not Included in the Trading Book	10
7.3.	Association of External Rating of Each Nominated ECAI or ECA with Credit Quality Steps	10
7.4.	Exposure Values Associated with Credit Quality Steps	10
8.	Exposures in Equities Not Included in the Trading Book	10
9.	Exposure to Interest Rate Risk on Positions Not Included in the Trading Book	11
	Impact on Net Assets	11
	Measuring the Interest Rate Effect	11

1. Introduction

Veles International Limited ('the Company') is regulated by the Cyprus Securities and Exchange Commission ('CySEC') under authorization number CIF075/06 issued on 20 September 2006 by which it is licensed to operate as a Cypriot Investment Firm and to provide investment and non-core services in relation to the transferable securities and shares in collective investments undertakings. The principal activities of the Company are the provision of investment services (receipt, transmission, execution of client orders and portfolio management services) and safe custody in accordance with the provisions of the applicable legislation and requirements issued by the Cyprus Securities and Exchange Commission.

This report has been prepared in accordance with the requirements of the Directive DI144-2007-05 for the Capital Requirements of Investment Firms ('the Directive') issued by the Cyprus Securities and Exchange Commission. The Directive implements the European Union's Capital Requirements Directive ('CRD').

The Directive describes the Basel II framework which is based on three pillars:

- Pillar 1 covers the standards that set out the minimum regulatory capital requirements that are required for credit, market and operational risk
- Pillar 2 covers the Supervisory Review Process which assesses the internal capital adequacy processes. Investment firms and Supervisors have to evaluate and assess whether an Investment Firm should hold additional capital against risks not covered in Pillar 1
- Pillar 3 (Market discipline) covers transparency and the obligation of Investment Firms to disclose meaningful information to the market related to their risks, capital and generally risk management.

The Company's Pillar 3 disclosures below have been prepared using 31 December 2010 data in accordance with the Directive.

The requirements of the Directive apply to the Company on an individual basis.

2. Risk Management Objectives and Policies

2.1. Risk Management Organization

Risk is inherent to the Company's business and activities. The Company's ability to identify, measure, monitor and manage each type of risk to which the Company is exposed is an important factor in its financial stability, performance, reputation and in the achievement of its strategic objectives.

Risk Management Framework

This framework provides a comprehensive approach of the Company for identifying, measuring, monitoring and managing each type of risk to which the Company is exposed. By adopting a formal approach to risk management, we achieve better outcomes as a result of systematically identifying and analyzing the wide range of issues that affect decision-making.

The risk management framework has been developed to:

- ensure that the primary objective of the risk management process is achieved. This is to ensure that a level of capital adequacy is maintained so that the total risk taken by the Company is no greater than the Company's ability to absorb losses

- allow the Company to proactively manage its risks in a systematic and structured way and to continually refine its processes to reduce its risk profile and ultimately its capital requirements
- ensure appropriate strategies are in place to mitigate or transfer risks
- embed the risk management process and ensure it is an integral part of the Company's process of strategic decision making and capital planning
- help create a risk awareness culture at all departments within the Company
- engage the Company's management's attention to the management, monitoring, reporting and reviewing of identified risks as well as considering new and emerging risks on a continuous basis.

Risk Management Process

The risk management process is integrated within the Company through established internal policies, systems, controls and comprehensive reporting, commensurate with the complexity of the Company's activities and structure. The system of internal controls provides reasonable assurance about the effectiveness and efficiency of operations, the reliability of financial reporting and compliance with applicable laws and regulations. The risk management process provides for the continuous monitoring of the system of internal controls to ensure its effectiveness.

The Risk Management Department is responsible for determination, evaluation and efficient management of the risks inherent in the provision of investment services. The department's aim is to provide these services in accordance with the provisions of the Investment Services, Activities and Regulated Markets Law of 2007 (Law 144(I)/2007) and Directives issued by the CySEC, as well as the internal regulations of the Company.

The Risk Management Department of the Company has the following duties and responsibilities:

- Development of policy regarding the assumption, follow up and management of risk which will include guidelines regarding possible risk exposure and acceptable risk levels
- Development of risk management policy for clients and counterparties for the following risks:
 - credit risk
 - liquidity risk
 - market risk
 - leverage risk
- Analysis for the Investment Committee of the potential hazards associated with the recommended framework on which investment decisions/advice are based
- Credit assessment (including quality and financial analysis) of clients when opening new client accounts and classification of clients according to the Company's risk criteria and limits
- Credit assessment of counterparties and classification of counterparties according to the Company's risk criteria and limits
- Monitoring of investment risk undertaken by the Company for each client, counterparty and the Company as a whole
- Estimating risk of the Company's clients' and counterparties' participation in money laundering and/or terrorist funding activities

- Monitoring of deals executed with counterparties in relation with securities' market prices
- Monitoring of brokerage and asset management transactions as regards adherence to established risk limits
- Monitoring risk associated with margin trading clients
- Monitoring day-to-day operational risks
- Building a risk-aware culture within the Company and providing relevant trainings
- Maintenance of appropriate internal control systems designed to manage key risk areas
- Evaluation of risks associated with the development of new investment products
- Providing an annual written report to the Company's Board of Directors on the matters of the Department's responsibilities indicating in particular whether the appropriate remedial measures have been taken in the event of any deficiencies.

The Company's strategies and processes for managing risks, as well as the measurement systems used and the hedging and mitigating strategies are analyzed below by risk division.

2.2. Credit Risk Management

Credit risk is defined as the potential that a company borrower or counterparty will fail to meet its obligations in accordance with agreed terms. The goal of credit risk management is to maximize a company's risk-adjusted rate of return in the provision of investment services by maintaining credit risk exposure within acceptable parameters. The effective management of credit risk is a critical component of a comprehensive approach to risk management and essential to the long-term success of an investment company.

Measurement and Assessment

The Credit Risk Management Policy establishes the framework for credit assessment, structure of limits and process of approval and monitoring of credit risks. The Company manages the credit risk inherent in its entire portfolio as well as the risk attributable to individual credits or transactions. Credit exposures from related accounts are aggregated and monitored on a consolidated basis.

The Company's Risk Manager sets targets and limits for the composition and quality of the loans, advances and trade debtors portfolio and monitors compliance with them. Limits approval is done by the Investment Committee of the Company on the basis of List of limits prepared by the Company's Risk Manager.

Creditworthiness Assessment of Clients and Counterparties

Evaluation of client or counterparty creditworthiness involves analysis of financial and non-financial data, including submitted pledge to cover their credit risks.

Financial data includes:

- balance sheet,
- income statement,
- diversification,
- leverage and other information from financial statements.

Non-financial data includes:

- Qualitative characteristics (such as industry review, business risk, etc)
- Reputation
- Assessments of credit risk by external assessors

All required information is collected from the clients during account opening KYC ('Know Your Client') procedures and from the counterparties during due diligence procedures.

The assessment of the quality of the portfolio is carried out using credit rating and credit scoring systems to determine the creditworthiness of customers. Credit Rating approach to credit risk classifies companies based on their rating with External Credit Assessment Institutions (ECAI) and calculates the historical percentage of defaults for each rating. The Company only uses ECAIs that have been recognized and announced as eligible by CySEC. The calculation of the overall credit risk is also performed using the SAS Credit Risk Management that gives the possibility to quickly and accurately calculate critical risk measures, such as probability of default, exposure at default, credit migration, regulatory capital, risk weighted assets, credit value at risk (CVaR) and economic capital. The system also allows performing mark-to-market calculations, model risk factors, running Monte Carlo simulations, exploring scenarios and building stress tests. Every step of the process can be viewed, validated, audited and customized.

Efficient Monitoring and Control

The Company's Risk Manager constantly reviews clients and counterparties creditworthiness. Monitoring includes review of the following data:

- previously collected information
- limits set previously for this client or counterparty
- all financial data information updates collected from the last review (not less than one year)
- all non-financial information (not less than six months)

The purpose of such monitoring is to ensure that limits set previously to clients and counterparties are valid and there is no negative information stipulating high probability of counterparty's/client's failure to carry its obligations. Following the review, Risk Management amends if required the limits set previously for the particular client or counterparty.

Approved credit limits are registered on a protected excel spreadsheet and circulated to all traders and front office and back office employees as an extra monitoring tool. In cases where a trader enters a deal which results in violation of credit limits, the deal is blocked by the system (ORC-software) and is not executed. The Risk Management department is informed of any violations and makes decision whether to accept the violation or close the deal.

2.3. Market Risk Management

Market risk reflects the extent to which the return of the security varies in response to, or in association with, variations in the overall market returns. Market risk is associated with the Company's open positions, which are exposed to the risks of changes in the market. Credit, country, liquidity, exchange rate and interest rate risks in particular have an impact in the form of price fluctuations.

The Company's Risk Management Department is responsible for measuring and monitoring of market risk, setting out the policy for management of this type of risk and approving acceptable market risk limits, such as position limits, stop-loss limits etc. The evaluation of market risk of certain instruments is carried out on a daily basis using the Value at Risk (VaR) approach. The Risk Management Department prepares reports on the methods used by the Company for the estimation and valuation of the market risk for the ratification by the Board of Directors of the Company.

The lack of sophistication in monitoring of emerging financial markets can result in poor levels of market transparency, liquidity, efficiency and regulation in the emerging markets. Moreover, high volatility and large price differences are characteristic of these markets. Finally, the inadequacy or

absence of regulatory measures gives rise to an increased danger of market manipulation or insider trading.

2.4. Operational Risk Management

Operational risk is defined as the risk of loss resulting from inadequate or failed internal processes, people and systems or from external events. It includes legal risk but excludes reputation and strategic risks. It is embedded in every business activity and potential losses may occur in all Company's activities.

The Company has adopted the Basic Indicator Approach for the assessment of own funds requirements for operational risk. The capital requirement for operational risk under the Basic Indicator Approach is equal to 15% of a relevant indicator, which is defined in Annex X, Part 1 of Part C of the Directive as the average over three years of the sum of net income.

3. Own Funds

The own funds of Veles International Limited as at 31.12.2010 were US\$2.809.507 as shown below:

Original Own Funds (Tier 1)	US\$
Share Capital	1.415.218
Retained earnings	1.395.287
Total Tier 1	2.810.505
Deductions from Original Own Funds	
Investment in subsidiary	(1.000)
Total Eligible Own Funds	2.809.505

3.1. Original Own Funds

Share Capital

As at 31.12.2010 the share capital of the Company comprised 600.000 shares with a nominal value of EUR 1,71 each for the total amount of US\$ 1.415.218.

4. Minimum Required Own Funds for Credit, Market and Operational Risk

4.1. Company's Approach to Assessing the Adequacy of its Internal Capital

Different approaches based on the different categories of risks are used to assess the adequacy of the Company's internal capital to support current and future activities. These approaches are described below.

Standardised Approach for Credit Risk

The necessary mechanism for the capital calculation in accordance with the Standardised Approach is implemented in accordance with the Directive, paragraphs 2-7 of Chapter 1 of Part C.

The following table shows 8% of the risk-weighted Company's exposure amounts as at 31.12.2010 for each of the exposure classes specified in paragraph 3 of Chapter 1 of Part C of the Directive.

	US\$
Short-term claims on institutions	179.195
Administrative bodies	3.262
Corporates	871
Other items	13.763
	<u>197.091</u>

Minimum Capital Requirements in Relation to Operational Risk

The minimum capital requirement in relation to operational risk calculated in accordance with the Standardised Approach (Part C, Chapter 5, paragraphs 27 to 29 of the Directive) amounts to US\$254.415.

Position, Foreign Exchange and Commodity Risks Own Funds Requirements

The capital requirement in relation to position, foreign exchange and commodity risks calculated in accordance with the Part D, Annexes I-IV of the Directive amounts to US\$114.623.

5. Counterparty Credit Risk

As at 31 December 2010, the Company did not have any margin lending transactions outstanding.

6. Company's Exposure to Credit Risk and Dilution Risk

Past due accounts receivable are defined as all accounts receivable where the counterparty has failed to make a payment when it was contractually due. At each balance sheet date the Company assesses whether there is any objective evidence that accounts receivable (/debts) are impaired. A debt is impaired if there is objective evidence of impairment as a result of one or more events that have occurred after the initial recognition of the liability (an incurred 'loss event') and that loss event (or events) has an impact on the estimated future cash flows of the debt or the group of debts, that can be reliably estimated.

6.1. Total Amount of Exposures

Exposures by different types of exposure classes as at 31 December 2010

Type	ST claims on institutions US\$	Administrative bodies US\$	Corporates US\$	Other items US\$	Total US\$
Cash and cash equivalents	10.663.433	-	-	-	10.663.433
Trade receivables	67.657	-	10.889	-	78.546
Other receivables	-	203.891	-	-	203.891
Prepayments	-	-	-	19.985	19.985
Amounts due from related parties	468.586	-	-	-	468.586
Fixed assets	-	-	-	152.054	152.054
Total	11.199.676	203.891	10.889	172.039	11.586.495

6.2. Geographic Distribution of the Exposures

Exposures by geographic area as at 31 December 2010

Country	ST claims on institutions US\$	Administrative bodies US\$	Corporates US\$	Other items US\$	Total US\$
Cyprus	5.710.513	203.891	244	172.039	6.086.687
British Virgin Islands	-	-	364	-	364
Latvia	4.798.897	-	-	-	4.798.897
Switzerland	5.851	-	-	-	5.851
Germany	-	-	1.811	-	1.811
Russia	611.385	-	520	-	611.905
Kazakhstan	-	-	7.950	-	7.950
Ukraine	73.030	-	-	-	73.030
Total	11.199.676	203.891	10.889	172.039	11.586.495

6.3. Distribution of the Exposures by Industry or Counterparty Type

Exposures by industry or counterparty type as at 31 December 2010

Industry / Counterparty type	ST claims on institutions US\$	Administrative bodies US\$	Corporates US\$	Other items US\$	Total US\$
Financial institutions	11.199.676	-	-	-	11.199.676
Others	-	203.891	10.889	172.039	386.819
Total	11.199.676	203.891	10.889	172.039	11.586.495

6.4. Residual Maturity Breakdown of the Exposures

Exposures by the residual maturity as at 31 December 2010

	ST claims on institutions US\$	Administrative bodies US\$	Corporates US\$	Other items US\$	Total US\$
Less than 1 year	11.199.676	-	10.889	19.986	11.230.551
Indefinite maturity	-	203.891	-	152.053	355.944
Total	11.199.676	203.891	10.889	172.039	11.586.495

6.5. Impaired Exposures and Past Due Exposures

As at 31 December 2010, the Company did not have any impaired exposures or past due exposures.

7. The Standardised Approach

7.1. Exposure Classes for which External Credit Assessment Institutions ('ECAI') or Export Credit Agencies ('ECA') are Used

The Company uses external ratings of Standard&Poor's. These ratings are used for all relevant exposure classes, which are the following:

- Claims or contingent claims on institutions
- Claims or contingent claims on corporates (it should be noted that most corporates are unrated)
- Short-term claims on institutions and corporates

7.2. Transfer of Credit Assessments onto Items not Included in the Trading Book

The exposures are classified into the above exposure classes, and are then ranked into respective credit quality steps, that determine the risk-weight to be used in accordance with the provisions of the Directive.

In the case of financial institutions, the credit quality step is determined, according to the rating of the country under whose supervision they operate. It should be noted that all exposures with financial institutions with original maturity of three months or less, are risk-weighted 20%, unless the counterparty is unrated and the risk-weight assigned to its country is higher.

7.3. Association of the External Rating of Each Nominated ECAI or ECA with Credit Quality Steps

The Company complies with the standard association published by CySEC, regarding the association of the external rating of each nominated ECAI or ECA with the credit quality steps prescribed in Annex VI of the Directive.

7.4. Exposure Values Associated with Credit Quality Steps

The exposure values before and after credit risk mitigation associated with each credit quality step prescribed in Annex VI of Part C of the Directive as at the 31 December 2010 were as follows:

Rating	Total exposure US\$
AAA	5.850
A	5.914.404
BBB	611.385
BB+	4.798.897
B+	73.030
Not rated	182.929
	<u>11.586.495</u>

As at the year-end the Company did not employ any credit risk mitigation for its exposures, therefore, the above amounts indicate the exposures both before and after credit risk mitigation.

8. Exposures in Equities Not Included in the Trading Book

The Company did not hold any equity securities not included in the trading book as at the 31 December 2010.

9. Exposure to Interest Rate Risk on Positions Not Included in the Trading Book

Interest rate risk is the risk that the value of financial instruments will fluctuate due to changes in market interest rates. The Company's Risk Manager monitors the interest rate fluctuations on a continuous basis and acts accordingly.

Impact on Net Assets

The following table demonstrates the sensitivity on the Company's post-tax profit to a reasonably possible change in interest rates, with all other variables held constant. The sensitivity of the Company's post tax profit is the effect of changes in interest rates which are reasonably possible at the reporting dates which arises on floating rate interest bearing financial assets and financial liabilities as at 31 December 2010 and 2009.

Sensitivity as of 31 December 2010

Increase /decrease in basis points	Sensitivity of profit after tax and net assets
2010	2010
	US\$
+/-50	+/- 47.985

Sensitivity as of 31 December 2009

Increase/decrease in basis points	Sensitivity of profit after tax and net assets
2009	2009
	US\$
+/-50	+/- 49.504

The following table demonstrates the sensitivity to a reasonable possible change in foreign exchange rates with all other variables held constant on the Company's post tax profit.

Currency	Change in currency rate	Effect on post tax profit and net assets
	2010	2010
	%	US\$
Russian Rouble	+/-15	-/+ 168.874
Euro	+/-10	-/+ 2.360

Currency	Change in currency rate	Effect on post tax profit and net assets
	2009	2009
	%	US\$
Russian Rouble	+/-15	-/+ 151.066
Euro	+/-10	-/+ 1.910

Measuring the Interest Rate Effect

The following methodology is used to measure the interest rate effect.

The assets and liabilities in each currency are placed in time bands, according to the number of days remaining from the reporting date until their maturity. The difference between assets and liabilities in each time band, 'the gap' is then calculated. The gaps are the starting point in calculating the impact on net assets from a certain change in interest rates.