JOINT STOCK COMPANY HALYK BANK GEORGIA

Financial Statements and
Independent Auditor's Report
For the Year Ended December 31, 2016

JOINT STOCK COMPANY HALYK BANK GEORGIA

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STATEMENT OF MANAGEMENT'S RESPONSIBILITIES FOR THE PREPARATION AND APPROVAL OF THE FINANCIAL STATEMENTS FOR THE YEAR ENDED DECEMBER 31, 2016

Management is responsible for the preparation of the financial statements that present fairly the financial position of Joint Stock Company Halyk Bank Georgia (the "Bank") as at December 31, 2016, the results of its operations, cash flows and changes in equity for the year then ended, in compliance with International Financial Reporting Standards ("IFRS").

In preparing the financial statements, management is responsible for:

- Properly selecting and applying accounting policies;
- Presenting information, including accounting policies, in a manner that provides relevant, reliable, comparable and understandable information;
- Providing additional disclosures when compliance with the specific requirements in IFRSs are insufficient to enable users to understand the impact of particular transactions, other events and conditions on the Bank's financial position and financial performance; and
- Making an assessment of the Bank's ability to continue as a going concern.

Management is also responsible for:

- Designing, implementing and maintaining an effective and sound system of internal controls, throughout the Bank;
- Maintaining adequate accounting records that are sufficient to show and explain the Bank's transactions and disclose with reasonable accuracy at any time the financial position of the Bank, and which enable them to ensure that the financial statements of the Bank comply with IFRS;
- Maintaining statutory accounting records in compliance with legislation and accounting standards of Georgia;
- Taking such steps that are reasonably available to them to safeguard the assets of the Bank; and
- Preventing and detecting fraud and other irregularities.

The financial statements for the year ended December 31, 2016 were authorized for issue on March 2, 2017 by the Management Board of the Bank.

On behalf of the Management Board:

Nikoloz Geguchadze	**Gulnara Marshanishvili**
General Director	**Chief Accountant**
March 2, 2017	March 2, 2017
Tbilisi, Georgia	Tbilisi, Georgia

Deloitte.

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INDEPENDENT AUDITOR'S REPORT

To the Shareholders and the Board of Directors of Joint Stock Company Halyk Bank Georgia:

Opinion

We have audited the financial statements of Joint Stock Company Halyk Bank Georgia (the "Bank"), which comprise the statement of financial position as at December 31, 2016, and the statement of comprehensive income, statement of changes in equity and statement of cash flows for the year then ended, and notes to the financial statements, including a summary of significant accounting policies.

In our opinion, the accompanying financial statements present fairly, in all material respects, the financial position of the Company as at December 31, 2016, and its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards ("IFRSs").

Basis for Opinion

We conducted our audit in accordance with International Standards on Auditing ("ISAs"). Our responsibilities under those standards are further described in the *Auditor's Responsibilities for the Audit of the Financial Statements* section of our report. We are independent of the Bank in accordance with the International Ethics Standards Board for Accountants' *Code of Ethics for Professional Accountants* (the "IESBA Code") together with the ethical requirements that are relevant to our audit of the financial statements in Georgia, and we have fulfilled our other ethical responsibilities in accordance with these requirements and the IESBA Code. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Responsibilities of Management and Those Charged with Governance for the Financial Statements

Management is responsible for the preparation and fair presentation of the financial statements in accordance with IFRSs, and for such internal control as management determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, management is responsible for assessing the Bank's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless management either intends to liquidate the Bank or to cease operations, or has no realistic alternative but to do so.

Those charged with governance are responsible for overseeing the Bank's financial reporting process.

Deloitte.

Auditor's Responsibilities for the Audit of the Financial Statements

Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISAs will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

As part of an audit in accordance with ISAs, we exercise professional judgment and maintain professional skepticism throughout the audit. We also:

- Identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- Obtain an understanding of internal control relevant to the audit 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 Company's internal control.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management.
- Conclude on the appropriateness of management's use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Company's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the Company to cease to continue as a going concern.
- Evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation.

We communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

Deloitte & Touche

March 2, 2017
Tbilisi, Georgia

JOINT STOCK COMPANY HALYK BANK GEORGIA

STATEMENT OF FINANCIAL POSITION
FOR THE YEAR ENDED DECEMBER 31, 2016
(in thousands of Georgian Lari)

	Notes	December 31, 2016	December 31, 2015
ASSETS:			
Cash and cash equivalents	5, 28	30,629	14,458
Mandatory cash balance with the National Bank of Georgia		37,751	16,560
Due from banks	6	871	239
Loans to customers	7, 28	273,501	201,610
Available-for-sale financial assets	8	54	54
Investments held to maturity	9	16,757	19,283
Property and equipment	10	12,119	10,427
Intangible assets	11	3,210	1,914
Other assets	12	1,465	1,363
TOTAL ASSETS		**376,357**	**265,908**
LIABILITIES:			
Deposits by banks	13, 28	205,746	140,363
Deposits by customers	14, 28	80,132	48,170
Income tax liabilities		412	-
Deferred income tax liabilities	23	1,720	877
Other liabilities	15	2,373	1,935
Subordinated debt	16, 28	26,561	24,047
TOTAL LIABILITIES		**316,944**	**215,392**
EQUITY:			
Equity attributable to owners of the Bank:			
Share capital	17	48,000	48,000
Property revaluation reserve		410	207
Retained earnings		11,003	2,309
TOTAL EQUITY		**59,413**	**50,516**
TOTAL LIABILITIES AND EQUITY		**376,357**	**265,908**

On behalf of the Management Board:

Nikoloz Geguchadze
General Director

March 2, 2017
Tbilisi, Georgia

Gulnara Marshanishvili
Chief Accountant

March 2, 2017
Tbilisi, Georgia

The notes on pages 8-53 form an integral part of these financial statements.

JOINT STOCK COMPANY HALYK BANK GEORGIA

STATEMENT OF PROFIT OR LOSS AND OTHER COMPREHENSIVE INCOME FOR THE YEAR ENDED DECEMBER 31, 2016
(in thousands of Georgian Lari)

	Notes	2016	2015
Continuing operations			
Interest income	18, 28	28,678	21,788
Interest expense	18, 28	(8,738)	(7,063)
Net interest income before impairment losses on interest bearing assets		19,940	14,725
Impairment losses on interest bearing assets	19	(2,664)	(1,291)
Net interest income		**17,276**	**13,434**
Net gain on foreign exchange operations	20	978	727
Fee and commission income	21	3,902	1,220
Fee and commission expense	21	(2,443)	(535)
Provision on other operations	15	(9)	(131)
Other income		95	65
Net non-interest income		**2,523**	**1,346**
Operating income		**19,799**	**14,780**
Operating expenses	22, 28	(9,888)	(7,774)
Profit before income tax		**9,911**	**7,006**
Income tax expense	23	(1,219)	(1,004)
Net profit for the year		**8,692**	**6,002**
Other comprehensive income			
Net gain resulting on revaluation of property		241	-
Income tax	23	(36)	-
Other comprehensive income after income tax		**205**	**-**
Total comprehensive income		**8,897**	**6,002**

On behalf of the Management Board:

Nikoloz Geguchadze
General Director

March 2, 2017
Tbilisi, Georgia

Gulnara Marshanishvili
Chief Accountant

March 2, 2017
Tbilisi, Georgia

The notes on pages 8-53 form an integral part of these financial statements.

JOINT STOCK COMPANY HALYK BANK GEORGIA

STATEMENT OF CHANGES IN EQUITY
FOR THE YEAR ENDED DECEMBER 31, 2016
(in thousands of Georgian Lari)

	Note	Share capital	Property revaluation reserve	Retained earnings	Total equity attributable to owners of the Bank
January 1, 2015		**48,000**	**209**	**(3,695)**	**44,514**
Profit for the year		-	-	6,002	6,002
Release of revaluation reserve due to depreciation of previously revalued assets		-	(2)	2	-
December 31, 2015		**48,000**	**207**	**2,309**	**50,516**
Profit for the period		-	-	8,692	8,692
Other comprehensive income after income tax		-	205	-	205
Release of revaluation reserve due to depreciation of previously revalued assets		-	(2)	2	-
December 31, 2016		**48,000**	**410**	**11,003**	**59,413**

On behalf of the Management Board:

Nikoloz Geguchadze
General Director

March 2, 2017
Tbilisi, Georgia

Gulnara Marshanishvili
Chief Accountant

March 2, 2017
Tbilisi, Georgia

The notes on pages 8-53 form an integral part of these financial statements.

JOINT STOCK COMPANY HALYK BANK GEORGIA

STATEMENT OF CASH FLOWS
FOR THE YEAR ENDED DECEMBER 31, 2016
(in thousands of Georgian Lari)

	2016	2015
CASH FLOWS FROM OPERATING ACTIVITIES:		
Profit before income tax	9,911	7,006
Adjustments for non-cash items:		
Provision for impairment losses on interest bearing assets	2,664	1,291
Provision on other operations	9	131
Depreciation and amortization	701	552
Foreign exchange gain	163	20
Net change in accrued interest	(2,483)	682
Cash flows from operating activities before changes in operating assets and liabilities	**10,965**	**9,682**
Changes in operating assets and liabilities		
Increase in operating assets:		
Mandatory cash balance with the NBG	(27,043)	(9,974)
Due from banks	(767)	(40)
Loans to customers	(102,726)	(68,897)
Other assets	(161)	(1,069)
Decrease in operating liabilities:		
Deposits by banks	39,781	62,665
Deposits by customers	99,157	(1,496)
Other liabilities	429	1,222
Net cash from operating activities / (used in)	**19,635**	**(7,907)**
CASH FLOWS FROM INVESTING ACTIVITIES		
Payments for property and equipment	(1,940)	(1,734)
Proceeds on disposal of property and equipment	47	1
Payments for intangible assets	(1,498)	(660)
Purchase of investments held to maturity	2,502	(3,439)
Net cash used in investing activities	**(889)**	**(5,832)**
Effect of exchange rate changes on the balance of cash held in foreign currencies	(2,575)	440
Net increase / (decrease) in cash and cash equivalents	**16,171**	**(13,299)**
CASH AND CASH EQUIVALENTS, beginning of the year	**14,458**	**27,757**
CASH AND CASH EQUIVALENTS, end of the year	**30,629**	**14,458**

Interest paid and received by the Bank during the year ended December 31, 2016 amounted to GEL 10,470 thousand and GEL 27,972 thousand, respectively. Interest paid and received by the Bank during the year ended December 31, 2015 amounted to GEL 4,804 thousand and GEL 19,912 thousand, respectively.

On behalf of the Management Board:

Nikoloz Geguchadze
General Director

March 2, 2017
Tbilisi, Georgia

Gulnara Marshanishvili
Chief Accountant

March 2, 2017
Tbilisi, Georgia

The notes on pages 8-53 form an integral part of these financial statements.

(in thousands of Georgian Lari)

1. Organization

Halyk Bank Georgia (the "Bank") is a joint stock bank, which was incorporated in Georgia on January 29, 2008. The Bank is regulated by the National Bank of Georgia (the "NBG") and conducts its business under general license number 0110246. The Bank's primary business consists of commercial activities, trading with securities, foreign currencies, originating loans and guarantees and deposit taking.

The registered office of the Bank is located on 74 Kostava Street, Tbilisi, Georgia.

As at December 31, 2016 and 2015 the Bank had seven and six branches, respectively, operating in Georgia.

As at December 31, 2016 and 2015 the following shareholder owned the issued shares of the Bank.

	December 31, 2016	December 31, 2015
First level shareholder:		
JSC Halyk Bank Kazakhstan	100%	100%
Total	**100%**	**100%**

Main shareholders of JSC Halyk Bank Kazakhstan are JSC Holding ALMEX and JSC Accumulated Pension Fund. JSC Halyk Bank Kazakhstan is ultimately controlled by Timur Kulibayev and Dinara Kulibayeva.

These financial statements were authorised for issue on March 2, 2017 by the Management Board.

2. Significant accounting policies

Statement of compliance. These financial statements have been prepared in accordance with International Financial Reporting Standards ("IFRS").

These financial statements have been prepared on the assumption that the Bank is a going concern and will continue in operation for the foreseeable future, because of following

As of 31 December 2016 the Bank has cumulative liquidity gap of GEL 58,130 thousand. The short-term liabilities mainly consisted of the deposits received from the Parent entity, all of which were borrowed during the second half of the 2016. Excessive short-term funding caused the Bank to face negative liquidity gap as shown in note 27. The Management of the Bank believes that liquidity gap do not lead to going concern issue for the Bank as the Parent entity shows its commitment to continue financing Georgian operations. The commitment is evidenced in gradual increase of existing funding facilities from year to year and re-volving the short-term deposits when they come due. Before the issuance of the report short-term deposits in the amount of GEL 120,429 thousand have been matured. To meet the liquidity needs the Bank has re-volved GEL 75,800 thousand short-term deposits from the Parent entity with the maturity of 2 months. In addition, the Bank has received comfort letter from the Parent entity that express the readiness to support the operations in Georgia.

These financial statements are presented in *Georgian Lari ("GEL")*, unless otherwise indicated.

These financial statements have been prepared on the historical cost basis except for certain properties that are measured at revalued amounts at the end of each reporting period, as explained in the accounting policies below.

Historical cost is generally based on the fair value of the consideration given in exchange for goods and services.

Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date, regardless of whether that price is directly observable or estimated using another valuation technique. In estimating the fair value of an asset or a liability, the Bank takes into account the characteristics of the asset or liability if market participants would take those characteristics into account when pricing the asset or liability at the measurement date. Fair value for measurement and/or disclosure purposes in these financial statements is determined on such a basis.

In addition, for financial reporting purposes, fair value measurements are categorised into Level 1, 2 or 3 based on the degree to which the inputs to the fair value measurements are observable and the significance of the inputs to the fair value measurement in its entirety, which are described as follows:

- Level 1 inputs are quoted prices (unadjusted) in active markets for identical assets or liabilities that the entity can access at the measurement date;
- Level 2 inputs are inputs, other than quoted prices included within Level 1, that are observable for the asset or liability, either directly or indirectly; and
- Level 3 inputs are unobservable inputs for the asset or liability.

The Bank is registered in Georgia and maintains its accounting records in accordance with Georgian law. These financial statements have been prepared from the statutory accounting records and have been adjusted to conform to IFRS.

The Bank presents its statement of financial position broadly in order of liquidity. An analysis regarding recovery or settlement within 12 months after the statement of financial position date (current) and more than 12 months after the statement of financial position date (non-current) is presented in Note 27.

Functional currency. Items included in the financial statements of the Bank are measured using the currency of the primary economic environment in which the Bank operates ("the functional currency"). The functional currency of the Bank is the Georgian Lari ("GEL"). The presentation currency of the financial statements of the Bank is the GEL. All values are rounded to the nearest thousand Lari, except when otherwise indicated.

Offsetting. Financial assets and financial liabilities are offset and the net amount reported in the statement of financial position only when there is a legally enforceable right to offset the recognized amounts and there is an intention to settle on a net basis, or to realize the assets and settle the liability simultaneously. Income and expense is not offset in the statement of profit or loss and other comprehensive income unless required or permitted by any accounting standard or interpretation, and as specifically disclosed in the accounting policies of the Bank.

The principal accounting policies are set out below.

Recognition of interest income and expense. Interest income from a financial asset is recognized when it is probable that the economic benefits will flow to the Bank and the amount of income can be measured reliably. Interest income and expense are recognized on an accrual basis using the effective interest method. The effective interest method is a method of calculating the amortized cost of a financial asset or a financial liability (or group of financial assets or financial liabilities) and of allocating the interest income or interest expense over the relevant period.

The effective interest rate is the rate that exactly discounts estimated future cash receipts (including all fees on points paid or received that form an integral part of the effective interest rate, transaction costs and other premiums or discounts) through the expected life of the debt instrument, or (where appropriate) a shorter period, to the net carrying amount on initial recognition.

Once a financial asset or a group of similar financial assets has been written down (partly written down) as a result of an impairment loss, interest income is thereafter recognized using the rate of interest used to discount the future cash flows for the purpose of measuring the impairment loss.

Recognition of fee and commission income. Loan origination fees are deferred, together with the related direct costs, and recognized as an adjustment to the effective interest rate of the loan. Where it is probable that a loan commitment will lead to a specific lending arrangement, the loan commitment fees are deferred, together with the related direct costs, and recognized as an adjustment to the effective interest rate of the resulting loan. Where it is unlikely that a loan commitment will lead to a specific lending arrangement, the loan commitment fees are recognized in profit or loss over the remaining period of the loan commitment. Where a loan commitment expires without resulting in a loan, the loan commitment fee is recognized in profit or loss on expiry. All other commissions are recognized when services are provided.

Financial instruments. The Bank recognizes financial assets and liabilities in its statement of financial position when it becomes a party to the contractual obligations of the instrument. Regular way purchases and sales of financial assets and liabilities are recognized using settlement date accounting. Regular way purchases or sales are purchases or sales of financial assets that require delivery of assets within the time frame established by regulation or convention in the marketplace.

Financial assets and financial liabilities are initially measured at fair value. Transaction costs that are directly attributable to the acquisition or issue of financial assets and financial liabilities (other than financial assets and financial liabilities at fair value through profit or loss) are added to or deducted from the fair value of the financial assets or financial liabilities, as appropriate, on initial recognition. Transaction costs directly attributable to the acquisition of financial assets or financial liabilities at fair value through profit or loss are recognized immediately in profit or loss.

Financial assets. Financial assets are classified into the following specified categories: financial assets 'at fair value through profit or loss' ("FVTPL"), 'held to maturity' ("HTM") investments, 'available-for-sale' ("AFS") financial assets and 'loans and receivables'. The classification depends on the nature and purpose of the financial assets and is determined at the time of initial recognition.

The principal financial assets of the Bank are cash and cash equivalents, mandatory cash balance with the NBG, investments available-for-sale, investments held to maturity and loans and receivables.

Cash and cash equivalents. Cash and cash equivalents consist of cash on hand, unrestricted balances on correspondent and term deposits with the National Bank of Georgia (the "NBG") with original maturity of less or equal to 90 days and amounts due from credit institutions with original maturity of less or equal to 90 days and are free from contractual encumbrances.

Mandatory cash balance with the National Bank of Georgia. Mandatory cash balance with the National Bank of Georgia (the "NBG") is carried at amortised cost and represent interest bearing mandatory reserve deposits, which are not available to finance the Bank's day to day operations and hence are not considered as part of cash and cash equivalents for the purposes of the statement of cash flows.
Available-for-sale financial assets. Available-for-sale financial assets are non-derivatives that are either designated as available-for-sale or are not classified as (a) loans and receivables, (2) held to maturity investments or (c) financial assets at fair value through profit or loss.

AFS equity investments that do not have a quoted market price in an active market and whose fair value cannot be reliably measured are measured at cost less any identified impairment losses at the end of each reporting period.

Investments held to maturity. Investments held to-maturity are non-derivative financial assets with fixed or determinable payments and fixed maturity dates that the Bank has the positive intent and ability to hold to maturity. Investments held to maturity investments are measured at amortized cost using the effective interest method less any impairment.

If the Bank were to sell or reclassify more than an insignificant amount of investments held to maturity before maturity (other than in certain specific circumstances), the entire category would be tainted and would have to be reclassified as available-for-sale. Furthermore, the Bank would be prohibited from classifying any financial asset as held to maturity during current financial year and following two financial years.

Loans and receivables. Trade receivables, loans, and other receivables that have fixed or determinable payments that are not quoted in an active market (including due from banks balances, loans to customers and other financial assets) are classified as 'loans and receivables'. Loans and receivables are measured at amortized cost using the effective interest method, less any impairment. Interest income is recognized by applying the effective interest rate, except for short-term receivables when the recognition of interest would be immaterial.

Impairment of financial assets. Financial assets, other than those at FVTPL, are assessed for indicators of impairment at the end of each reporting period. Financial assets are considered to be impaired when there is objective evidence that, as a result of one or more events that occurred after the initial recognition of the financial asset, the estimated future cash flows of the investment have been affected.

For listed and unlisted equity investments classified as AFS, a significant or prolonged decline in the fair value of the security below its cost is considered to be objective evidence of impairment.

For all other financial assets, objective evidence of impairment could include:

- Significant financial difficulty of the issuer or counterparty; or
- Breach of contract, such as default or delinquency in interest or principal payments;
- Default or delinquency in interest or principal payments; or
- It becoming probable that the borrower will enter bankruptcy or financial re-organisation; or
- Disappearance of an active market for that financial asset because of financial difficulties.

For certain categories of financial asset, such as loans and receivables, assets that are assessed not to be impaired individually are, in addition, assessed for impairment on a collective basis. Objective evidence of impairment for a portfolio of loans and receivables could include the Bank's past experience of collecting payments, an increase in the number of delayed payments in the portfolio, as well as observable changes in national or local economic conditions that correlate with default on receivables.

For financial assets carried at amortised cost, the amount of the impairment loss recognised is the difference between the asset's carrying amount and the present value of estimated future cash flows, discounted at the financial asset's original effective interest rate.

For financial assets carried at cost, the amount of the impairment loss is measured as the difference between the asset's carrying amount and the present value of the estimated future cash flows discounted at the current market rate of return for a similar financial asset. Such impairment loss will not be reversed in subsequent periods.

The carrying amount of the financial asset is reduced by the impairment loss directly for all financial assets with the exception of loans and receivables, where the carrying amount is reduced through the use of an allowance account. When a loan or a receivable is considered uncollectible, it is written off against the allowance account. Subsequent recoveries of amounts previously written off are credited against the allowance account. Changes in the carrying amount of the allowance account are recognised in profit or loss.

For financial assets measured at amortized cost, if, in a subsequent period, the amount of the impairment loss decreases and the decrease can be related objectively to an event occurring after the impairment was recognized, the previously recognized impairment loss is reversed through profit or loss to the extent that the carrying amount of the investment at the date the impairment is reversed does not exceed what the amortized cost would have been had the impairment not been recognized.

Renegotiated loans. Where possible, the Bank seeks to restructure loans rather than to take possession of collateral. This may involve extending the payment arrangements and the agreement of new loan conditions. Once the terms have been renegotiated any impairment is measured using the original effective interest rate as calculated before the modification of terms and the loan is no longer considered past due. Management continually reviews renegotiated loans to ensure that all criteria are met and that future payments are likely to occur. The loans continue to be subject to an individual or collective impairment assessment, calculated using the loan's original effective interest rate.

Write off of loans and advances. Loans and advances are written off against the allowance for impairment losses when deemed uncollectible. Loans and advances are written off after management has exercised all possibilities available to collect amounts due to the Bank and after the Bank has sold all available collateral. Subsequent recoveries of amounts previously written off are reflected as an offset to the charge for impairment of financial assets in the statement of profit or loss and other comprehensive income in the period of recovery.

Derecognition of financial assets. The Bank derecognizes a financial asset only when the contractual rights to the cash flows from the asset expire, or when it transfers the financial asset and substantially all the risks and rewards of ownership of the asset to another party. If the Bank neither transfers nor retains substantially all the risks and rewards of ownership and continues to control the transferred asset, the Bank recognizes its retained interest in the asset and an associated liability for amounts it may have to pay. If the Bank retains substantially all the risks and rewards of ownership of a transferred financial asset, the Bank continues to recognise the financial asset and also recognises a collateralised borrowing for the proceeds received.

On derecognition of a financial asset in its entirety, the difference between the asset's carrying amount and the sum of the consideration received and receivable and the cumulative gain of loss that had been recognized in other comprehensive income and accumulated in equity is recognized in profit or loss.

Financial liabilities and equity instruments issued

<u>Classification as debt or equity.</u> Debt and equity instruments issued by a Bank entity are classified as either financial liabilities or as equity in accordance with the substance of the contractual arrangements and the definitions of a financial liability and an equity instrument.

<u>Equity instruments.</u> An equity instrument is any contract that evidences a residual interest in the assets of an entity after deducting all of its liabilities. Equity instruments issued by the Bank are recognised at the proceeds received, net of direct issue costs.

Financial liabilities. Financial liabilities, including deposits by banks, deposits by customers, borrowed funds, subordinated debt and other financial liabilities are initially measured at fair value, net of transaction costs.

Other financial liabilities are subsequently measured at amortised cost using the effective interest method, with interest expense recognised on an effective yield basis.

The effective interest method is a method of calculating the amortized cost of a financial liability and of allocating interest expense over the relevant period. The effective interest rate is the rate that exactly discounts estimated future cash payments (including all fees and points paid or received that form an integral part of the effective interest rate, transaction costs and other premiums or discounts) through the expected life of the financial liability, or (where appropriate) a shorter period, to the net carrying amount on initial recognition.

Financial guarantee contracts. A financial guarantee contract is a contract that requires the issuer to make specified payments to reimburse the holder for a loss it incurs because a specified debtor fails to make payments when due in accordance with the terms of a debt instrument.

Financial guarantee contracts issued by the Bank are initially measured at their fair values and, if not designated as at FVTPL, are subsequently measured at the higher of:

- The amount of the obligation under the contract, as determined in accordance with IAS 37 *Provisions, Contingent Liabilities and Contingent Assets* ; and
- The amount initially recognized less, where appropriate, cumulative amortization recognized in accordance with the revenue recognition policies.

Derecognition of financial liabilities. The Bank derecognises financial liabilities when, and only when, the Bank's obligations are discharged, cancelled or have expired. 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. The difference between the carrying amount of the financial liability derecognized and the consideration paid and payable is recognized in profit and loss.

Leases. Leases are classified as finance leases whenever the terms of the lease transfer substantially all the risks and rewards of ownership to the lessee. All other leases are classified as operating leases.

The Bank as lessee. Operating lease payments are recognised as an expense on a straight-line basis over the lease term, except where another systematic basis is more representative of the time pattern in which economic benefits from the leased asset are consumed. Contingent rentals arising under operating leases are recognised as an expense in the period in which they are incurred.

In the event that lease incentives are received to enter into operating leases, such incentives are recognised as a liability. The aggregate benefit of incentives is recognised as a reduction of rental expense on a straight-line basis, except where another systematic basis is more representative of the time pattern in which economic benefits from the leased asset are consumed.

Repossessed assets. In certain circumstances, assets are repossessed following the foreclosure on loans that are in default. Repossessed assets are measured at the lower of carrying amount and fair value less costs to sell.

Property and equipment. Buildings held for use in supply of goods or services, or for administrative purposes, are stated in the statement of financial position at their revalued amounts, being the fair value at the date of revaluation, less any subsequent accumulated depreciation and subsequent accumulated impairment losses. Revaluations are performed with sufficient regularity such that the carrying amounts do not differ materially from those that would be determined using fair values at the end of each reporting period.

Any revaluation increase arising on the revaluation of such premises is recognised in other comprehensive income and accumulated in equity, except to the extent that it reverses a revaluation decrease for the same asset previously recognised in profit or loss, in which case the increase is credited to profit or loss to the extent of the decrease previously expensed. A decrease in the carrying amount arising on the revaluation of such premises is recognised in profit or loss to the extent that it exceeds the balance, if any, held in the revaluation reserve for premises relating to a previous revaluation of that asset.

(in thousands of Georgian Lari)

Properties in the course of construction for production, supply or administrative purposes are carried at cost, less any recognised impairment loss. Cost includes professional fees and, for qualifying assets, borrowing costs capitalised in accordance with the Bank's accounting policy. Such properties are classified to the appropriate categories of premises and equipment when completed and ready for intended use. Depreciation of these assets, on the same basis as other property assets, commences when the assets are ready for their intended use.

Depreciation on revalued premises is recognised in profit or loss. On the subsequent sale or retirement of revalued premises, the attributable revaluation surplus remaining in the revaluation reserve for premises is transferred directly to retained earnings.

Freehold land is not depreciated.

Depreciation is recognised so as to write off the cost or valuation of assets (other than freehold land and properties under construction) less their residual values over their useful lives, using the straight-line method. The estimated useful lives, residual values and depreciation method are reviewed at the end of each reporting period, with the effect of any changes in estimate accounted for on a prospective basis at the following annual rates:

Buildings and other real estate	1%-2%
Furniture and fixtures	10%-15%
Computer and communication equipment	10%-33.33%
Vehicles	10%-33.33%
Leasehold improvement	20%-50%
Other	15%

An item of property and equipment is derecognized upon disposal or when no future economic benefits are expected to arise from the continued use of the asset. Any gain or loss arising on the disposal or retirement of an item of property and equipment is determined as the difference between the sales proceeds and the carrying amount of the asset and is recognized in profit or loss.

Intangible Assets. Intangible assets with finite useful lives that are acquired separately are carried at cost less accumulated amortization and accumulated impairment losses, if any. Amortization is recognized on a straight-line basis over their estimated useful lives of 15 years. The estimated useful life and amortization method are reviewed at the end of each reporting period, with the effect of any changes in estimate being accounted for on a prospective basis. Intangible assets with indefinite useful lives that are acquired separately are carried at cost less accumulated impairment losses.

An intangible asset is derecognized on disposal, or when no future economic benefits are expected from use or disposal. Gains or losses arising from derecognition of an intangible asset, measured as the difference between the net disposal proceeds and the carrying amount of the asset, are recognized in profit or loss when the asset is derecognized.

<u>Derecognition of intangible assets.</u> An intangible asset is derecognised on disposal, or when no future economic benefits are expected from use or disposal. Gains or losses arising from derecognition of an intangible asset, measured as the difference between the net disposal proceeds and the carrying amount of the asset, are recognised in profit or loss when the asset is derecognised.

<u>Impairment of tangible and intangible assets other than goodwill.</u> At the end of each reporting period, the Bank reviews the carrying amounts of its tangible and intangible assets to determine whether there is any indication that those assets have suffered an impairment loss. If any such indication exists, the recoverable amount of the asset is estimated in order to determine the extent of the impairment loss (if any). When it is not possible to estimate the recoverable amount of an

individual asset, the Bank estimates the recoverable amount of the cash-generating unit to which the asset belongs. When a reasonable and consistent basis of allocation can be identified, corporate assets are also allocated to individual cash-generating units, or otherwise they are allocated to the smallest group of cash-generating units for which a reasonable and consistent allocation basis can be identified.

Intangible assets with indefinite useful lives and intangible assets not yet available for use are tested for impairment at least annually, and whenever there is an indication that the asset may be impaired.

Recoverable amount is the higher of 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 which the estimates of future cash flows have not been adjusted.

If the recoverable amount of an asset (or cash-generating unit) is estimated to be less than its carrying amount, the carrying amount of the asset (or cash-generating unit) is reduced to its recoverable amount. An impairment loss is recognised immediately in profit or loss, unless the relevant asset is carried at a revalued amount, in which case the impairment loss is treated as a revaluation decrease.

When an impairment loss subsequently reverses, the carrying amount of the asset (or a cash-generating unit) is increased to the revised estimate of its recoverable amount, but so that the increased carrying amount does not exceed the carrying amount that would have been determined had no impairment loss been recognised for the asset (or cash-generating unit) in prior years. A reversal of an impairment loss is recognised immediately in profit or loss, unless the relevant asset is carried at a revalued amount, in which case the reversal of the impairment loss is treated as a revaluation increase.

Taxation. Income tax expense represents the sum of the tax currently payable and deferred tax.

Current tax. The tax currently payable is based on taxable profit for the year. Taxable profit differs from profit as reported in the statement of profit or loss because of items of income or expense that are taxable or deductible in other years and items that are never taxable or deductible. The Bank's liability for current tax is calculated using tax rates that have been enacted or substantively enacted by the end of the reporting period.

Deferred tax. Deferred tax is recognised on temporary differences between the carrying amounts of assets and liabilities in the financial statements and the corresponding tax bases used in the computation of taxable profit. Deferred tax liabilities are generally recognised for all taxable temporary differences. Deferred tax assets are generally recognised for all deductible temporary differences to the extent that it is probable that taxable profits will be available against which those deductible temporary differences can be utilised. Such deferred tax assets and liabilities are not recognised if the temporary difference arises from the initial recognition of assets and liabilities in a transaction that affects neither the taxable profit nor the accounting profit.

The carrying amount of deferred tax assets is reviewed at the end of each reporting period and reduced to the extent that it is no longer probable that sufficient taxable profits will be available to allow all or part of the asset to be recovered.

Deferred tax assets and liabilities are measured at the tax rates that are expected to apply in the period in which the liability is settled or the asset realized, based on tax laws and rates that have been enacted or substantively enacted by the end of the reporting period.

The measurement of deferred tax liabilities and assets reflects the tax consequences that would follow from the manner in which the Bank expects, at the end of the reporting period, to recover or settle the carrying amount of its assets and liabilities.

Current and deferred tax for the year. Current and deferred tax are recognised in profit or loss, except when they relate to items that are recognised in other comprehensive income or directly in equity, in which case, the current and deferred tax are also recognised in other comprehensive income or directly in equity respectively.

(in thousands of Georgian Lari)

In May 2016, the parliament of Georgia approved a change in the current corporate taxation model, with changes applicable on 1 January 2019 for all entities apart from certain financial institutions. The changed model implies zero corporate tax rate on retained earnings and a 15% corporate tax rate on disbursed earnings, compared to previous model of 15% tax rate charged to the company's profit before tax, regardless of the retention or distribution status. The change has had an immediate impact on deferred tax asset and deferred tax liability balances attributable to previously recognised temporary differences arising from prior periods.

Operating taxes. Georgia also has various other taxes, which are assessed on the Bank's activities. These taxes are included as a component of operating expenses in the statement of profit or loss.

Provisions. Provisions are recognised when the Bank has a present obligation (legal or constructive) as a result of a past event, it is probable that the Bank will be required to settle the obligation, and a reliable estimate can be made of the amount of the obligation.

The amount recognised as a provision is the best estimate of the consideration required to settle the present obligation at the end of the reporting period, taking into account the risks and uncertainties surrounding the obligation. When a provision is measured using the cash flows estimated to settle the present obligation, its carrying amount is the present value of those cash flows (when the effect of the time value of money is material).

When some or all of the economic benefits required to settle a provision are expected to be recovered from a third party, a receivable is recognised as an asset if it is virtually certain that reimbursement will be received and the amount of the receivable can be measured reliably.

Contingencies. Contingent liabilities are not recognized in the statement of financial position but are disclosed unless the possibility of any outflow in settlement is remote. A contingent asset is not recognized in the statement of financial position but disclosed when an inflow of economic benefits is probable.

Foreign currencies. In preparing the financial statements of the Bank, transactions in currencies other than the entity's functional currency (foreign currencies) are recognised at the rates of exchange prevailing at the dates of the transactions. At the end of each reporting period, monetary items denominated in foreign currencies are retranslated at the rates prevailing at that date. Non-monetary items that are measured in terms of historical cost in a foreign currency are not retranslated.

Exchange differences on monetary items are recognized in profit or loss in the period in which they arise.

The exchange rates used by the Bank in the preparation of the financial statements as at year-end are as follows:

	December 31, 2016	December 31, 2015
GEL/1 US Dollar	2.6468	2.3949
GEL/1 Euro	2.7940	2.6169

Collateral. The Bank obtains collateral in respect of customer liabilities where this is considered appropriate. The collateral normally takes the form of a lien over the customer's assets and gives the Bank a claim on these assets for both existing and future customer liabilities.

Equity reserves. The reserve recorded in equity (other comprehensive income) on the Bank's statement of financial position includes property revaluation reserve which comprises revaluation reserve of land and building.

3. Critical accounting judgements and key sources of estimation uncertainty

In the application of the Bank's accounting policies the management is required to make judgements, estimates and assumptions about the carrying amounts of assets and liabilities that are not readily apparent from other sources. The estimates and associated assumptions are based on historical experience and other factors that are considered to be relevant. Actual results may differ from these estimates.

The estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognized in the period in which the estimate is revised if the revision affects only that period or in the period of the revision and future periods if the revision affects both current and future periods.

Critical judgements in applying accounting policies. The following are the critical judgements, apart from those involving estimations (see below), that the management has made in the process of applying the Banks's accounting policies and that have the most significant effect on the amounts recognized in the financial statements.

Investments held to maturity. The management has reviewed the Bank's investments held to maturity in the light of its capital maintenance and liquidity requirements and have confirmed the Bank's positive intention and ability to hold those assets to maturity. As at December 31, 2016 and 2015 the carrying amount of the investments held to maturity is GEL 16,757 thousand and GEL 19,283 thousand, respectively. Details of these assets are set out in Note 9.

Key sources of estimation uncertainty. The following are the key assumptions concerning the future, and other key sources of estimation uncertainty at the end of the reporting period, that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year.

Impairment of loans and receivables. The Bank's management regularly reviews its loans and receivables to assess for impairment. The Banks's loan impairment provisions are established to recognize incurred impairment losses in its portfolio of loans and receivables. The Bank's management considers accounting estimates related to allowance for impairment of loans and receivables a key source of estimation uncertainty because (i) they are highly susceptible to change from period to period as the assumptions about future default rates and valuation of potential losses relating to impaired loans and receivables are based on recent performance experience, and (ii) any significant difference between the Banks's estimated losses and actual losses would require the Bank to record provisions which could have a material impact on its financial statements in future periods.

The Bank uses management's judgment to estimate the amount of any impairment loss in cases where a borrower has financial difficulties and there are few available sources of historical data relating to similar borrowers. Similarly, the Bank estimates changes in future cash flows based on past performance, past customer behavior, observable data indicating an adverse change in the payment status of borrowers in a group, and national or local economic conditions that correlate with defaults on assets in the group. Management uses estimates based on historical loss experience for assets with credit risk characteristics and objective evidence of impairment similar to those in the group of loans. The Bank uses management's judgment to adjust observable data for a group of loans to reflect current circumstances not reflected in historical data. The Bank makes individual as well as group assessment of the loan portfolio for impairment.

The allowances for impairment of financial assets in the financial statements have been determined on the basis of existing economic and political conditions. The Bank is not in a position to predict what changes in conditions will take place in Georgia and what effect such changes might have on the adequacy of the allowances for impairment of financial assets in future periods.

As at December 31, 2016 and 2015 the gross loans to customers totaled GEL 278,954 thousand and GEL 204,398 thousand, respectively, and allowance for impairment losses on loans to customers amounted to GEL 5,453 thousand and GEL 2,788 thousand, respectively.

Property and equipment carried at revalued amounts. Certain properties are measured at revalued amounts. The latest appraisal was in May 2016. Details of the valuation techniques used are set out in Note 10.

Useful lives of property and equipment, and intangible assets. As described above, the Bank's management reviews the estimated useful lives of property, plant and equipment, and intangible assets at the end of each annual reporting period. The estimation of the useful life of an item of property, plant and equipment and intangible assets is a matter of management judgment based upon experience with similar assets. In determining useful life of an asset, management considers the expected usage, estimated technical obsolescence, physical wear and tear and the physical environment in which the asset is operated. Changes in any of these conditions or estimates may result in adjustment to future depreciation and amortization rates.

Recoverability of deferred tax assets. According to changes in Georgian Tax Code from January 1 2019 banks are obliged to pay income tax based on dividend disbursed. Consequently, there is an expectation that temporary differences will disappear beginning from that effective date. The management of the Bank is confident that no valuation allowance against deferred tax assets at the reporting date is considered necessary, because it is more likely that the deferred tax liability will be fully realized or the effect will be immaterial for the users of financial statements. The carrying value of deferred tax liabilities and assets amounted to GEL 1,720 thousand and GEL 877 thousand as at December 31, 2016 and 2015, respectively.

Initial recognition of related party transactions. In the normal course of business the Bank enters into transactions with its related parties. IAS 39 requires initial recognition of financial instruments based on their fair values. Judgement is applied in determining if transactions are priced at market or non-market interest rates, where there is no active market for such transactions. The basis for judgement is pricing for similar types of transactions with unrelated parties and effective interest rate analysis. The information on related party balances is disclosed in Note 28.

4. Application of new and revised international financial reporting standards (IFRSs)

Amendments to IFRSs affecting amounts reported in the financial statements. In the current year, the following new and revised Standards and Interpretations have been adopted and have affected the amounts reported in these financial statements.

- Amendments to IFRS 10, IFRS 12 and IAS 28 *Investment Entities: Applying the Consolidation Exception*;
- Amendments to IFRS 11 *Accounting for Acquisitions of Interests in Joint Operations*;
- Amendments to IAS 1 Disclosure Initiative;
- Amendments to IAS 16 and IAS 38 *Clarification of Acceptable Methods of Depreciation and Amortisation;*
- Amendments to IAS 16 and IAS 41 *Agriculture: Bearer Plants*;
- IFRS 14 *Regulatory Deferral Accounts*;
- Amendments to IAS 27 – *Equity Method in Separate Financial Statements*;
- Annual Improvements to IFRSs 2012-2014 Cycle

Amendments to IAS 1 Disclosure Initiative

The Bank has applied these amendments for the first time in the current year. The amendments clarify that an entity need not provide a specific disclosure required by an IFRS if the information resulting from that disclosure is not material, and give guidance on the bases of aggregating and disaggregating information for disclosure purposes. However, the amendments reiterate that a bank should consider providing additional disclosures when compliance with the specific requirements in IFRS is insufficient to enable users of financial statements to understand the impact of particular transactions, events and conditions on the bank's financial position and financial performance.

The application of these amendments has not resulted in any impact on the financial performance or financial position of the Bank.

Amendments to IAS 16 and IAS 38 Clarification of Acceptable Methods of Depreciation and Amortisation

The Bank has applied these amendments for the first time in the current year. The amendments to IAS 16 prohibit entities from using a revenue-based depreciation method for items of property, plant and equipment. The amendments to IAS 38 introduce a rebuttable presumption that revenue is not an appropriate basis for amortisation of an intangible asset. This presumption can only be rebutted in the following two limited circumstances:

a. when the intangible asset is expressed as a measure of revenue; or
b. when it can be demonstrated that revenue and consumption of the economic benefits of the intangible asset are highly correlated.

As the Bank already uses the straight-line method for depreciation and amortisation for its property, plant and equipment, and intangible assets respectively, the application of these amendments has had no impact on the Bank's consolidated financial statements.

Annual Improvements to IFRSs - 2012-2014 Cycle

The Bank has applied these amendments for the first time in the current year. The Annual Improvements to IFRSs 2012-2014 Cycle include a number of amendments to various IFRSs, which are summarised below.

The amendments to IFRS 5 introduce specific guidance in IFRS 5 for when an entity reclassifies an asset (or disposal group) from held for sale to held for distribution to owners (or vice versa). The amendments clarify that such a change should be considered as a continuation of the original plan of disposal and hence requirements set out in IFRS 5 regarding the change of sale plan do not apply. The amendments also clarifies the guidance for when held-for-distribution accounting is discontinued.

The amendments to IFRS 7 provide additional guidance to clarify whether a servicing contract is continuing involvement in a transferred asset for the purpose of the disclosures required in relation to transferred assets.

The amendments to IAS 19 clarify that the rate used to discount post-employment benefit obligations should be determined by reference to market yields at the end of the reporting period on high quality corporate bonds. The assessment of the depth of a market for high quality corporate bonds should be at the currency level (i.e. the same currency as the benefits are to be paid). For currencies for which there is no deep market in such high quality corporate bonds, the market yields at the end of the reporting period on government bonds denominated in that currency should be used instead.

The application of these amendments has had no significant effect on the Bank's financial statements.

New and revised IFRSs in issue but not yet effective.

The Bank has not applied the following new and revised IFRSs that have been issued but are not yet effective:

- IFRS 9 *Financial Instruments*[2];
- IFRS 15 *Revenue from Contracts with Customers*[2];
- IFRS 16 *Leases*
- Amendments to IFRS 2 – *Classification and Measurement of Share-based Payment Transactions*[2];
- Amendments to IFRS 10 and IAS 28 - *Sale or Contribution of Assets between an Investor and its Associate or Joint Venture*[4];
- Amendments to IAS 7 – *Disclosure Initiative*[1];

- Amendments to IAS 12 – *Recognition of Deferred Tax Assets for Unrealised Losses*[1];
- Amendments to IFRS 4 – *Applying IFRS 9 Financial Instruments with IFRS 4 Insurance Contracts*[2];
- IFRIC 22 *Foreign Currency Transactions and Advance Consideration*[2];
- Amendments to IAS 40 – *Transfers of Investment Property*[2];
- Annual Improvements to IFRSs 2014-2016 Cycle.

[1] Effective for annual periods beginning on or after 1 January 2017, with earlier application permitted.
[2] Effective for annual periods beginning on or after 1 January 2018, with earlier application permitted.
[3] Effective for annual periods beginning on or after 1 January 2019, with earlier application permitted.
[4] Effective for annual periods beginning on or after a date to be determined. Earlier application is permitted.

IFRS 9 *Financial Instruments.* IFRS 9 issued in November 2009 introduced new requirements for the classification and measurement of financial assets. IFRS 9 was subsequently amended in October 2010 to include requirements for the classification and measurement of financial liabilities and for derecognition, and in November 2013 to include the new requirements for general hedge accounting. In July 2014 IASB issued a finalised version of IFRS 9 mainly introducing impairment requirements for financial assets and limited amendments to the classification and measurement requirements by introducing a 'fair value through other comprehensive income' (FVTOCI) measurement category for certain simple debt instruments. IFRS 9 is aiming at replacing IAS 39 Financial Instruments: Recognition and Measurement.

The key requirements of IFRS 9 are:

- **Classification and measurement of financial liabilities.** Financial assets are classified by reference to the business model within which they are held and their contractual cash flow characteristics. Specifically, debt instruments that are held within the business model whose objective is to collect the contractual cash flows, and that have contractual cash flows that are solely payments of principal and interest on the principal outstanding are generally measured at amortised cost after initial recognition. The 2014 version of IFRS 9 introduces a 'fair value through other comprehensive income' category for debt instruments held within the business model whose objective is achieved both by collecting contractual cash flows and selling financial assets, and that have contractual terms of the financial asset giving rise on specified dates to cash flows that are solely payments of principal and interest on the principal amount outstanding which are measured at fair value through other comprehensive income after initial recognition. All other debt and equity investments are measured at their fair values. In addition, under IFRS 9, entities may make an irrevocable election to present subsequent changes in the fair value of an equity investment (that is not held for trading) in other comprehensive income, with only dividend income generally recognised in profit or loss.

  Financial liabilities are classified in a similar manner to under IAS 39, however there are differences in the requirements applying to the measurement of an entity's own credit risk. IFRS 9 requires that the amount of change in the fair value of the financial liability that is attributable to changes in the credit risk of that liability is presented in other comprehensive income, unless the recognition of the effects of changes in the liability's credit risk in OCI would create or enlarge an accounting mismatch in profit or loss. Changes in fair value attributable to a financial liability's credit risk are not subsequently reclassified to profit or loss.
- **Impairment.** The 2014 version of IFRS 9 introduces an 'expected credit loss' model for the measurement of the impairment of financial assets, as opposed to an incurred credit loss model under IAS 39. The expected credit loss model requires an entity to account for expected credit losses and changes in those expected credit losses at each reporting date to reflect changes in credit risk since initial recognition. In other words, it is no longer necessary for a credit event to have occurred before a credit loss is recognized.
- **Hedge accounting.** The new general hedge accounting requirements retain the three types of hedge accounting mechanisms currently available in IAS 39. Under IFRS 9, greater

flexibility has been introduced to the types of transactions eligible for hedge accounting, specifically broadening the types of instruments that qualify for hedging instruments and the types of risk components of non-financial items that are eligible for hedge accounting. In addition, the effectiveness test has been overhauled and replaced with the principle of an 'economic relationship'. Retrospective assessment of hedge effectiveness is also no longer required. Enhanced disclosure requirements about an entity's risk management activities have also been introduced.

- **Derecognition.** The requirements for the derecognition of financial assets and liabilities are carried forward from IAS 39.

The standard is effective from 1 January 2018 with early application permitted. Depending on the chosen approach to applying IFRS 9, the transition can involve one or more than one date of initial application for different requirements.

The management of the Bank anticipates that the application of IFRS 9 in the future may have a significant impact on amounts reported in respect of the Bank's financial assets and financial liabilities. However, it is not practicable to provide a reasonable estimate of the effect of IFRS 9 until a detailed review has been completed.

IFRS 15 *Revenue from Contracts with Customers.* In May 2014, IFRS 15 was issued which establishes a single comprehensive model for entities to use in accounting for revenue arising from contracts with customers. IFRS 15 will supersede the current revenue recognition guidance including IAS 18 *Revenue*, IAS 11 *Construction Contracts* and the related interpretations when it becomes effective.

The core principle of IFRS 15 is that an entity should recognise revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods and services. Specifically, the standard provides a single, principles based five-step model to be applied to all contracts with customers.

The five steps in the model are as follows:

- Identify the contract with the customer;
- Identify the performance obligations in the contract;
- Determine the transaction price;
- Allocate the transaction price to the performance obligations in the contracts;
- Recognise revenue when (or as) the entity satisfies a performance obligation.

Under IFRS 15, an entity recognises revenue when or as a performance obligation is satisfied, i.e. when 'control' of the goods or services underlying the particular performance obligation is transferred to the customer. Far more prescriptive guidance has been added on topics such as the point in which revenue is recognised, accounting for variable consideration, costs of fulfilling and obtaining a contract and various related matters. Furthermore, extensive disclosures are required by IFRS 15

The management of the Bank anticipates that the application of IFRS 15 in the future may have a significant impact on the amount and timing of revenue recognition. However, it is not practicable to provide a reasonable estimate of the effect of IFRS 15 until a detailed review has been completed.

Amendments to IFRS 16 – Leases. IFRS 16 specifies how an IFRS reporter will recognize measure, present and disclose leases. The standard provides a single lessee accounting model, requiring lessees to recognize assets and liabilities for all the leases unless the lease term is 12 months or less or underlying asset has a low value. Lessors continue to classify leases as operating or finance, with IFRS 16s approach to lessor accounting substantially unchanged from its predecessor, IAS 17.

Amendments to IFRS 2 *Classification and Measurement of Share-based Payment Transactions*

The amendments clarify the following:

1. In estimating the fair value of a cash-settled share-based payment, the accounting for the effects of vesting and non-vesting conditions should follow the same approach as for equity-settled share-based payments.
2. Where tax law or regulation requires an entity to withhold a specified number of equity instruments equal to the monetary value of the employee's tax obligation to meet the employee's tax liability which is then remitted to the tax authority, i.e. the share-based payment arrangement has a 'net settlement feature', such an arrangement should be classified as equity-settled in its entirety, provided that the share-based payment would have been classified as equity-settled had it not included the net settlement feature.
3. A modification of a share-based payment that changes the transaction from cash-settled to equity-settled should be accounted for as follows:

   a. the original liability is derecognised;
   b. the equity-settled share-based payment is recognised at the modification date fair value of the equity instrument granted to the extent that services have been rendered up to the modification date; and
   c. any difference between the carrying amount of the liability at the modification date and the amount recognised in equity should be recognised in profit or loss immediately.

The amendments are effective for annual reporting periods beginning on or after 1 January 2018 with earlier application permitted. Specific transition provisions apply.
The management of the Bank does not anticipate that the application of the amendments in the future will have a significant impact on the Bank's financial statements as the Bank does not have any cash-settled share-based payment arrangements or any withholding tax arrangements with tax authorities in relation to share-based payments.

Amendments to IFRS 10 and IAS 28 Sale or Contribution of Assets between an Investor and its Associate or Joint Venture

The amendments to IFRS 10 and IAS 28 deal with situations where there is a sale or contribution of assets between an investor and its associate or joint venture. Specifically, the amendments state that gains or losses resulting from the loss of control of a subsidiary that does not contain a business in a transaction with an associate or a joint venture that is accounted for using the equity method, are recognised in the parent's profit or loss only to the extent of the unrelated investors' interests in that associate or joint venture. Similarly, gains and losses resulting from the remeasurement of investments retained in any former subsidiary (that has become an associate or a joint venture that is accounted for using the equity method) to fair value are recognised in the former parent's profit or loss only to the extent of the unrelated investors' interests in the new associate or joint venture.

The effective date of the amendments has yet to be set by the IASB; however, earlier application of the amendments is permitted.
The management of the Bank anticipates that the application of these amendments may have an impact on the Bank's financial statements in future periods should such transactions arise.

Amendments to IAS 7 Disclosure Initiative

The amendments require an entity to provide disclosures that enable users of financial statements to evaluate changes in liabilities arising from financing activities.

The amendments apply prospectively for annual periods beginning on or after 1 January 2017 with earlier application permitted. The management of the Bank does not anticipate that the application of these amendments will have a material impact on the Bank's financial statements.

Amendments to IAS 12 Recognition of Deferred Tax Assets for Unrealised Losses

The amendments clarify the following:

1. Decreases below cost in the carrying amount of a fixed-rate debt instrument measured at fair value for which the tax base remains at cost give rise to a deductible temporary difference, irrespective of whether the debt instrument's holder expects to recover the carrying amount of the debt instrument by sale or by use, or whether it is probable that the issuer will pay all the contractual cash flows;
2. When an entity assesses whether taxable profits will be available against which it can utilise a deductible temporary difference, and the tax law restricts the utilisation of losses to deduction against income of a specific type (e.g. capital losses can only be set off against capital gains), an entity assesses a deductible temporary difference in combination with other deductible temporary differences of that type, but separately from other types of deductible temporary differences;
3. The estimate of probable future taxable profit may include the recovery of some of an entity's assets for more than their carrying amount if there is sufficient evidence that it is probable that the entity will achieve this; and
4. In evaluating whether sufficient future taxable profits are available, an entity should compare the deductible temporary differences with future taxable profits excluding tax deductions resulting from the reversal of those deductible temporary differences.

The amendments apply retrospectively for annual periods beginning on or after 1 January 2017 with earlier application permitted. The management of the Bank does not anticipate that the application of these amendments will have a material impact on the Bank's financial statements.

Amendments to IFRS 4 Applying IFRS 9 Financial Instruments with IFRS 4 Insurance Contracts

The amendments provide entities meeting a criterion for engaging in predominantly insurance activities with the option to continue current IFRS accounting and to defer the application of IFRS 9 until the earlier of the application of the new insurance Standard or periods beginning on or after 1 January 2021 (the "sunset clause"). The assessment of predominance has to be made at the reporting entity level and at the annual reporting date immediately preceding 1 April 2016. Thereafter it should not be reassessed, unless there is a significant change in the entity's activities that would trigger a mandatory reassessment. An entity shall apply those amendments, which permit insurers that meet specified criteria to apply a temporary exemption from IFRS 9, for annual periods beginning on or after 1 January 2018.

Separately, the amendments provide all entities with contracts within the scope of IFRS 4 with an option to apply IFRS 9 in full but to make adjustments to profit or loss to remove the impact of IFRS 9, compared with IAS 39, for designated qualifying financial assets. This is referred to as the 'overlay approach' and is available on an asset-by asset basis with specific requirements around designations and de-designations. An entity shall apply those amendments, which permit insurers to apply the overlay approach to designated financial assets, when it first applies IFRS 9.

The management of the Bank does not anticipate that the application of these amendments will have a material impact on the Bank's financial statements as the Bank does not have any insurance contracts to which IFRS 4 applies.

IFRIC 22 Foreign Currency Transactions and Advance Consideration

The Interpretation clarifies that when an entity pays or receives consideration in advance in a foreign currency, the date of the transaction for the purpose of determining the exchange rate to use on initial recognition of the related asset, expense or income is the date of the advance consideration, i.e. when the prepayment or liability in respect of the income received in advance was recognised. If there is more than one advance payment or receipt the date of the transaction for each payment of receipt of advance consideration should be determined. The amendments apply to annual periods beginning on or after 1 January 2018 with earlier application permitted. Entities may elect to apply amendments either retrospectively or prospectively.

The management of the Bank does not anticipate that the application of these amendments will have a material impact on the Bank's financial statements as the Bank currently uses the approach prescribed in IFRIC 22.

Amendments to IAS 40 Transfers of Investment Property

The amendments are intended to clarify that an entity can only reclassify a property to/ from investment property when, and only when, there is evidence that a change in the use of the property has occurred. The amendments emphasise that a change in management's intentions alone would not be enough to support a transfer of property. The standard has a list of circumstances that evidence a change in use, which is perceived by some as being exhaustive, the amendments make it clear that they are only examples. The amendments apply to annual periods beginning on or after 1 January 2018 with earlier application permitted. Entities may elect to apply them either retrospectively (if it is possible without the use of hindsight) or prospectively.
The management of the Bank does not anticipate that the application of these amendments will have a material impact on the Bank's financial statements.

Annual Improvements to IFRSs 2014-2016 Cycle

This annual improvements package amended three standards:

The Amendments to IFRS 1 delete the short-term exemptions that related to disclosures about financial instruments, employee benefits and investment entities as the reporting period to which the exemptions applied have already passed and as such, these exemptions are no longer applicable. The amendments are effective for annual periods beginning on or after 1 January 2018.

The amendments to IFRS 12 clarify that concession from the requirement to provide summarised financial information in respect of interests in subsidiaries, associates or joint ventures classified as held for sale or included in a disposal group is the only concession available for such interests. The amendments apply retrospectively and are effective for annual periods beginning on or after 1 January 2017.

In accordance with IAS 28, a venture capital organisation and other similar entities may elect to measure investments in associates and joint ventures at FVTPL. In addition, an entity that is not an investment entity but has an interest in an associate or joint venture that is an investment entity, may, when applying the equity method, elect to retain the fair value measurement applied by that associate or joint venture to its own interests in subsidiaries. Amendments to IAS 28 clarify that such election should be made separately for each associate or joint venture at initial recognition. The amendments apply retrospectively and are effective for annual periods beginning on or after 1 January 2018. Early application is permitted.

The management of the Bank does not anticipate that the application of these amendments will have a material impact on the Bank's financial statements.

(in thousands of Georgian Lari)

5. Cash and cash equivalents

	December 31, 2016	December 31, 2015
Cash	6,509	4,362
Balances with the NBG	3,186	3,687
Correspondent accounts and time deposits with original maturities up to 90 days	20,934	6,409
Total cash and cash equivalents	**30,629**	**14,458**

6. Due from banks

Due from banks comprise:

	December 31, 2016	December 31, 2015
Time deposits	871	239
Less: allowance for impairment losses	-	-
Total due from banks	**871**	**239**

As at December 31, 2016 and 2015 total due from banks represent guarantee deposits placed by the Bank for its VISA banking operations.

7. Loans to customers

Loans to customers comprise:

	December 31, 2016	December 31, 2015
Loans to customers	278,954	204,398
Less: allowance for impairment losses	(5,453)	(2,788)
Total loans to customers	**273,501**	**201,610**

Movements in the allowance for impairment losses for the years ended December 31, 2016 and 2015 are disclosed in Note 19.

As at December 31, 2016 and 2015 loans to customers included accrued interest in the amount of GEL 2,870 thousand and GEL 2,099 thousand, respectively.

(in thousands of Georgian Lari)

The table below summarizes carrying value of loans to customers analysed by sector:

	December 31, 2016	December 31, 2015
Loans to legal entities		
Trade and service	151,380	116,142
Construction	28,152	16,661
Mining	8,189	5,633
Agriculture	7,711	4,834
Energetics	5,239	-
Other sector	10,746	8,623
Total loans to legal entities	**211,417**	**151,893**
Loans to individuals		
Consumer loans	37,139	33,242
Mortgage loans	30,398	19,263
Total loans to Individuals	**67,537**	**52,505**
Gross loans to customers	**278,954**	**204,398**
Less: allowance for impairment losses	(5,453)	(2,788)
Total loans to customers	**273,501**	**201,610**

As at December 31, 2016 and 2015 the Bank granted loans to 9 and 6 customers totaling GEL 53,047 thousand and GEL 31,762 thousand, respectively, which individually exceeded 5% of the Bank's equity.

The table below summarizes carrying value of loans to customers analysed by type of collateral obtained by the Bank:

	December 31, 2016	December 31, 2015
Loans collateralized by combined collateral	190,833	130,914
Loans collateralized by pledge of real estate	72,019	60,386
Loans collateralized by cash	9,761	8,517
Loans collateralized by guarantees	1,118	1,216
Unsecured loans	5,223	3,365
Gross loans to customers	278,954	204,398
Less: allowance for impairment losses	(5,453)	(2,788)
Total loans to customers	**273,501**	**201,610**

As at December 31, 2016 and 2015 significant amount of customers (99% of total loans to customers) is granted to companies operating in Georgia, which represents a significant geographical concentration in one region.

As at December 31, 2016 and 2015 loans to customers included loans totaling GEL 11,731 thousand and GEL 8,781 thousand, respectively, whose terms were renegotiated. Otherwise these loans would be past due or impaired.

(in thousands of Georgian Lari)

Analysis by credit quality of loans to customers outstanding as at 31 December 2016 and 2015 was as follows:

As at December 31, 2016	Gross loans	Provision for impairment	Net loans	Provision for impairment to gross loans
Collectively assessed				
Not past due	211,585	(1,607)	209,978	0.76%
Overdue:				
up to 30 days	5,569	(159)	5,410	2.86%
31 to 60 days	3,581	(149)	3,432	4.16%
61 to 90 days	5,320	(420)	4,900	7.89%
91 to 180 days	1,815	(158)	1,657	8.71%
over 180 days	1,772	(205)	1,567	11.57%
Total collectively assessed loans	**229,642**	**(2,698)**	**226,944**	**1.18%**
Individually assessed				
Not past due	20,755	(369)	20,386	1.78%
Overdue:				
up to 30 days	24,450	(1,065)	23,385	4.36%
31 to 60 days	1,456	(161)	1,295	11.06%
61 to 90 days	2,651	(1,160)	1,491	43.76%
91 to 180 days	-	-	-	-
over 180 days	-	-	-	-
Total individually assessed loans	**49,312**	**(2,755)**	**46,557**	**5.59%**
Total loans to customers	**278,954**	**(5,453)**	**273,501**	**1.96%**

As at December 31, 2015	Gross loans	Provision for impairment	Net loans	Provision for impairment to gross loans
Collectively assessed				
Not past due	148,922	(934)	147,988	0.63%
Overdue:				
up to 30 days	9,467	(172)	9,295	1.82%
31 to 60 days	971	(28)	943	2.88%
61 to 90 days	611	(19)	592	3.11%
91 to 180 days	1,720	(140)	1,580	8.14%
over 180 days	496	(57)	439	11.49%
Total collectively assessed loans	**162,187**	**(1,350)**	**160,837**	**0.83%**
Individually assessed				
Not past due	32,796	(776)	32,020	2.37%
Overdue:				
up to 30 days	9,415	(662)	8,753	7.03%
31 to 60 days	-	-	-	-
61 to 90 days	-	-	-	-
91 to 180 days	-	-	-	-
over 180 days	-	-	-	-
Total individually assessed loans	**42,211**	**(1,438)**	**40,773**	**3.41%**
Total loans to customers	**204,398**	**(2,788)**	**201,610**	**1.37%**

(in thousands of Georgian Lari)

The table below summarizes an analysis of loans to customers by type of impairment:

	December 31, 2016			December 31, 2015		
	Carrying value before allowance	Allowance for impairment losses	Carrying value	Carrying value before allowance	Allowance for impairment losses	Carrying value
Loans to customers individually determined to be impaired	8,000	(1,324)	6,676	3,924	(1,025)	2,899
Loans to customers collectively determined to be impaired	270,954	(4,129)	266,825	200,474	(1,763)	198,711
Unimpaired loans	-	-	-	-	-	-
Total	**278,954**	**(5,453)**	**273,501**	**204,398**	**(2,788)**	**201,610**

During 2016 the Bank received non-financial asset by taking possession of collateral it held as security for loans. As at December 31, 2016 the carrying value of the asset was GEL 391 thousand included in other assets as repossessed assets.

8. Available-for-sale financial assets

Available-for-sale financial assets comprise:

	% of ownership	December 31, 2016	December 31, 2015
OJSC United Clearing Center	6,25%	54	54
Total available-for-sale financial assets		**54**	**54**

Management could not reliably estimate the fair value of the Bank's investment in the shares of OJSC United Clearing Center. This investment is carried at cost. This investee company has not published its recent financial information about its operations, its shares are not quoted and recent trade prices are not publicly accessible as at December 31, 2016.

9. Investments held to maturity

	December 31, 2016		December 31, 2015	
	Nominal annual interest rate	Amount	Nominal annual interest rate	Amount
Treasury bills	6.8%-15.2%	16,900	6.8%-15.2%	19,468
Less: discount		(143)		(185)
Total investments held to maturity		**16,757**		**19,283**

As at December 31, 2016 and 2015 interest accrued on investments held to maturity represents GEL 668 thousand and GEL 733 thousand, respectively.

(in thousands of Georgian Lari)

10. Property and equipment

Property and equipment comprise:

	Buildings and other real estate	Computers and communi-cation equipment	Vehicles	Furniture and fixture	Other	Construc-tion in progress	Leasehold improve-ments	Total
At cost / revalued amount								
January 1, 2015	**7,872**	**1,274**	**392**	**560**	**524**	**59**	**65**	**10,746**
Additions	-	198	-	77	93	1,296	57	1,721
Disposals	-	-	-	-	(3)	-	-	(3)
Transfers	-	1	-	-	5	(6)	-	-
December 31, 2015	**7,872**	**1,473**	**392**	**637**	**619**	**1,349**	**122**	**12,464**
Additions	327	716	286	208	203	89	168	1,997
Disposals	-	(117)	(121)	(17)	(133)	-	(32)	(420)
Transfers	1,131	113	-	-	46	(1,290)	-	-
Revaluation	(14)	-	-	-	-	-	-	(14)
December 31, 2016	**9,316**	**2,185**	**557**	**828**	**735**	**148**	**258**	**14,027**
Accumulated depreciation								
January 1, 2015	**27**	**706**	**235**	**362**	**289**	**-**	**15**	**1,634**
Charge for the year	110	126	21	60	69	-	19	405
Eliminated on disposal	-	-	-	-	(2)	-	-	(2)
December 31, 2015	**137**	**832**	**256**	**422**	**356**	**-**	**34**	**2,037**
Charge for the year	120	167	40	61	71	-	40	499
Eliminated on disposal	-	(115)	(121)	(17)	(135)	-	(13)	(401)
Eliminated on revaluation	(227)	-	-	-	-	-	-	(227)
December 31, 2016	**30**	**884**	**175**	**466**	**292**	**-**	**61**	**1,908**

(in thousands of Georgian Lari)

Net book value								
As at December 31, 2016	**9,286**	**1,301**	**382**	**362**	**443**	**148**	**197**	**12,119**
As at December 31, 2015	**7,735**	**641**	**136**	**215**	**263**	**1,349**	**88**	**10,427**

As at December 31, 2016 and 2015 the Bank did not have any pledged property and equipment.

As at December 31, 2016 and 2015 included in property and equipment were fully depreciated assets totaling GEL 981 thousand and GEL 1,137 thousand, respectively.

The Bank's buildings are stated at their revalued amounts, being the fair value at the date of revaluation, less any subsequent accumulated depreciation and subsequent accumulated impairment losses.

As at December 31, 2016 the fair value of the buildings was determined based on the market comparable approach that reflects recent transaction prices for similar properties.

Details of the Bank's buildings and information about the fair value hierarchy as at 31 December 2016 and 2015 are as follows:

	Fair value hierarchy	Fair value as at December 31, 2016	Fair value as at December 31, 2015
Buildings in following region:			
- Tbilisi - Kostava street	Level 3	2,660	2,801
- Tbilisi - Shartava street	Level 3	4,315	4,192
- Batumi - Gorgasali street	Level 3	883	852
Total		**7,858**	**7,845**

Had the Bank's buildings (other than land and buildings classified as held for sale) been measured on a historical cost basis, their carrying amount would have been GEL 6,102 thousand and GEL 7,303 thousand as at December 31, 2016 and December 31, 2015, respectively.

(in thousands of Georgian Lari)

11. Intangible assets

	Intangible
At initial cost:	
January 1, 2015	**2,522**
Additions	661
December 31, 2015	**3,183**
Additions	1,498
December 31, 2016	**4,681**
Accumulated amortization:	
January 1, 2015	**1,122**
Charge for the year	147
December 31, 2015	**1,269**
Charge for the year	202
December 31, 2016	**1,471**
Net book value	
As at December 31, 2016	**3,210**
As at December 31, 2015	**1,914**

Intangible assets include software and licenses.

12. Other assets

Other assets comprise:

	December 31, 2016	December 31, 2015
Other financial assets		
Accounts receivable	652	1,002
Other non-financial assets		
Repossessed assets	391	64
Prepaid expenses	198	78
Tax settlements, other than income tax	99	86
Prepayments for property and equipment	-	57
Other	125	76
Total other assets	**1,465**	**1,363**

(in thousands of Georgian Lari)

13. Deposits by banks

Deposits by banks comprise:

	December 31, 2016	December 31, 2015
Deposits by parent	123,431	129,421
Loans from parent	69,078	9,500
Deposits by resident commercial banks	13,237	1,442
Total deposits by banks	**205,746**	**140,363**

As at December 31, 2016 and 2015 deposits by banks included accrued interest in the amount of GEL 711 thousand and GEL 2,494 thousand, respectively.

As at December 31, 2016 and 2015 deposits by Banks totaling GEL 218,361 thousand and GEL 129,421 thousand (94% and 92%) of total deposits by banks, respectively, were due to 1 Bank, which represents a significant concentration.

14. Deposits by customers

Deposits by customers comprise:

	December 31, 2016	December 31, 2015
Repayable on demand	44,825	21,165
Term deposits	35,307	27,005
Total deposits by customers	**80,132**	**48,170**

As at December 31, 2016 and 2015 deposits by customers included accrued interest in the amount of GEL 987 thousand and GEL 837 thousand, respectively.

As at December 31, 2016 and 2015 deposits by customers totaling GEL 36,183 thousand and GEL 28,348 thousand (45% and 59% of total deposits by customers), respectively were due to 10 customers, which represents a significant concentration.

As at December 31, 2016 and 2015 deposits by customers totaling GEL 16,188 thousand and GEL 8,191 thousand, respectively were held as security against guarantees issued by the Bank.

As at December 31, 2016 and 2015 deposits by customers totaling GEL 10,347 thousand and GEL 8,464 thousand, respectively, were pledged as security for loans to customers.

	December 31, 2016	December 31, 2015
Analysis by industries:		
Trade and service	32,883	23,322
Individuals	21,687	13,176
Construction	9,346	2,112
Transportation and communication	4,348	43
State and public organisations	3,117	4,801
Energy	101	-
Other	8,650	4,716
Total deposits by customers	**80,132**	**48,170**

(in thousands of Georgian Lari)

15. Other liabilities

Other liabilities comprise:

	December 31, 2016	December 31, 2015
Other financial liabilities:		
Accounts payable	668	1,047
Other non-financial liabilities:		
Provision for employee benefits	1,440	653
Provision for guarantees	146	137
Taxes payable, other than income tax	119	98
Total other liabilities	**2,373**	**1,935**

The movements in provisions on other operations were as follows:

	Guarantees
January 1, 2015	**6**
Provision recognized during the year	131
December 31, 2015	**137**
Provision recognized during the year	9
December 31, 2016	**146**

16. Subordinated debt

Subordinated debt comprises:

	Currency	Maturity date year	Nominal interest rate %	Weighted average effective rate	December 31, 2016	December 31, 2015
JSC "Halyk Bank Kazakhstan"	USD	2022	6%	6%	26,561	24,047
Total subordinated debt					**26,561**	**24,047**

In the event of bankruptcy or liquidation of the Bank, repayment of this debt is subordinated to the repayments of the Bank's liabilities to all other creditors.

As at December 31, 2016 and 2015 subordinated debt included accrued interest in the amount of GEL 93 and GEL 98 thousand, respectively.

17. Share capital

As at December 31, 2016 and 2015 the Bank's authorized and issued share capital consisted of 48,000 ordinary shares with par value of GEL 1,000 each. As at December 31, 2016 and 2015, the Bank's issued share capital was fully paid.

(in thousands of Georgian Lari)

18. Net interest income

	2016	2015
Interest income comprises:		
Financial assets recorded at amortized cost:		
- impaired financial assets	26,278	19,568
- unimpaired financial assets	2,400	2,220
Total interest income	**28,678**	**21,788**
Financial assets recorded at amortized cost comprises:		
Loans to customers	25,990	19,388
Investments held to maturity	1,818	1,862
Cash and cash equivalents	496	314
Guarantees	288	180
Mandatory cash balance with the NBG	86	44
Total interest income on financial assets recorded at amortized cost	**28,678**	**21,788**
Interest expense comprises:		
Interest on financial liabilities recorded at amortized cost:		
Deposits by banks	(4,714)	(3,505)
Deposits by customers	(2,356)	(1,938)
Subordinated debt	(1,668)	(1,620)
Total interest expense	**(8,738)**	**(7,063)**
Net interest income before impairment on interest bearing financial assets	**19,940**	**14,725**

19. Impairment losses on interest bearing assets

The movements in allowance for impairment losses on interest bearing assets were as follows:

	Loans to Customers
January 1, 2015	**1,500**
Additional provision recognized	1,291
Write-off of assets	(5)
Recoveries of assets previously written off	2
December 31, 2015	**2,788**
Additional provision recognised	2,664
Recoveries of assets previously written off	1
December 31, 2016	**5,453**

(in thousands of Georgian Lari)

20. Net gain on foreign exchange operations

Net gain on foreign exchange operations comprise:

	2016	2015
Dealing, net	1,142	747
Translation differences, net	(164)	(20)
Total net gain on foreign exchange operations through profit or loss	**978**	**727**

21. Fee and commission income and expense

Fee and commission income and expense comprise:

	2016	2015
Fee and commission income:		
Plastic card operations	3,397	837
Cash operations	217	181
Settlements	212	142
Other	76	60
Total fee and commission income	**3,902**	**1,220**
Fee and commission expense:		
Plastic card operations	(2,260)	(415)
Settlements	(149)	(105)
Cash operations	(33)	(13)
Other	(1)	(2)
Total fee and commission expense	**(2,443)**	**(535)**

As at December 31, 2016 and 2015 Fee and Commission income and expense included service fees for Plastic Cards operations. The bank acts as an intermediary between the number of resident companies and the provider of the plastic card services – VISA and MasterCard, for which the Bank receives and pays commission charges.

22. Operating expenses

Operating expenses comprise:

	2016	2015
Staff costs	6,526	4,968
Depreciation and amortization	701	552
Advertising costs	355	218
Operating leases	347	329
Communications	153	112
Professional services	137	121
Taxes, other than income tax	117	98
Utilities	110	86
Office supplies	63	56
Property and equipment maintenance	60	28
Security expenses	45	42
Business trip expenses	30	38
Representative expenses	14	9
Insurance expense	7	55
Other expenses	1,223	1,062
Total operating expenses	**9,888**	**7,774**

(in thousands of Georgian Lari)

23. Income taxes

The Bank measures and records its current income tax payable and its tax bases in its assets and liabilities in accordance with the tax regulations of Georgia, which differ from IFRS.

The Bank is subject to certain permanent tax differences due to the non-tax deductibility of certain expenses and certain income being treated as non-taxable for tax purposes.

Deferred taxes reflect the net tax effects of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for tax purposes. Temporary differences as at December 31, 2016 and 2015 relate mostly to different methods/timing of income and expense recognition as well as to temporary differences generated by tax – book bases' differences for certain assets.

The tax rate used for the reconciliations below is the corporate tax rate of 15% payable by corporate entities in Georgia on taxable profits as defined under tax law of Georgia.

Deferred tax liabilities as at December 31, 2016 and 2015 comprise:

	December 31, 2016	December 31, 2015
Provisions for other operations	221	98
Other financial liabilities	25	29
Other assets	10	15
Loans to customers	(461)	(301)
Property and equipment and intangible assets	(1,515)	(718)
Net deferred tax liability	**(1,720)**	**(877)**

The effective tax rate reconciliation is as follows for the years ended December 31, 2016 and 2015:

	2016	2015
Profit before income tax	**9,911**	**7,006**
Tax at the statutory tax rate (15%)	1,487	1,051
Effect of non-taxable income	-	(78)
Tax effect of permanent differences	(268)	31
Income tax expense	**1,219**	**1,004**
Current year tax expense	412	-
Deferred tax expense recognized in the current year	807	1,004
Income tax expense	**1,219**	**1,004**

Deferred income tax (liabilities)/assets	2016	2015
As at January 1 – deferred tax assets	**(877)**	**127**
Change in deferred tax liability recongised in profit or loss	(807)	(1,004)
Change in deferred income tax liability recongised in other comprehensive income	(36)	-
As at December 31- deferred tax liabilities	**(1,720)**	**(877)**

(in thousands of Georgian Lari)

In May 2016 the Georgian parliament adopted and the president signed into changes to the corporate tax code, with changes applicable on 1 January 2019. The code is applicable for Georgian companies and permanent establishments ("Pes") of resident companies, apart from certain financial institutions.

The previous profit tax regime, under which companies were subject to tax on their annual taxable profits, is now changed to a system where tax will have to be paid only if corporate profits are distributed.

The change has had an immediate impact on deferred tax of the Companies as it abolishes temporary differences between carrying value of certain assets and liabilities for financial reporting purposes and their tax bases. Due to the changes of the tax legislation balance of deferred tax asset attributable to previously recognised temporary differences arising from prior periods was should be fully written off till 1 January 2019

24. Commitments and contingencies

In the normal course of business, the Bank is a party to financial instruments with off-balance sheet risk in order to meet the needs of its customers. These instruments, involving varying degrees of credit risk, are not reflected in the statement of financial position.

The Bank's uses the same credit control and management policies in undertaking off-balance sheet commitments as it does for on-balance operations.

Provision for losses on contingent liabilities totaled GEL 176 thousand and nil as at December 31, 2016 and 2015, respectively.

As at December 31, 2016 and 2015 contingent liabilities comprise:

	December 31, 2016	December 31, 2015
Contingent liabilities and credit commitments		
Guarantees issued and similar commitments	8,094	7,162
Commitments on loans and unused credit lines	16,942	12,066
Total contingent liabilities and credit commitments	**25,036**	**19,228**

Extension of loans to customers within credit line limits is approved by the Bank on a case-by-case basis and depends on the borrowers' financial performance, debt service and other conditions.

Capital commitments – No material capital commitments were outstanding as at December 31, 2016 and 2015.

Operating lease commitments – No material rental commitments were outstanding as at December 31, 2016 and 2015.

Legal proceedings – From time to time and in the normal course of business, claims against the Bank are received from customers and counterparties. Management is of the opinion that no material unaccrued losses will be incurred and accordingly no provision has been made in these financial statements.

Taxation – Commercial legislation of Georgia, including tax legislation, may allow more than one interpretation. In addition, there is a risk of tax authorities making arbitrary judgments of business activities. If a particular treatment, based on management's judgment of the Bank's business activities, was to be challenged by the tax authorities, the Bank may be assessed additional taxes, penalties and interest.

Georgian transfer pricing legislation was amended starting from January 1, 2014 to introduce additional reporting and documentation requirements. The new legislation allows the tax authorities to impose additional tax liabilities in respect of certain transactions, including but not limited to transactions with related parties, if they consider transaction to be priced not at arm's length. The impact of challenge of the Bank's transfer pricing positions by the tax authorities cannot be reliably estimated.

Such uncertainty may relate to the valuation of financial instruments, valuation of provision for impairment losses and the market pricing of deals. Additionally such uncertainty may relate to the valuation of temporary differences on the provision and recovery of the provision for impairment losses on loans to customers and receivables, as an underestimation of the taxable profit. The management of the Bank believes that it has accrued all tax amounts due and therefore no allowance has been made in the financial statements.

Operating environment – Emerging markets such as Georgia are subject to different risks than more developed markets, including economic, political and social, and legal and legislative risks. Laws and regulations affecting businesses in Georgia continue to change rapidly, tax and regulatory frameworks are subject to varying interpretations. The future economic direction of Georgia is heavily influenced by the fiscal and monetary policies adopted by the government, together with developments in the legal, regulatory, and political environment.

Throughout 2016 Georgia's neighbouring countries, which are large trading partners of Georgia, have experienced significant political and economic turmoil which has had a knock-on effect on the Georgian economy. This has resulted in a significant devaluation of the Georgian Lari against the US dollar and other major currencies.

25. Fair value of financial instruments

IFRS defines fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date.

Assets and liabilities for which fair value approximates carrying value

For financial assets and liabilities that have a short term maturity (less than 3 months), it is assumed that the carrying amounts approximate to their fair value. This assumption is also applied to demand deposits and current accounts without a maturity.

Cash and cash equivalents, mandatory reserves with NBG due from banks, deposits by banks and deposits by customers

For cash and cash equivalents, mandatory reserves with NBG due from banks, deposits by banks and deposits by customers fair value has been estimated by reference to the market rates available at the balance sheet date for similar instruments of maturity equal to the remaining fixed period.

Loans to customers

Loans to individual customers are made both at variable and at fixed rates. As there is no active secondary market in Georgia for such loans and advances, there is no reliable market value available for this portfolio. Fixed rate – Certain of the loans secured are at a fixed rate. Fair value has been estimated by reference to the market rates available at the balance sheet date for similar loans of maturity equal to the remaining fixed period.

Investments held to maturity

The estimated fair value of fixed interest rate instruments is based on estimated future cash flows expected to be received discounted at current interest rates of new instruments with similar credit risk and remaining maturity. Discount rates depend on currency, maturity of the instrument and credit risk of the counterparty.

(in thousands of Georgian Lari)

Subordinated debt and borrowed funds

The fair values of subordinated debt and borrowed funds is determined in accordance with generally accepted pricing models based on discounted cash flow analysis using prices from observable current market transactions for similar instruments.

Other financial assets and liabilities

Other financial assets and liabilities are mainly represented by short-term receivables and payables, therefore the carrying amount is assumed to be a reasonable estimate of their fair value.

Fair value of financial assets and financial liabilities that are not measured at fair value on a recurring basis (but fair value disclosures are required).

The fair value of financial assets and liabilities compared with the corresponding carrying amount in the statement of financial position of the Bank is presented below:

		December 31, 2016		December 31, 2015	
	Fair value hierarchy	Carrying amount	Fair value	Carrying amount	Fair value
Due from Banks	Level 3	871	871	239	239
Loans to customers	Level 3	273,501	274,966	201,610	203,168
Investments held to maturity	Level 3	16,757	18,091	19,283	18,356
Other financial assets	Level 3	652	652	1,002	1,002
Deposits by Banks	Level 3	205,746	232,045	140,363	140,037
Deposits by customers	Level 3	80,132	75,974	48,170	48,170
Other financial liabilities	Level 3	668	668	1,047	1,047
Subordinated debt	Level 3	26,561	26,561	24,047	24,366

26. Capital risk management

The Bank manages its capital to ensure that the Bank will be able to continue as a going concern while maximizing the return to stakeholders through the optimization of its debt and equity balances.

The adequacy of the Bank's capital is monitored using, among other measures, the ratios established by the NBG in supervising the Bank.

The ratios set by the NBG are monitored monthly with reports outlining their calculation reviewed and signed by the Bank's General Director and the Financial Manager and subsequently submitted to the NBG. Other objectives of capital management are evaluated on an ongoing basis.
Under the current capital requirements set by the NBG banks have to: (a) hold the minimum level of share capital of GEL 12,000,000 (b) maintain a ratio of regulatory capital to risk weighted assets ("regulatory capital ratio") at or above a prescribed minimum of 12% and (c) maintain a ratio of tier-1 capital to the risk-weighted assets (the 'Tier-1 capital ratio') at or above the prescribed minimum of 8%.

From June 2014, in addition to the above ratios, banks are also required to calculate capital adequacy in accordance with the regulation on capital adequacy requirements for commercial banks dated October 28, 2013 according to which banks have to (a) maintain a ratio of common equity tier 1 capital to risk weighted assets at or above 7%, (b) maintain a ratio of tier 1 capital to risk weighted assets at or above 8.5%, (c) maintain a ratio of regulatory capital to risk weighted assets at or above 10.5%.

The capital structure of the Bank consists of equity, comprising issued capital and accumulated deficit as disclosed in statement of changes in equity.

(in thousands of Georgian Lari)

The following table analyzes the Bank's regulatory capital resources for capital adequacy purposes based on reports prepared in accordance with the NBG requirements. Ratios are calculated based on Basel III:

	Year ended December 31, 2016	Year ended December 31, 2015
Share capital	48,000	48,000
Retained earnings plus profit for the period	2,277	(1,710)
Less: intangible assets	(2,838)	(1,914)
Tier 1 capital	47,439	44,376
Profit for the period	-	-
General provisions (maximum 1.25% credit and market risk weighted assets)	4,829	3,717
Subordinated debt (up to 100% / 50% of tier 1 capital)	26,468	23,949
Tier 2 capital	31,297	27,666
Total regulatory capital	**78,736**	**72,042**
Risk weighted assets	**547,248**	**374,998**
Tier 1 capital adequacy ratio	8.67%	11.83%
Total regulatory capital adequacy ratio	14.39%	19.21%

As at December 31, 2016 and 2015, the Bank included in the computation of total regulatory capital for capital adequacy purposes the subordinated deposit received, limited to 100% of Tier 1 capital. In the event of bankruptcy or liquidation of the Bank, repayment of this debt is subordinated to the repayments of the Bank's liabilities to all other creditors.

27. Risk management policies

Management of risk is fundamental to the Bank's business and is an essential element of the Bank's operations. The main risks inherent to the Bank's operations are those related to:

- Credit risk
- Liquidity risk
- Market risk

The Bank recognizes that it is essential to have efficient and effective risk management processes in place. To enable this, the Bank has established a risk management framework with the main purpose to protect the Bank from risk and allow it to achieve its performance objectives. Through the risk management framework, the Bank manages the following risks:

Credit risk. The Bank is exposed to credit risk which is the risk that one party to a financial instrument will fail to discharge an obligation and cause the other party to incur a financial loss.

Risk management and monitoring is performed within set limits of authority. These processes are performed by the Bank's Management Board. The Risk Management division plays an important role in managing and controlling the credit risk. This division is responsible for the credit risks identification and evaluation, implementation of the control and monitoring measures. The Risk Management division directly participates in the credit decision-making processes and consideration of internal rules, regulations and loan programs. Along with that, the division provides independent recommendations concerning credit exposure minimization measures, controls and monitors credit risks, provides relevant reporting to the management and ensures compliance of the credit process with external laws/regulations as well as internal requirements and procedures. The Bank structures the level of credit risk it undertakes by placing limits on the amount of risk accepted in relation to one borrower/counterparty, or a group of borrowers, and to industry segments. Limits on the level of credit risk concentration by industry sector are approved and controlled by the Assets and Liabilities Management Committee (ALMC). Limits on credit risk exposure with respect to credit programmes (Small and medium enterprises (SME) and retail) are approved by the Management Board. The exposure to any one borrower, covers on and off-balance sheet exposures which are reviewed by the Credit Committees and ALMC. Actual exposures against limits are monitored daily.

Where appropriate, and in the case of guarantees issued, the Bank obtains collateral and corporate and personal guarantee.

Commitments to extend credit represent guarantees or letter of credit. The credit risk on off-balance sheet financial instruments is defined as the probability of losses due to the inability of counterparty to comply with the contractual terms and conditions. With respect to credit risk on commitments to extend credit, the Bank is potentially exposed to a loss in an amount equal to the total unused commitments. However, the likely amount of the loss is less than the total unused commitments since most commitments to extend credit are contingent upon customers maintaining specific credit standards. The Bank monitors the term to maturity of off balance sheet contingencies because longer term commitments generally have a greater degree of credit risk than short-term commitments.

Credit risk assessment. To assess credit risk of exposures to the borrowers the Bank has developed methodology in accordance with IFRS.

The Bank divides loan portfolio into individually significant and non-significant borrowers. Individually significant are borrowers which exposure exceeds 500,000 US Dollar. Individually significant borrowers are assessed for the probability of default using the Bank's specific methodology. In case of absence of impairment signs, an individually assessed loan is provided for using the rate that is based on the collective assessment applied to the same borrower category.

Individual assessment methodology. Factors that the Bank considers in determining whether it has objective evidence that an impairment loss has been incurred include information about the borrowers' liquidity, solvency and business and financial risk exposures, levels of and trends in delinquencies for similar financial assets and the fair value of collaterals (real estate and deposits). These and other factors may, either individually or taken together, provide sufficient objective evidence that an impairment loss has been incurred in a financial asset or group of financial assets.

The Bank assesses liquidation value of the collaterals and future cash flows for provision estimation purposes. Liquidation value is discounted for the selling period using the original effective interest rate.

Risk of defaulted exposure is reduced by discounted collateral liquidation value.

Methodology for collective assessment of portfolio. Collective assessment of the portfolio was implemented using migration matrixes. Portfolio was divided by segments Corporate, SME and Collateralised Retail and Non-collateralised Retail. Observation period for each segment was taken as one year from November 2015. During the observation period by the state of end of months and with account of exposure of each loan, the one month migration matrixes were generated. In order to exclude portfolio growth effect, the loans disbursed from June 2015 were excluded from the statistics.

Based on migration matrix probability of default was calculated for each segment. Default was determined as 90 days overdue for each segment. Defaulted exposure is reduced by the loan recovery amount which was determined based on the discounted liquidation value of property pledged.

Georgian Lari depreciation effect on loan loss provisioning. To recognise the loss on the credit portfolio that was caused by the national currency devaluation, the USD loans from Retail and SME segments were further analysed. In 2015 the Bank has additionally adjusted prior period stress test results by growth rate of both total gross loan portfolio (66%) and USD/GEL exchange rate (29%). Based on these anlaysis the Bank applied adjusting factors in the collective assessment to reflect stress test results in the loan loss calculations by the amount of GEL 344 thousand. In 2016 the Bank has adopted new methodology for considering macroeconomic effects, as well as currency depreciation effect in loan provision rate. Based on the analysis of the prior period probabilities of default together with the actual rates of impaired loans in the past periods the Bank applied adjusting factors in the collective assessment to reflect stress test results in the loan loss calculations by the amount of GEL 2,329 thousand.

(in thousands of Georgian Lari)

Maximum exposure of credit risk. The Bank's maximum exposure to credit risk varies significantly and is dependent on both individual risks and general market economy risks.

The following table presents the maximum exposure to credit risk of balance sheet and off balance sheet financial assets. For financial assets in the balance sheet, the maximum exposure is equal to the carrying amount of those assets prior to any offset or collateral. The Bank's maximum exposure to credit risk under contingent liabilities and commitments to extend credit, in the event of non-performance by the other party where all counterclaims, collateral or security prove valueless, is represented by the contractual amounts of those instruments.

December 31, 2016	Maximum Exposure	Net exposure
Cash and cash equivalents	24,120	24,120
Mandatory cash balance with the NBG	37,751	37,751
Due from banks	871	871
Loans to customers	278,954	273,501
Investments available-for-sale	54	54
Investments held to maturity	16,757	16,757
Other financial assets	652	652

December 31, 2015	Maximum Exposure	Net exposure
Cash and cash equivalents	10,096	10,096
Mandatory cash balance with the NBG	16,560	16,560
Due from banks	239	239
Loans to customers	204,398	201,610
Investments available-for-sale	54	54
Investments held to maturity	19,283	19,283
Other financial assets	1,002	1,002

Off-balance sheet risk. The Bank applies fundamentally the same risk management policies for off-balance sheet risks as it does for its on-balance sheet risks. In the case of commitments to lend, customers and counterparties will be subject to the same credit management policies as for loans and advances. Collateral may be sought depending on the strength of the counterparty and the nature of the transaction.

Geographical concentration. The Assets and Liabilities Management Committee ("ALMC") exercises control over the risk in the legislation and regulatory arena and assesses its influence on the Bank's activity. The Bank's financial assets and financial liabilities as at December 31, 2016 and 2015 were concentrated in Georgia.

(in thousands of Georgian Lari)

The geographical concentration of assets and liabilities is set out below:

	Georgia	Other non-OECD countries	OECD countries	December 31, 2016 Total
NON-DERIVATIVE FINANCIAL ASSETS				
Cash and cash equivalents	19,928	10,480	221	30,629
Mandatory cash balance with the NBG	37,751	-	-	37,751
Due from banks	-	-	871	871
Loans to customers	272,226	1,275	-	273,501
Investments available-for-sale	54	-	-	54
Investments held to maturity	16,757	-	-	16,757
Other financial assets	652	-	-	652
TOTAL NON-DERIVATIVE FINANCIAL ASSETS	**347,368**	**11,755**	**1,092**	**360,215**
NON-DERIVATIVE FINANCIAL LIABILITIES				
Deposits by banks	64,464	12,391	3,277	80,132
Deposits by customers	13,237	192,509	-	205,746
Other financial liabilities	668	-	-	668
Subordinated debt	-	26,561	-	26,561
TOTAL NON-DERIVATIVE FINANCIAL LIABILITIES	**78,369**	**231,461**	**3,277**	**313,107**
NET POSITION ON FINANCIAL INSTRUMENTS	**268,999**	**(219,706)**	**(2,185)**	**47,108**

	Georgia	Other non-OECD countries	OECD countries	December 31, 2015 Total
NON-DERIVATIVE FINANCIAL ASSETS				
Cash and cash equivalents	11,751	117	2,590	14,458
Mandatory cash balance with the NBG	16,560	-	-	16,560
Due from banks	-	-	239	239
Loans to customers	201,170	440	-	201,610
Investments available-for-sale	54	-	-	54
Investments held to maturity	19,283	-	-	19,283
Other financial assets	1,002	-	-	1,002
TOTAL NON-DERIVATIVE FINANCIAL ASSETS	**249,820**	**557**	**2,829**	**253,206**
NON-DERIVATIVE FINANCIAL LIABILITIES				
Deposits by banks	10,942	129,421	-	140,363
Deposits by customers	46,160	2,010	-	48,170
Other financial liabilities	1,047	-	-	1,047
Subordinated debt	-	24,067	-	24,067
TOTAL NON-DERIVATIVE FINANCIAL LIABILITIES	**58,149**	**155,498**	**-**	**213,647**
NET POSITION ON FINANCIAL INSTRUMENTS	**191,671**	**(154,941)**	**2,829**	**39,559**

(in thousands of Georgian Lari)

Collateral

The amount and type of collateral required depends on an assessment of the credit risk of the counterparty. Guidelines are implemented regarding the acceptability of types of collateral and valuation parameters.

The main types of collateral obtained are as follows:

- For commercial lending, charges over real estate properties, guarantees, vehicles and equipment;
- For retail lending, mortgages over residential properties, guarantees, vehicles and equipment.

Management monitors the market value of collateral, requests additional collateral in accordance with the underlying agreement, and monitors the market value of collateral obtained during its review of the adequacy of the allowance for impairment losses. As at December 31, 2016 and 2015 market values of the collaterals pledged were GEL 630,407 thousand and GEL 305,874 thousand, respectively.

Credit quality by class of financial assets

The following table details an analysis of individually assessed loans to customers:

Loans to customers	Neither past due nor individually impaired	Past due but not individually impaired	Individually impaired	(Impairment allowance)	Total
December 31, 2016	19,019	22,293	8,000	(2,755)	46,557
December 31, 2015	27,856	10,429	3,926	(1,438)	40,773

Financial assets are graded according to the current credit rating they have been issued by an internationally regarded agency such as Fitch. The highest possible rating is AAA. Investment grade financial assets have ratings from AAA to BBB. Financial assets which have ratings lower than BBB are classed as speculative grade.

The following table details the credit ratings of financial assets held by the Bank as at December 31, 2016 and 2015:

December 31, 2016	AAA	AA	A	BBB	<BBB	Not rated	Total
Cash and cash equivalents	-	-	10,480	203	10,233	9,713	**30,629**
Mandatory cash balance with the NBG	-	-	-	-	37,751	-	**37,751**
Due from banks	-	871	-	-	-	-	**871**
Loans to customers	-	-	-	-	-	273,501	**273,501**
Investments available-for-sale	-	-	-	-	-	54	**54**
Investments held to maturity	-	-	-	-	16,757	-	**16,757**
Other financial assets	-	-	-	-	-	652	**652**
December 31, 2015							
Mandatory cash balance with the NBG	-	-	-	-	16,560	-	**16,560**
Due from banks	-	239	-	-	-	-	**239**
Loans to customers	-	-	-	-	-	201,610	**201,610**
Investments available-for-sale	-	-	-	-	-	54	**54**
Investments held to maturity	-	-	-	-	19,283	-	**19,283**
Other financial assets	-	-	-	-	-	1,002	**1,002**

Financial assets other than loans to customers are graded according to the current credit rating they have been issued by an internationally regarded agency such as Fitch, Standard & Poor's and Moody's.

The banking industry is generally exposed to credit risk through its loans to customers and inter-bank deposits. With regard to the loans to customers this risk exposure is concentrated within Georgia. The exposure is monitored on a regular basis to ensure that the credit limits and credit worthiness guidelines established by the Bank's risk management policy are not breached.

The credit rating of Georgia according to the international rating agencies corresponded to investment level BB-.

The Bank enters into numerous transactions where the counterparties are not rated by international rating agencies. The Bank has developed internal models, which allow it to determine the rating of counterparties. A methodology to determine credit ratings of borrowers has been developed in the Group to assess borrowers based on transparency of financial information, availability of audited financial statements, quality of management, competitive ability, share on market, related parties etc.

Renegotiated loans and advances. Loans and advances are generally renegotiated either as part of an ongoing customer relationship or in response to an adverse change in the circumstances of the borrower. In the latter case, renegotiation can result in an extension of the due date of payment or repayment plans under which the Bank offers a concessionary rate of interest to genuinely distressed borrowers. This will result in the asset continuing to be overdue and will be individually impaired where the renegotiated payments of interest and principal will not recover the original carrying amount of the asset. In other cases, renegotiation will lead to a new agreement, which is treated as a new loan.

The table below shows the carrying amount of renegotiated financial assets, by class:

Financial asset class	December 31, 2016	December 31, 2015
Loans to customers	11,731	8,781
Less: allowance	(1,791)	(1,247)

Liquidity risk

Liquidity risk refers to the availability of sufficient funds to meet deposit withdrawals and other financial commitments associated with financial instruments as they actually fall due.

The Assets and Liabilities Management Committee ("ALMC") controls these types of risks by means of maturity analysis, determining the Bank's strategy for the next financial period. Current liquidity is managed by the Treasury Department, which deals in the money markets for current liquidity support and cash flow optimization.

In order to manage liquidity risk, the Bank performs daily monitoring of future expected cash flows on clients' and banking operations, which is a part of assets/liabilities management process. The Management Board sets limits on the minimum proportion of maturing funds available to meet deposit withdrawals and on the minimum level on interbank and other borrowing facilities that should be in place to cover withdrawals at unexpected levels of demand.

The Bank sets limits for the ratio of cumulative GAP (difference between assets and liability) to total assets in order to control liquidity risk. In case of violation of the limits ALMC makes decision on corrective measures.

Further is analysis of liquidity and interest rate risks:

(a) term to maturity of financial liabilities, calculated for non-discounted cash flows on financial liabilities (main debt and interests) on the earliest date, when the Bank will be liable to redeem the liability, and
(b) estimated term till maturity of financial assets, calculated for non-discounted cash flows on financial assets (including interests), which will be received on these assets based on contractual

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terms of maturity, except the cases when the Bank expects that cash flows will be received in the different time.

An analysis of the liquidity and interest rate risks is presented in the following table. The presentation below is based upon the information provided internally to key management personnel of the Bank.

	Up to 1 month	1 month to 3 months	3 months to 1 year	1 year to 5 years	Over 5 years	Maturity undefined	December 31, 2016 Total
FINANCIAL ASSETS:							
Cash and cash equivalents	11,188	-	-	-	-	-	11,188
Mandatory cash balance with the NBG	37,751	-	-	-	-	-	37,751
Investments held to maturity	5,309	1,033	87	5,264	5,064	-	16,757
Loans to customers	15,754	15,088	63,202	105,014	74,443	-	273,501
Total interest bearing financial assets	**70,002**	**16,121**	**63,289**	**110,278**	**79,507**	**-**	**339,197**
Cash and cash equivalents	19,441	-	-	-	-	-	19,441
Due from banks	-	-	-	871	-	-	871
Investments available-for-sale	-	-	-	-	-	54	54
Other financial assets	652	-	-	-	-	-	652
Total non-interest bearing financial assets	**20,093**	**-**	**-**	**871**	**-**	**54**	**21,018**
TOTAL FINANCIAL ASSETS	**90,095**	**16,121**	**63,289**	**111,149**	**79,507**	**54**	**360,215**
FINANCIAL LIABILITIES							
Deposits by banks	74,148	60,901	16,182	54,515	-	-	205,746
Deposits by customers	7,496	1,668	21,742	4,396	-	-	35,302
Subordinated debt	-	-	-	-	26,561	-	26,561
Total interest bearing financial liabilities	**81,644**	**62,569**	**37,924**	**58,911**	**26,561**	**-**	**267,609**
Deposits by customers	44,830	-	-	-	-	-	44,830
Other financial liabilities	668	-	-	-	-	-	668
Total non-interest bearing financial liabilities	**45,498**	**-**	**-**	**-**	**-**	**-**	**45,498**
TOTAL FINANCIAL LIABILITIES	**127,142**	**62,569**	**37,924**	**58,911**	**26,561**	**-**	**313,107**
Interest sensitivity gap	(11,642)	(46,448)	25,365	51,367	52,946	-	
Cumulative interest sensitivity gap	(11,642)	(58,090)	(32,725)	18,642	71,588	71,588	
Liquidity gap	(37,047)	(46,448)	25,365	52,238	52,955	54	
Cumulative liquidity gap	**(37,047)**	**(83,495)**	**(58,130)**	**(5,892)**	**47,054**	**47,108**	

(in thousands of Georgian Lari)

	Up to 1 month	1 month to 3 months	3 months to 1 year	1 year to 5 years	Over 5 years	Maturity undefined	December 31, 2015 Total
FINANCIAL ASSETS:							
Cash and cash equivalents	1,672	-	-	-	-	-	1,672
Mandatory cash balance with the NBG	16,560	-	-	-	-	-	16,560
Investments held to maturity	370	731	2,094	11,015	5,073	-	19,283
Loans to customers	7,563	14,819	42,686	80,699	55,843	-	201,610
Total interest bearing financial assets	26,165	15,550	44,780	91,714	60,916	-	239,125
Cash and cash equivalents	12,786	-	-	-	-	-	12,786
Due from banks	-	-	-	239	-	-	239
Investments available-for-sale	-	-	-	-	-	54	54
Other financial assets	1,002	-	-	-	-	-	1,002
Total non-interest bearing financial assets	13,788	-	-	239	-	54	14,081
TOTAL FINANCIAL ASSETS	**39,953**	**15,550**	**44,780**	**91,953**	**60,916**	**54**	**253,206**
FINANCIAL LIABILITIES							
Deposits by banks	53,815	1,442	47,185	37,921	-	-	140,363
Deposits by customers	2,993	2,890	17,351	3,773	-	-	27,007
Subordinated debt	-	-	-	-	24,047	-	24,047
Total interest bearing financial liabilities	56,808	4,332	64,536	41,694	24,047	-	191,417
Deposits by customers	21,163	-	-	-	-	-	21,163
Other financial liabilities	1,047	-	-	-	-	-	1,047
Total non-interest bearing financial liabilities	22,210	-	-	-	-	-	22,210
TOTAL FINANCIAL LIABILITIES	**79,018**	**4,332**	**64,536**	**41,694**	**24,047**	**-**	**213,627**
Interest sensitivity gap	(30,643)	11,218	(19,756)	50,020	36,869	-	
Cumulative interest sensitivity gap	**(30,643)**	**(19,425)**	**(39,181)**	**10,839**	**47,708**	**47,708**	
Liquidity gap	(39,065)	11,218	(19,756)	50,259	36,870	54	
Cumulative liquidity gap	**(39,065)**	**(27,847)**	**(47,603)**	**2,656**	**39,526**	**39,580**	

The following tables detail the Bank's remaining contractual maturity for its financial liabilities with agreed repayment periods. The tables have been drawn up based on the undiscounted cash flows of financial liabilities based on the earliest date on which the Bank can be required to pay. The tables include both interest and principal cash flows. To the extent that interest flows are floating rate, the undiscounted amount is derived from interest rate curves at the end of the reporting period. The contractual maturity is based on the earliest date on which the Bank may be required to pay.

Demand deposits by customers are included in the up to 1 month liquidity category, as contractually any amount at reporting date can be withdrawn upon the customer's demand. The main deposit holders of the Bank are borrowers which under the loan agreements are required to have an operational accounts and maintain certain turnover ratios through the Bank.

(in thousands of Georgian Lari)

	Weighted average effective interest rate	Up to 1 month	1 month to 3 months	3 months to 1 year	1 year to 5 years	Over 5 years	December 31, 2016 Total
Fixed interest rate instruments							
Deposits by banks	3.58%	74,180	60,964	16,397	61,306	33,039	245,886
Deposits by customers	7.56%	7,496	1,739	22,666	5,113	-	37,014
Subordinated debt	6.00%	51	160	1,261	3,757	26,561	31,790
Total fixed interest bearing financial liabilities		**81,727**	**62,863**	**40,324**	**70,176**	**59,600**	**314,690**
Non-interest bearing instruments							
Deposits by customers		44,830	-	-	-	-	44,830
Other financial liabilities		668	-	-	-	-	668
Total non-interest bearing financial liabilities		**45,498**	**-**	**-**	**-**	**-**	**45,498**
Total financial liabilities		**127,225**	**62,863**	**40,324**	**70,176**	**59,600**	**360,188**

	Weighted average effective interest rate	Up to 1 month	1 month to 3 months	3 months to 1 year	1 year to 5 years	Over 5 years	December 31, 2015 Total
Fixed interest rate instruments							
Deposits by banks	3.58%	53,873	1,518	48,410	44,208	-	148,009
Deposits by customers	7.56%	3,557	3,107	17,556	4,210	432	28,862
Subordinated debt	7.00%	24	72	72	1,437	24,047	25,652
Total fixed interest bearing financial liabilities		**57,454**	**4,697**	**66,038**	**49,855**	**24,479**	**202,523**
Non-interest bearing instruments							
Deposits by banks		21,163	-	-	-	-	21,163
Other financial liabilities		1,047	-	-	-	-	1,047
Total non-interest bearing financial liabilities		**22,210**	**-**	**-**	**-**	**-**	**22,210**
Total financial liabilities		**79,664**	**4,697**	**66,038**	**49,855**	**24,479**	**224,733**

In the table above, the terms to maturity correspond to the contractual terms. However, individuals are entitled to terminate the deposit agreement ahead of schedule according to effective laws.

The amounts included above for variable interest rate instruments for both non-derivative financial assets and liabilities is subject to change if changes in variable interest rates differ to those estimates of interest rates determined at the end of the reporting period.

(in thousands of Georgian Lari)

Market risk. Market risk is that the risk that the Bank's earnings or capital or its ability to meet business objectives will be adversely affected by changes in the level or volatility of market rates or prices. Market risk covers interest rate risk, currency risk, credit spreads, etc. There have been no changes as to the way the Bank measures risk or to the risk it is exposed or the manner in which these risks are managed and measured.

The ALMC also manages interest rate and market risks by matching the Bank's interest rate position, which provides the Bank with a positive interest rate margin. The Bank's management conducts monitoring of the Bank's current financial performance, estimates the Bank's sensitivity to changes in interest rates and its influence on the Bank's profitability.

Interest rate sensitivity. The Bank manages fair value interest rate risk through periodic estimation of potential losses that could arise from adverse changes in market conditions. The Bank's management conducts monitoring of the Bank's current financial performance, estimates the Bank's sensitivity to changes in fair value interest rates and its influence on the Bank's profitability.

Main tool for management on interest rate risk in the bank is establishment and monitoring of limits on interest rate GAP. According to market risk management policy of the Bank limit on interest rate GAP is established taking into consideration that loss caused by changes on interest rates by 2%, should not exceed 10% of net interest income stated in the budget of the year.

The following table presents a sensitivity analysis of interest rate risk, which has been determined based on "reasonably possible changes in the risk variable". The level of these changes is determined by management and is contained within the risk reports provided to key management personnel.

Impact on profit before tax based on asset values as at December 31, 2016 and 2015:

	As at December 31, 2016		As at December 31, 2015	
	Interest rate +2%	Interest rate -2%	Interest rate +2%	Interest rate -2%
Non-derivative financial assets:				
Cash and cash equivalents	224	(224)	33	(33)
Mandatory cash balance with the NBG	755	(755)	331	(331)
Loans to customers	5,470	(5,470)	4,032	(4,032)
Investments held to maturity	335	(335)	386	(386)
Non-derivative financial liabilities:				
Deposits by banks	(4,115)	4,115	(2,807)	2,807
Deposits by customers	(706)	706	(540)	540
Subordinated debt	(531)	531	(481)	481
Net impact on profit before tax	**1,432**	**(1,432)**	**954**	**(954)**

(in thousands of Georgian Lari)

Impact on shareholders' equity:

	As at December 31, 2016		As at December 31, 2015	
	Interest rate +2%	Interest rate +2%	Interest rate +2%	Interest rate -2%
Non-derivative financial assets:				
Cash and cash equivalents	190	(190)	28	(28)
Mandatory cash balance with the NBG	642	(642)	281	(281)
Loans to customers	4,650	(4,650)	3,427	(3,427)
Investments held to maturity	285	(285)	328	(328)
Non-derivative financial liabilities:				
Deposits by banks	(3,498)	3,498	(2,386)	2,386
Deposits by customers	(600)	600	(459)	459
Subordinated debt	(451)	451	(409)	409
Net impact on equity	**1,218**	**(1,218)**	**810**	**(810)**

Currency risk. Currency risk is defined as the risk that the value of a financial instrument will fluctuate due to changes in foreign exchange rates. The Bank is exposed to the effects of fluctuations in the prevailing foreign currency exchange rates on its financial position and cash flows.

The ALMC controls currency risk by management of the open currency position on the estimated basis of Georgian Lari devaluation and other macroeconomic indicators, which gives the Bank an opportunity to minimize losses from significant currency rates fluctuations toward its national currency. The Treasury Department performs daily monitoring of the Bank's open currency position with the aim to match the requirements of the NBG.

The Bank's open positions by the major currencies in which it holds the assets and liabilities are presented below:

	GEL	USD USD 1 = GEL 2.3949	EUR EUR 1 = GEL 2.6169	Other currency	December 31, 2015 Total
FINANCIAL ASSETS					
Cash and cash equivalents	6,364	6,386	1,596	112	14,458
Mandatory cash balance with the NBG	-	16,309	251	-	16,560
Due from banks	-	239	-	-	239
Loans to customers	46,264	153,678	1,668	-	201,610
Investments available-for-sale	54	-	-	-	54
Investments held to maturity	19,283	-	-	-	19,283
Other financial assets	1,002	-	-	-	1,002
TOTAL FINANCIAL ASSETS	**72,967**	**176,612**	**3,515**	**112**	**253,206**
FINANCIAL LIABILITIES					
Deposits by banks	9,500	129,421	1,442	-	140,363
Deposits by customers	22,471	23,609	2,054	36	48,170
Subordinated debt	-	24,047	-	-	24,047
Other financial liabilities	1,047	-	-	-	1,047
TOTAL FINANCIAL LIABILITIES	**33,018**	**177,077**	**3,496**	**36**	**213,627**
OPEN POSITION	**39,949**	**(465)**	**19**	**76**	

(in thousands of Georgian Lari)

	GEL	USD USD 1 = GEL 2.6468	EUR EUR 1 = GEL 2.7940	Other currency	December 31, 2016 Total
FINANCIAL ASSETS					
Cash and cash equivalents	14,011	13,667	2,849	102	30,629
Mandatory cash balance with the NBG	-	36,786	965	-	37,751
Due from banks	-	871	-	-	871
Loans to customers	43,977	228,202	1,322	-	273,501
Investments available-for-sale	54	-	-	-	54
Investments held to maturity	16,757	-	-	-	16,757
Other financial assets	652	-	-	-	652
TOTAL FINANCIAL ASSETS	**75,451**	**279,526**	**5,136**	**102**	**360,215**
FINANCIAL LIABILITIES					
Deposits by banks	-	205,746	-	-	205,746
Deposits by customers	28,734	46,229	5,071	98	80,132
Subordinated debt	-	26,561	-	-	26,561
Other financial liabilities	668	-	-	-	668
TOTAL FINANCIAL LIABILITIES	**29,402**	**278,536**	**5,071**	**98**	**313,107**
OPEN POSITION	**46,049**	**990**	**65**	**4**	

Currency risk sensitivity. The following table details the Bank's sensitivity to a 25% increase and decrease in the USD against the GEL. 25% is the sensitivity rate used when reporting foreign currency risk internally to key management personnel and represents management's assessment of the possible change in foreign currency exchange rates. The sensitivity analysis includes only outstanding foreign currency denominated monetary items and adjusts their translation at the end of the period for a 25% change in foreign currency rates.

Impact on net profit and equity based on asset values as at December 31, 2016 and 2015:

	As at December 31, 2016		As at December 31, 2015	
	GEL/USD 25%	GEL/USD (25%)	GEL/USD 25%	GEL/USD (25%)
Impact on profit or loss	248	(248)	(116)	116
Impact on equity	211	(211)	(99)	99

	As at December 31, 2016		As at December 31, 2015	
	GEL/EUR 25%	GEL/EUR (25%)	GEL/EUR 10%	GEL/EUR (10%)
Impact on profit or loss	16	(16)	5	(5)
Impact on equity	14	(14)	4	(4)

Limitations of sensitivity analysis. The above tables demonstrate the effect of a change in a key assumption while other assumptions remain unchanged. In reality, there is a correlation between the assumptions and other factors. It should also be noted that these sensitivities are non-linear, and larger or smaller impacts should not be interpolated or extrapolated from these results.

The sensitivity analysis do not take into consideration that the Bank's assets and liabilities are actively managed. Additionally, the financial position of the Bank may vary at the time that any actual market movement occurs. For example, the Bank's financial risk management strategy aims to manage the exposure to market fluctuations. As investment markets move past various trigger levels, management actions could include selling investments, changing investment portfolio allocation and taking other protective action. Consequently, the actual impact of a change in the assumptions may not have any impact on the liabilities, whereas assets are held at market value in the statement of financial position. In these circumstances, the different measurement bases for liabilities and assets may lead to volatility in shareholder equity.

(in thousands of Georgian Lari)

Other limitations in the above sensitivity analysis include the use of hypothetical market movements to demonstrate potential risk that only represent the Bank's view of possible near-term market changes that cannot be predicted with any certainty; and the assumption that all interest rates move in an identical fashion.

Price risk. Price risk is the risk that the value of a financial instrument will fluctuate as a result of changes in market prices whether those changes are caused by factors specific to the individual security or its issuer or factors affecting all securities traded in the market. The Bank is exposed to price risks of its products which are subject to general and specific market fluctuations.

The Bank manages price risk through periodic estimation of potential losses that could arise from adverse changes in market conditions and establishing and maintaining appropriate stop-loss limits and margin and collateral requirements. With respect to undrawn loan commitments the Bank is potentially exposed to a loss of an amount equal to the total amount of such commitments. However, the likely amount of a loss is less than that, since most commitments are contingent upon certain conditions set out in the loan agreements.

Operational risk. Operational risk is the risk of loss arising from systems failure, human error, fraud or external events. When controls fail to perform, operational risks can cause damage to reputation, have legal or regulatory implications, or lead to financial loss. The Bank cannot expect to eliminate all operational risks, but it endeavours to manage these risks through a control framework and by monitoring and responding to potential risks. Controls include effective segregation of duties, access, authorization and reconciliation procedures, staff education and assessment processes.

28. Transactions with related parties

Transactions between the Bank and its subsidiaries, which are related parties of the Bank, have been eliminated on and are not disclosed in this note. Details of transactions between the Bank and other related parties are disclosed below:

	December 31, 2016		December 31, 2015	
	Related party balances	Total category as per the financial statements caption	Related party balances	Total category as per the financial statements caption
Cash and cash equivalents	203	30,629	95	14,458
- the parent	203		95	
Loans to customers	783	278,954	1,087	204,398
- key management personnel of the Bank	377		306	
-other related parties	406		782	
Allowance for impairment losses on loans to customers	5	5,453	5	2,788
- key management personnel of the Bank	1		1	
- other related parties	4		4	
Deposits by banks	192,509	205,746	129,421	140,363
- the parent	192,509		129,421	
Deposits by customers	669	80,132	1,400	48,170
- key management personnel of the Bank	380		161	
- other related parties	289		1,239	
Subordinated debt	26,561	26,561	24,047	24,047
- the parent	26,561		24,047	

(in thousands of Georgian Lari)

The remuneration of directors and other members of key management were as follows:

	2016		2015	
	Related party transactions	Total category as per the financial statements caption	Related party transactions	Total category as per the financial statements caption
Key management personnel compensation:				
- short-term employee benefits	851	6,526	750	4,968
Total	**851**	**6,526**	**750**	**4,968**

Included in the statement of profit or loss and other comprehensive income for the year ended December 31, 2016 and 2015 are the following amounts which were recognized in transactions with related parties:

	2016		2015	
	Related party transactions	Total category as per the financial statements caption	Related party transactions	Total category as per the financial statements caption
Interest income	117	28,678	117	21,788
- key management personnel of the Bank	36		36	
-other related parties	81		81	
Interest expense	6,152	8,738	4,711	7,063
- the parent	6,138		4,700	
- key management personnel of the Bank	2		2	
- other related parties	9		9	
Operating expenses	857	9,888	857	7,774
- key management personnel of the Bank	857		857	

29. Subsequent events

Subsequent to the reporting period, Georgian Lari has continued to depreciate against US Dollar. At 2 March 2017, official exchange rate equaled to 2.4828 Georgian Lari per 1 US Dollar.