JSC Cartu Bank and Subsidiaries

Consolidated financial statements

Year ended 31 December 2020
together with independent auditor's report

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Selected explanatory notes to the consolidated financial statements

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Independent auditor's report

To the Shareholders and the Board of Directors of JSC Cartu Bank

Opinion

We have audited the consolidated financial statements of JSC Cartu Bank and its subsidiaries (the Group), which comprise the consolidated statement of financial position as at 31 December 2020, and the consolidated statement of comprehensive income, consolidated statement of changes in equity and consolidated statement of cash flows for the year then ended, and notes to the consolidated financial statements, including a summary of significant accounting policies.

In our opinion, the accompanying consolidated financial statements present fairly, in all material respects, the consolidated financial position of the Group as at 31 December 2020 and its consolidated financial performance and its consolidated 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 consolidated financial statements* section of our report. We are independent of the Group in accordance with the International Ethics Standards Board for Accountants' *Code of Ethics for Professional Accountants (including International Independence Standards)* (*IESBA Code*), and we have fulfilled our other ethical responsibilities in accordance with the IESBA Code. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Other information included in the Group's 2020 Annual report

Other information consists of the information included in the Annual Report other than the consolidated financial statements and our auditor's report thereon. Management is responsible for the other information. The Annual Report is expected to be made available to us after the date of this auditor's report.

Our opinion on the consolidated financial statements does not cover the other information and we will not express any form of assurance conclusion thereon in our report on the audit of the consolidated financial statements.

In connection with our audit of the consolidated financial statements, our responsibility is to read the other information identified above when it becomes available and, in doing so, consider whether the other information is materially inconsistent with the consolidated financial statements or our knowledge obtained in the audit or otherwise appears to be materially misstated.

Responsibilities of management and the Supervisory Board for the consolidated financial statements

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

In preparing the consolidated financial statements, management is responsible for assessing the Group'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 Group or to cease operations, or has no realistic alternative but to do so.

The Supervisory Board is responsible for overseeing the Group's financial reporting process.

Auditor's responsibilities for the audit of the consolidated financial statements

Our objectives are to obtain reasonable assurance about whether the consolidated 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 consolidated 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 consolidated 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 Group's internal control.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management.

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- 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 Group'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 consolidated 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 Group to cease to continue as a going concern.
- Evaluate the overall presentation, structure and content of the consolidated financial statements, including the disclosures, and whether the consolidated financial statements represent the underlying transactions and events in a manner that achieves fair presentation.
- Obtain sufficient appropriate audit evidence regarding the financial information of the entities or business activities within the Group to express an opinion on the consolidated financial statements. We are responsible for the direction, supervision and performance of the group audit. We remain solely responsible for our audit opinion.

We communicate with the Supervisory Board 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.

Ruslan Khoroshvili

For and on behalf of EY LLC

Tbilisi, Georgia

31 May 2021

Consolidated statement of financial position

As at 31 December 2020

(thousands of Georgian lari)

	Notes	*2020*	*2019*
Assets			
Cash and cash equivalents	5	138,401	147,598
Amounts due from credit institutions	6	211,683	168,905
Loans to customers	7	1,031,840	879,329
Investment securities	8	62,338	42,526
Property and equipment	9	11,939	13,020
Right of use assets	10	4,184	5,436
Intangible assets	11	3,561	4,395
Income tax asset		7,333	2,311
Deferred income tax asset	16	83	333
Other assets	12	72,108	73,034
Total assets		**1,543,470**	**1,336,887**
Liabilities			
Amounts due to credit institutions	13	9	13
Amounts due to customers	14	976,190	778,274
Provisions		2,445	3,188
Current income tax liability		–	1,650
Deferred income tax liability	16	6,303	7,787
Lease liabilities	10	4,575	5,680
Other liabilities	12	16,226	10,364
Subordinated debt	15	199,039	206,500
Total liabilities		**1,204,787**	**1,013,456**
Equity			
Share capital	17	114,430	114,430
Additional paid–in capital	17	17,845	12,667
Retained earnings		205,601	195,670
Total equity attributable to shareholders of the Bank		**337,877**	**322,767**
Non–controlling interests		806	664
Total equity		**338,683**	**323,431**
Total equity and liabilities		**1,543,470**	**1,336,887**

Signed and authorized for release on behalf of the Board of Directors of the Bank on 31 May 2021:

Nato Khaindrava General Director

Givi Lebanidze Chief Financial Officer

The accompanying selected explanatory notes on pages 8 to 49 are an integral part of these consolidated financial statements.

Consolidated statement of comprehensive income

For the year ended 31 December 2020

(thousands of Georgian lari)

	Notes	*2020*	*2019*
Interest revenue calculated using effective interest rate			
Loans to customers		86,704	86,504
Investment securities		5,676	2,543
Amounts due from credit institutions		1,408	5,518
Other interest income		61	53
		93,849	**94,618**
Interest expense			
Amounts due to credit institutions		(61)	(372)
Amounts due to customers		(21,458)	(18,069)
Subordinated debt		(12,287)	(11,956)
Lease liabilities		(486)	(602)
		(34,292)	**(30,999)**
Net interest income		**59,557**	**63,619**
Credit loss expense on interest bearing assets	19	(45,770)	(15,275)
Net interest income after credit loss expense		**13,787**	**48,344**
Fee and commission income	20	5,864	6,930
Fee and commission expense	20	(4,738)	(6,652)
Net gains/(losses) from foreign currencies			
- *dealing*		5,698	5,584
- *translation differences*		13,384	2,828
Other income, net	21	5,681	4,775
Non–interest income		**25,889**	**13,465**
Personnel expenses	22	(13,852)	(14,432)
Other operating expenses	22	(10,458)	(13,432)
Depreciation and amortisation	9, 10, 11	(4,305)	(4,081)
Other impairment and provisions	19	(2,463)	(3,711)
Non–interest expenses		**(31,078)**	**(35,656)**
Profit before income tax		**8,598**	**26,153**
Income tax benefit/expense	16	1,234	(3,839)
Net profit for the period		**9,832**	**22,314**
Other comprehensive income		**242**	–
Total comprehensive income for the year		**10,074**	**22,314**
Attributable to:			
– shareholders of the Bank		9,690	21,724
– non–controlling interests		142	590
		9,832	**22,314**

The accompanying selected explanatory notes on pages 8 to 49 are an integral part of these consolidated financial statements.

Consolidated statement of changes in equity

For the year ended 31 December 2020

(thousands of Georgian lari)

	Attributable to shareholders of the Bank					
	Share capital	***Additional paid–in capital***	***Retained earnings***	***Total***	***Non–controlling interests***	***Total equity***
1 January 2019	**114,430**	**12,667**	**218,946**	**346,043**	**74**	**346,117**
Profit for the year	–	–	21,724	**21,724**	590	**22,314**
Total comprehensive income for the year	**–**	**–**	**21,724**	**21,724**	**590**	**22,314**
Dividends declared and disbursed (Note 17)	–	–	(45,000)	**(45,000)**	–	**(45,000)**
31 December 2019	**114,430**	**12,667**	**195,670**	**322,767**	**664**	**323,431**
Profit for the year	–	–	9,690	**9,690**	142	**9,832**
Other comprehensive income for the year (Note 8)	–	–	242	**242**	–	**242**
Total comprehensive income for the year	–	–	**9,932**	**9,932**	**142**	**10,074**
Additional paid–in capital (Note 15)	–	5,178	–	**5,178**	–	**5,178**
31 December 2020	**114,430**	**17,845**	**205,602**	**337,877**	**806**	**338,683**

The accompanying selected explanatory notes on pages 8 to 49 are an integral part of these consolidated financial statements.

Consolidated statement of Cash Flows

For the year ended 31 December 2020

(thousands of Georgian lari)

	Notes	2020	2019
Cash flows from operating activities:			
Profit before income tax		**8,598**	**26,153**
Adjustments for non–cash Items:			
Provision for impairment losses on interest bearing assets		45,770	15,275
Provision for impairment losses on non-interest bearing assets		3,510	823
Provision on other operations		(1,047)	2,888
Modification loss		2,432	891
Net gain on disposal of property and equipment		(28)	(62)
Net gain on disposal of repossessed assets		(2,848)	(542)
Depreciation and amortization expense		4,305	4,081
Change in interest accruals, net		(22,669)	(2,067)
Gain on foreign exchange operations from translation differences		(13,384)	(2,828)
Cash inflow from operating activities before changes in operating assets and liabilities		**24,639**	**44,612**
Changes in operating assets and liabilities			
Amounts due from credit institutions		(16,604)	(4,576)
Loans to customers		(75,600)	(26,229)
Other assets		(7,757)	(145)
Amounts due to credit institutions		(6)	(15,518)
Amounts due to customers		87,408	102,705
Other liabilities		5,206	38
Cash inflow/(outflow) from operating activities before taxation		**17,286**	**100,887**
Income tax paid		(6,672)	(1,419)
Net cash inflow/(outflow) from operating activities		**10,614**	**99,468**
Cash flows from investing activities:			
Purchase of property and equipment		(687)	(2,450)
Purchase of intangible assets		(451)	(323)
Proceeds from sale of property and equipment		8	560
Proceeds from sale of repossessed assets		8,488	3,056
Proceeds from investments securities at amortised cost		29,575	33,460
Acquisition of investments securities at amortised cost		(36,667)	(55,817)
Acquisition of investments securities at FVOCI		(9,000)	–
Net cash (outflow)/inflow from investing activities		**(8,734)**	**(21,514)**
Cash flows from financing activities:			
Payment of dividends		–	(45,000)
Repayment of subordinated debt		(32,233)	–
Payment of lease liabilities		(1,263)	(1,173)
Net cash outflow from financing activities		**(33,496)**	**(46,173)**
Effect of changes in foreign exchange rate fluctuations on cash and cash equivalents		22,419	(8,718)
Net increase/(decrease) in cash and cash equivalents		**(9,197)**	**23,063**
Cash and cash equivalents, beginning	5	147,598	124,535
Cash and cash equivalents, ending	5	**138,401**	**147,598**

Material non-cash transactions

- As at 31 December 2020 change in other assets includes repossession of collaterals in amount of GEL 8,078 thousands
- As at 31 December 2020 change in subordinated debt balance includes GEL 5,178 thousands recorded as increase of additional paid in capital

The accompanying selected explanatory notes on pages 8 to 49 are an integral part of these consolidated financial statements.

(thousands of Georgian lari)

1. Principal activities

Joint Stock Company Cartu Bank (the "Bank") was incorporated in Georgia in 1996. The Bank is regulated by the National Bank of Georgia (the "NBG") and conducts its business under general license number 229. The Bank's primary business consists of commercial activities, originating loans and guarantees, investing in securities, trading foreign currencies and taking deposits.

The registered office of the Bank is located on 39a Chavchavadze Avenue, Tbilisi, Georgia.

As at 31 December 2020 and 2019, the Bank had five service centers operating in Tbilisi, division in Shekvetili and service centres in Gori, Telavi, Kutaisi and Batumi.

The Bank is the parent company of the group (the "Group"), which consists of the following entities consolidated in these financial statements:

		Ownership interest (%)		
Name	***Country of operation***	***2020***	***2019***	***Type of operation***
Cartu Broker LLC	Georgia	100.00%	100.00%	Brokerage
Insurance Company Cartu JSC	Georgia	91.39%	91.39%	Insurance
Investment Company Cartu Invest LLC	Georgia	100.00%	100.00%	Dormant
Geoplast LLC	Georgia	100.00%	100.00%	Dormant

As at 31 December 2019 JSC the Cartu Group owned 100% of the Bank's shares.

As at 31 December 2020 JSC the Cartu Group had transferred all its stake to the International Charity Foundation Cartu (the "Parent" or the "Shareholder"). The Group is ultimately owned by Uta Ivanishvili, the son of Bidzina Ivanishvili.

These consolidated financial statements have not yet been approved by the Parent on the general meeting of shareholders of the Bank. The shareholders have the power and authority to amend the financial statements after the issuance.

2. Basis of preparation

General

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

The consolidated financial statements have been prepared under the historical cost convention except as disclosed in the accounting policies below.

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

Effect of COVID-19 pandemic

Due to the rapid spread of COVID-19 pandemic in 2020 many governments, including the Georgian Government, have introduced various measures to combat the outbreak, including travel restrictions, quarantines, closure of businesses and other venues and lockdown of certain areas. These measures have affected the global supply chain, demand for goods and services, as well as scale of business activity. It is expected that pandemic itself as well as the related public health and social measures may influence the business of the entities in a wide range of industries.

Support measures were introduced by the Government and the National Bank of Georgia to counter the economic downturn caused by the COVID-19 pandemic. These measures include, among others, subsidized lending to affected industries and individuals, payment holidays and easing of certain regulatory restrictions to help the financial sector maintain its capabilities to provide resources and to help customers avoid liquidity shortages as a result of the COVID-19 containment measures.

As at 31 December 2020, impact of Covid-19 pandemic on the consolidated financial statements of the Group was mainly reflected in increased ECL, increased number of renegotiated loans and modification losses (Note 7).
The Group continues to assess the effect of the pandemic and changing economic conditions on its activities, financial position and financial results.

(thousands of Georgian lari)

3. Summary of accounting policies

Changes in accounting policies

The Group has not early adopted any standards, interpretations or amendments that have been issued but are not yet effective.

Several other amendments effective since 1 January 2020 were applied but do not have an impact on the consolidated financial statements of the Group.

Basis of consolidation

Subsidiaries, which are those entities which are controlled by the Group, are consolidated. Control is achieved when the Group is exposed, or has rights, to variable returns from its involvement with the investee and has the ability to affect those returns through its power over the investee. Specifically, the Group controls an investee if, and only if, the Group has:

- Power over the investee (i.e., existing rights that give it the current ability to direct the relevant activities of the investee);
- Exposure, or rights, to variable returns from its involvement with the investee;
- The ability to use its power over the investee to affect its returns.

Generally, there is a presumption that a majority of voting rights results in control. To support this presumption and when the Group has less than a majority of the voting or similar rights of an investee, the Group considers all relevant facts and circumstances in assessing whether it has power over an investee, including:

- The contractual arrangement(s) with the other vote holders of the investee;
- Rights arising from other contractual arrangements;
- The Group's voting rights and potential voting rights.

Subsidiaries are consolidated from the date on which control is transferred to the Group and are no longer consolidated from the date that control ceases. All intra–group transactions, balances and unrealised gains on transactions between group companies are eliminated in full; unrealised losses are also eliminated unless the transaction provides evidence of an impairment of the asset transferred. Where necessary, accounting policies for subsidiaries have been changed to ensure consistency with the policies adopted by the Group.

A change in the ownership interest of a subsidiary, without a change of control, is accounted for as an equity transaction. Losses are attributed to the non–controlling interests even if that results in a deficit balance.

If the Group loses control over a subsidiary, it derecognises the assets (including goodwill) and liabilities of the subsidiary, the carrying amount of any non–controlling interests, the cumulative translation differences, recorded in equity; recognises the fair value of the consideration received, the fair value of any investment retained and any surplus or deficit in profit or loss and reclassifies the parent's share of components previously recognised in other comprehensive income to profit or loss

Fair value measurement

Fair values of financial instruments measured at amortised cost are disclosed in Note 24.

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. The fair value measurement is based on the presumption that the transaction to sell the asset or transfer the liability takes place either:

- In the principal market for the asset or liability; or
- In the absence of a principal market, in the most advantageous market for the asset or liability.

The principal or the most advantageous market must be accessible by the Bank. The fair value of an asset or a liability is measured using the assumptions that market participants would use when pricing the asset or liability, assuming that market participants act in their economic best interest. Fair value measurement of a non–financial asset takes into account a market participant's ability to generate economic benefits by using the asset in its highest and best use or by selling it to another market participant that would use the asset in its highest and best use.

(thousands of Georgian lari)

3. Summary of accounting policies (continued)

Fair value measurement (continued)

The Group uses valuation techniques that are appropriate in the circumstances and for which sufficient data are available to measure fair value, maximising the use of relevant observable inputs and minimising the use of unobservable inputs. All assets and liabilities for which fair value is measured or disclosed in the financial statements are categorized within the fair value hierarchy, described as follows, based on the lowest level input that is significant to the fair value measurement as a whole:

- Level 1 − quoted (unadjusted) market prices in active markets for identical assets or liabilities;
- Level 2 − valuation techniques for which the lowest level input that is significant to the fair value measurement is directly or indirectly observable;
- Level 3 − valuation techniques for which the lowest level input that is significant to the fair value measurement is unobservable.

For assets and liabilities that are recognised in the financial statements on a recurring basis, the Group determines whether transfers have occurred between levels in the hierarchy by re–assessing categorization (based on the lowest level input that is significant to the fair value measurement as a whole) at the end of each reporting period.

Financial assets and liabilities

Initial recognition

Date of recognition

All regular way purchases and sales of financial assets and liabilities are recognised on the trade date i.e. the date that the Group commits to purchase the asset or liability. Regular way purchases or sales are purchases or sales of financial assets and liabilities that require delivery of assets and liabilities within the period generally established by regulation or convention in the marketplace.

Initial measurement

The classification of financial instruments at initial recognition depends on their contractual terms and the business model for managing the instruments. Financial instruments are initially measured at their fair value and, except in the case of financial assets and financial liabilities recorded at FVPL, transaction costs are added to, or subtracted from, this amount.

Measurement categories of financial assets and liabilities

The Group classifies all of its financial assets based on the business model for managing the assets and the asset's contractual terms, measured at either:

- Amortised cost;
- FVOCI;
- FVPL.

The Group classifies and measures its derivative portfolio at FVPL. The Group may designate financial instruments at FVPL, if so doing eliminates or significantly reduces measurement or recognition inconsistencies.

Financial liabilities, other than loan commitments and financial guarantees, are measured at amortised cost or at FVPL when they are held for trading, are derivative instruments or the fair value designation is applied.

Amounts due from credit institutions, loans to customers, investments securities at amortised cost

The Group only measures amounts due from credit institutions, loans to customers and other financial investments at amortised cost if both of the following conditions are met:

- The financial asset is held within a business model with the objective to hold financial assets in order to collect contractual cash flows;
- The contractual terms of the financial asset give rise on specified dates to cash flows that are solely payments of principal and interest on the principal amount outstanding (SPPI).

(thousands of Georgian lari)

3. Summary of accounting policies (continued)

Financial assets and liabilities (continued)

The details of these conditions are outlined below:

Business model assessment

The Group determines its business model at the level that best reflects how it manages groups of financial assets to achieve its business objective.

The Group's business model is not assessed on an instrument–by–instrument basis, but at a higher level of aggregated portfolios and is based on observable factors such as:

- How the performance of the business model and the financial assets held within that business model are evaluated and reported to the entity's key management personnel;
- The risks that affect the performance of the business model (and the financial assets held within that business model) and, in particular, the way those risks are managed;
- How managers of the business are compensated (for example, whether the compensation is based on the fair value of the assets managed or on the contractual cash flows collected);
- The expected frequency, value and timing of sales are also important aspects of the Group's assessment.

The business model assessment is based on reasonably expected scenarios without taking 'worst case' or 'stress case' scenarios into account. If cash flows after initial recognition are realised in a way that is different from the Group's original expectations, the Group does not change the classification of the remaining financial assets held in that business model, but incorporates such information when assessing newly originated or newly purchased financial assets going forward.

The SPPI test

As a second step of its classification process the Group assesses the contractual terms of financial asset to identify whether they meet the SPPI test.

'Principal' for the purpose of this test is defined as the fair value of the financial asset at initial recognition and may change over the life of the financial asset (for example, if there are repayments of principal or amortisation of the premium/discount).

The most significant elements of interest within a lending arrangement are typically the consideration for the time value of money and credit risk. To make the SPPI assessment, the Group applies judgement and considers relevant factors such as the currency in which the financial asset is denominated, and the period for which the interest rate is set.

In contrast, contractual terms that introduce a more than de minimis exposure to risks or volatility in the contractual cash flows that are unrelated to a basic lending arrangement do not give rise to contractual cash flows that are solely payments of principal and interest on the amount outstanding. In such cases, the financial asset is required to be measured at FVPL.

Letters of credit and undrawn loan commitments

The Group issues letters of credit and loan commitments. Undrawn loan commitments and letters of credits are commitments under which, over the duration of the commitment, the Group is required to provide a loan with pre–specified terms to the customer.

Performance guarantees

Performance guarantees are contracts that provide compensation if another party fails to perform a contractual obligation. Performance guarantees do not transfer credit risk. The risk under performance guarantee contracts is the possibility that the failure to perform the contractual obligation by another party occurs. Therefore, performance guarantees are not considered financial instruments and thus do not fall in scope of IFRS 9.

Reclassification of financial assets and liabilities

The Group does not reclassify its financial assets subsequent to their initial recognition, apart from the exceptional circumstances in which the Group changes the business model for managing financial assets. Financial liabilities are never reclassified. The Group did not reclassify any of its financial assets and liabilities in 2020.

(thousands of Georgian lari)

3. Summary of accounting policies (continued)

Renegotiated loans

Where possible, the Group seeks to restructure loans rather than to take possession of collateral or begin enforcement procedures. This may involve extending the payment arrangements and the agreement of new loan conditions.

The Group derecognises a financial asset, such as a loan to a customer, when the terms and conditions have been renegotiated to the extent that, substantially, it becomes a new loan, with the difference recognised as a derecognition gain or loss, to the extent that an impairment loss has not already been recorded. The newly recognised loans are classified as Stage 1 for ECL measurement purposes, unless the new loan is deemed to be POCI. When assessing whether or not to derecognise a loan to a customer, amongst others, the Group considers the following factors:

- Change in currency of the loan;
- Change in counterparty;
- If the modification is such that the instrument would no longer meet the SPPI criterion.

If the modification does not result in cash flows that are substantially different, the modification does not result in derecognition. Based on the change in cash flows discounted at the original EIR, the Group records a modification gain or loss, presented within interest revenue calculated using EIR in the statement of profit or loss, to the extent that an impairment loss has not already been recorded.

For modifications not resulting in derecognition, the Group also reassesses whether here has been a significant increase in credit risk or whether the assets should be classified as credit–impaired. In particular, it has revised indicators of significant increase in credit risk and does not automatically consider the credit risk to have significantly increased in the case of a loan modification being part of the Government support measures. Asset that has been classified as credit–impaired as the result of modification, can be recorded as Stage 2 or Stage 3 if certain criteria are met according to the Group's approved methodology.

Derecognition of financial assets and liabilities

Financial assets

A financial asset (or, where applicable a part of a financial asset or part of a group of similar financial assets) is derecognised where:

- The rights to receive cash flows from the asset have expired;
- The Group has transferred its rights to receive cash flows from the asset, or retained the right to receive cash flows from the asset, but has assumed an obligation to pay them in full without material Delay to a third party under a "pass–through" arrangement; and
- the Group either (a) has transferred substantially all the risks and rewards of the asset, or (b) has neither transferred nor retained substantially all the risks and rewards of the asset, but has transferred control of the asset.

Where the Group has transferred its rights to receive cash flows from an asset and has neither transferred nor retained substantially all the risks and rewards of the asset nor transferred control of the asset, the asset is recognised to the extent of the Group's continuing involvement in the asset. Continuing involvement that takes the form of a guarantee over the transferred asset is measured at the lower of the original carrying amount of the asset and the maximum amount of consideration that the Bank could be required to repay.

Write–off

Financial assets are written off either partially or in their entirety only when the Group has stopped pursuing the recovery. If the amount to be written off is greater than the accumulated loss allowance, the difference is first treated as an addition to the allowance that is then applied against the gross carrying amount. Any subsequent recoveries are credited to credit loss expense. A write–off constitutes a derecognition event.

Financial liabilities

A financial liability is derecognised when the obligation under the liability is discharged or cancelled or expires.

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, and the difference in the respective carrying amounts is recognised in profit or loss.

(thousands of Georgian lari)

3. Summary of accounting policies (continued)

Cash and cash equivalents

Cash and cash equivalents consist of cash on hand, amounts due from the National Bank of Georgia, excluding mandatory reserves, and amounts due from credit institutions that mature within ninety days of the date of origination and are free from contractual encumbrances.

Mandatory reserve deposit with the NBG

Mandatory reserve deposits with the NBG are carried at amortised cost and represent interest bearing mandatory reserve deposits which are not available to finance the Group'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. Mandatory reserve is included in amounts due from credit institutions.

Offsetting of financial instruments

Financial assets and liabilities are offset and the net amount is reported in the statement of financial position when there is a legally enforceable right to set off the recognised amounts and there is an intention to settle on a net basis, or to realise the asset and settle the liability simultaneously. The right of set–off must not be contingent on a future event and must be legally enforceable in all of the following circumstances:

- The normal course of business;
- The event of default; and
- The event of insolvency or bankruptcy of the entity and all of the counterparties.

These conditions are not generally met in master netting agreements, and the related assets and liabilities are presented gross in the statement of financial position.

Taxation

The current income tax expense is calculated in accordance with the regulations of Georgia.

Deferred tax assets and liabilities are calculated in respect of temporary differences using the liability method. Deferred income taxes are provided for all temporary differences arising between the tax bases of assets and liabilities and their carrying values for financial reporting purposes, except where the deferred income tax arises from the initial recognition of goodwill or of an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit nor taxable profit or loss.

A deferred tax asset is recorded only to the extent that it is probable that taxable profit will be available against which the deductible temporary differences can be utilised. Deferred tax assets and liabilities are measured at tax rates that are expected to apply to the period when the asset is realised or the liability is settled, based on tax rates (applicable to undistributed profits) and tax laws, that have been enacted or substantively enacted by the end of the reporting period.

Georgia also has various operating taxes that are assessed on the Group's activities. These taxes are included as a component of other operating expenses.

Leases

i. Group as a lessee

The Group applies a single recognition and measurement approach for all leases, except for short–term leases and leases of low–value assets. The Group recognises lease liabilities to make lease payments and right–of–use assets representing the right to use the underlying assets.

<u>Right–of–use assets</u>

The Group recognises right–of–use assets at the commencement date of the lease (i.e., the date the underlying asset is available for use). Right–of–use assets are measured at cost, less any accumulated depreciation and impairment losses, and adjusted for any remeasurement of lease liabilities. The cost of right–of–use assets includes the amount of lease liabilities recognised, initial direct costs incurred, and lease payments made at or before the commencement date less any lease incentives received. Unless the Group is reasonably certain to obtain ownership of the leased asset at the end of the lease term, the recognised right–of–use assets are depreciated on a straight–line basis over the shorter of its estimated useful life and the lease term. Right–of–use assets are subject to impairment.

(thousands of Georgian lari)

3. Summary of accounting policies (continued)

Leases (continued)

Lease liabilities

At the commencement date of the lease, the Group recognises lease liabilities measured at the present value of lease payments to be made over the lease term. The lease payments include fixed payments (including in–substance fixed payments) less any lease incentives receivable, variable lease payments that depend on an index or a rate, and amounts expected to be paid under residual value guarantees. The variable lease payments that do not depend on an index or a rate are recognised as expense in the period on which the event or condition that triggers the payment occurs.

In calculating the present value of lease payments, the Group uses the incremental borrowing rate at the lease commencement date if the interest rate implicit in the lease is not readily determinable. After the commencement date, the amount of lease liabilities is increased to reflect the accretion of interest and reduced for the lease payments made. In addition, the carrying amount of lease liabilities is remeasured if there is a modification, a change in the lease term, a change in the in–substance fixed lease payments or a change in the assessment to purchase the underlying asset.

Short–term leases and leases of low–value assets

The Group applies the short–term lease recognition exemption to its short–term leases (i.e., those leases that have a lease term of 12 months or less from the commencement date and do not contain a purchase option). It also applies the lease of low–value assets recognition exemption to leases of office equipment that are considered of low value. Lease payments on short–term leases and leases of low–value assets are recognised as expense on a straight–line basis over the lease term.

ii. Operating − Group as a lessor

Leases in which the Group does not transfer substantially all the risks and rewards incidental to ownership of an asset are classified as operating leases. Rental income arising is accounted for on a straight-line basis over the lease terms and is included in other income, in the consolidated statement of profit or loss due to its operating nature, that is disclosed in note 21.

Property and equipment

Property and equipment are carried at cost, excluding the costs of day–to–day servicing, less accumulated depreciation and any accumulated impairment. Such cost includes the cost of replacing part of equipment when that cost is incurred if the recognition criteria are met.

The carrying values of property and equipment are reviewed for impairment when events or changes in circumstances indicate that the carrying value may not be recoverable.

Depreciation of an asset begins when it is available for use. Depreciation is calculated on a straight–line basis using the following annual depreciation rates:

Buildings and other real estate	2–3%
Furniture and office fixtures	10–20%
Computers and office equipment	10–33%
Other	5–20%

The asset's residual values, useful lives and methods are reviewed, and adjusted as appropriate, at each financial year–end.

Costs related to repairs and renewals are charged when incurred and included in other operating expenses, unless they qualify for capitalization.

Intangible assets

Intangible assets include computer software and licenses. Intangible assets acquired separately are measured on initial recognition at cost. The cost of intangible assets acquired in a business combination is fair value as at the date of acquisition. Following initial recognition, intangible assets are carried at cost less any accumulated amortisation and any accumulated impairment losses. The useful lives of intangible assets are assessed to be either finite or indefinite.

Intangible assets with finite lives are amortised over the useful economic lives of 10 years and assessed for impairment whenever there is an indication that the intangible asset may be impaired. Amortisation periods and methods for intangible assets with indefinite useful lives are reviewed at least at each financial year–end.

(thousands of Georgian lari)

3. Summary of accounting policies (continued)

Provisions

Provisions are recognised when the Group has a present legal or constructive obligation as a result of past events, and it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation and a reliable estimate of the amount of obligation can be made.

Contingencies

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

Share capital

Ordinary shares are classified as equity. External costs directly attributable to the issue of new shares, other than on a business combination, are shown as a deduction from the proceeds in equity. Any excess of the fair value of consideration received over the par value of shares issued is recognised as additional paid–in capital.

Dividends are recognised as a liability and deducted from equity at the reporting date only if they are declared before or on the reporting date. Dividends are disclosed when they are proposed before the reporting date or proposed or declared after the reporting date but before the consolidated financial statements are authorised for issue. All expenses associated with dividend distribution are added to dividend amount and recorded directly through equity.

Recognition of income and expenses

Revenue is recognised to the extent that it is probable that the economic benefits will flow to the Group and the revenue can be reliably measured. The following specific recognition criteria must also be met before revenue is recognised:

Interest and similar income and expense

The Group calculates interest revenue on debt financial assets measured at amortized cost by applying the EIR to the gross carrying amount of financial assets other than credit–impaired assets. EIR is the rate that exactly discounts estimated future cash payments or receipts through the expected life of the financial instrument or a shorter period, where appropriate, to the net carrying amount of the financial asset or financial liability. The calculation takes into account all contractual terms of the financial instrument (for example, prepayment options) and includes any fees or incremental costs that are directly attributable to the instrument and are an integral part of the effective interest rate, but not future credit losses. The carrying amount of the financial asset or financial liability is adjusted if the Group revises its estimates of payments or receipts. The adjusted carrying amount is calculated based on the original effective interest rate and the change in carrying amount is recorded as interest revenue or expense.

When a financial asset becomes credit–impaired, the Group calculates interest revenue by applying the effective interest rate to the net amortised cost of the financial asset. If the financial assets cures and is no longer credit–impaired, the Group reverts to calculating interest revenue on a gross basis.

Interest revenue on all financial assets at FVPL is recognised using the contractual interest rate.

Fee and commission income

The Group earns fee and commission income from several types of services it provides to its customers. Fee income can be divided into the following categories:

Fee income earned from services that are provided over a certain period of time

Fees earned for the provision of services over a period of time are accrued over that period. These fees include commission income on guarantees and letters of credit. Loan commitment fees for loans that are likely to be drawn down and other credit related fees are deferred (together with any incremental costs) and recognised as an adjustment to the effective interest rate on the loan.

Fee income earned at a point in time

Fees arising from settlement and cash operations are recognized upon completion of the underlying transactions. Each cash operation and settlement operation is treated as a separate performance obligation.

(thousands of Georgian lari)

3. Summary of accounting policies (continued)

Recognition of income and expenses (continued)

Fee income from providing transaction services

Fees arising from negotiating or participating in the negotiation of a transaction for a third party − such as where the Group's performance obligation is the arrangement of the acquisition of shares or other securities − are recognised on completion of the underlying transaction. Fees or components of fees that are linked to certain performance obligations are recognised after fulfilling the corresponding criteria. When the contract provides for a variable consideration, fee and commission income is only recognized to the extent that it is probable that a significant reversal in the amount of cumulative revenue recognized will not occur until the uncertainty associated with the variable consideration is subsequently resolved.

Foreign currency translation

The consolidated financial statements are presented in Georgian lari ("GEL"), which is the Group's functional and presentation currency. Transactions in foreign currencies are initially recorded in the functional currency, converted at the rate of exchange ruling at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies are retranslated at the functional currency rate of exchange ruling at the reporting date. Gains and losses resulting from the translation of foreign currency transactions are recognised in the statement of profit or loss as gains less losses from foreign currencies − translation differences. Non–monetary items that are measured in terms of historical cost in a foreign currency are translated using the exchange rates as at the dates of the initial transactions. Non–monetary items measured at fair value in a foreign currency are translated using the exchange rates at the date when the fair value was determined.

Differences between the contractual exchange rate of a transaction in a foreign currency and the NBG exchange rate on the date of the transaction are included in gains less losses from dealing in foreign currencies. The official GEL exchange rates at 31 December 2020 and 2019 were 3.2766 GEL and 2.8677 GEL to 1 USD, respectively, 4.0233 GEL and 3.2095 GEL to 1 EUR, respectively.

Standards issued but not yet effective

The new and amended standards and interpretations that are issued, but not yet effective, up to the date of issuance of the Group's financial statements are disclosed below. The Group intends to adopt these new and amended standards and interpretations, if applicable, when they become effective.

IFRS 17 Insurance contracts

In May 2017, the IASB issued IFRS 17 Insurance Contracts (IFRS 17), a comprehensive new accounting standard for insurance contracts covering recognition and measurement, presentation and disclosure. Once effective, IFRS 17 will replace IFRS 4 Insurance Contracts (IFRS 4) that was issued in 2005. IFRS 17 applies to all types of insurance contracts (i.e., life, non-life, direct insurance and re-insurance), regardless of the type of entities that issue them, as well as to certain guarantees and financial instruments with discretionary participation features. A few scope exceptions will apply. IFRS 17 introduces new accounting requirements for banking products with insurance features that may affect the determination of which instruments or which components thereof will be in the scope of IFRS 9 or IFRS 17.

Credit cards and similar products that provide insurance coverage: most issuers of these products will be able to continue with their existing accounting treatment as a financial instrument under IFRS 9. IFRS 17 excludes from its scope credit card contracts (and other similar contracts that provide credit or payment arrangements) that meet the definition of an insurance contract if, and only if, the entity does not reflect an assessment of the insurance risk associated with an individual customer in setting the price of the contract with that customer.

When the insurance coverage is provided as part of the contractual terms of the credit card, the issuer is required to:

- Separate the insurance coverage component and apply IFRS 17 to it
- Apply other applicable standards (such as IFRS 9, IFRS 15 Revenue from Contracts with Customers or IAS 37 Provisions, Contingent Liabilities and Contingent Assets) to the other components

Loan contracts that meet the definition of insurance but limit the compensation for insured events to the amount otherwise required to settle the policyholder's obligation created by the contract: Issuers of such loans – e.g. a loan with waiver on death – have an option to apply IFRS 9 or IFRS 17. The election would be made at a portfolio level and would be irrevocable.

(thousands of Georgian lari)

3. Summary of accounting policies (continued)

Standards issued but not yet effective (continued)

IFRS 17 is effective for reporting periods beginning on or after 1 January 2023, with comparative figures required. Early application is permitted, provided the entity also applies IFRS 9 and IFRS 15 on or before the date it first applies IFRS 17.

The Group is currently in the process of assessing the impact of adopting IFRS 17 on its consolidated financial statements.

IFRS 9 Financial Instruments – Fees in the '10 per cent' test for derecognition of financial liabilities

As part of its 2018-2020 Annual Improvements to IFRS standards process, the IASB issued an amendment to IFRS 9. The amendment clarifies the fees that an entity includes when assessing whether the terms of a new or modified financial liability are substantially different from the terms of the original financial liability. These fees include only those paid or received between the borrower and the lender, including fees paid or received by either the borrower or lender on the other's behalf. An entity applies the amendment to financial liabilities that are modified or exchanged on or after the beginning of the annual reporting period in which the entity first applies the amendment.

The amendment is effective for annual reporting periods beginning on or after 1 January 2022 with earlier adoption permitted. The Group will apply the amendments to consolidated financial liabilities that are modified or exchanged on or after the beginning of the annual period in which it will first apply the amendment and does not expect this will result in a material impact on its consolidated financial statements.

Interest Rate Benchmark Reform - Phase 2 Amendments to IFRS 9, IAS 39 IFRS 7, IFRS 4 and IFRS 16

In August 2020 the IASB issued Interest Rate Benchmark Reform - Phase 2 Amendments to IFRS 9, IAS 39, IFRS 7, IFRS 4 and IFRS 16, (IBOR reform Phase 2) to address the accounting issues which arise upon the replacement of an IBOR with a RFR.

IBOR reform Phase 2 includes a number of reliefs and additional disclosures. The reliefs apply upon the transition of a financial instrument from an IBOR to a risk-free-rate (RFR).

Changes to the basis for determining contractual cash flows as a result of interest rate benchmark reform are required as a practical expedient to be treated as changes to a floating interest rate, provided that, for the financial instrument, the transition from the IBOR benchmark rate to RFR takes place on an economically equivalent basis.

The Group will apply IBOR reform Phase 2 from 1 January 2021.

4. Significant accounting judgments and estimates

Estimation uncertainty

In the process of applying the Group's accounting policies, management has used its judgments and made estimates in determining the amounts recognized in the financial statements. The most significant use of judgments and estimates are as follows:

Impairment losses on financial assets

The measurement of impairment losses under IFRS 9 across all categories of financial assets requires, judgement, in particular, the estimation of the amount and timing of future cash flows and collateral values when determining impairment losses and the assessment of a significant increase in credit risk. These estimates are driven by a number of factors, changes in which can result in different levels of allowances. The Group's ECL calculations are outputs of complex models with a number of underlying assumptions regarding the choice of variable inputs and their interdependencies. Elements of the ECL models that are considered accounting judgements and estimates include:

- The Group's model which assigns PDs to the individual grades;
- The Group's criteria for assessing if there has been a significant increase in credit risk and so allowances for financial assets should be measured on a LTECL basis;
- The segmentation of financial assets when their ECL is assessed on a collective basis;
- Development of ECL models, including the various formulae and the choice of inputs;
- Determination of relationship between borrowers' financials and, macroeconomic inputs, such as GDP growth rate, foreign exchange rates and inflation rate, and the effect on PDs, EADs and LGDs;
- Selection of forward–looking macroeconomic scenarios and their probability weightings, to derive the economic inputs into the ECL models.

(thousands of Georgian lari)

4. Significant accounting judgments and estimates (continued)

Estimation uncertainty (continued)

The amount of allowance for loans to customers, investment securities and credit related commitments recognized in the consolidated statement of financial position at 31 December 2020 was GEL 152,502 (2019: GEL 113,568), GEL 1,543 (2019: GEL 409) and GEL 1,650 (2019: GEL 1,350), respectively. Refer to Note 7, Note 8 and Note 18.

To assess potential impact of ongoing COVID-19 pandemic on its ECL, the Group introduced certain changes in process of estimating expected credit losses. The Group has performed the analysis of portfolio using Covid-19 related stress scenarios agreed with the National Bank of Georgia (NBG). Portfolio was reviewed under the stress conditions included all the borrowers and sectors. the expected revenues for the next two years were reduced by different percentage points for different corporate borrowers, based on sector vulnerability to COVID 19 stress and was assumed that economy will fully recover in three years. Based on the results of the stress test, corporate borrowers with potential significant increase in credit risk since initial recognition, have been identified based on the solvency ratios and have been reclassified into stage 2 or stage 3 impairment buckets. In case of retail segment, the selection included the borrowers with loans modified at least twice since the beginning of COVID-19 pandemic and without renewed information about their disposable incomes.

In addition, the Group revised its approach to LGD assessment, to reflect increased risk of GEL/USD rate volatility caused by COVID-19 related economic downturn. In the previous models, the Group applied automatic update to GEL value of collateral based on the change of GEL to USD exchange rate from the date of valuation till the reporting date. Due to said volatility of exchange rates in 2020, the Group discontinued this practice and only updates values of collateral as a result of a full valuation exercise or uses latest values as assessed in GEL. This change resulted in increased ECL in amount of GEL 17,357 thousand as at 31 December 2020 .

Forward looking information used in ECL assessment process has also been modified according to the macroeconomic forecasts published by the NBG. For details on provisioning results please refer to Note 7.

Fair value of financial instruments

Where the fair values of financial assets and financial liabilities recorded in the statement of financial position cannot be derived from active markets, they are determined using a variety of valuation techniques that include the use of mathematical models. The input to these models is taken from observable markets where possible, but where this is not feasible, a degree of judgment is required in establishing fair values. Additional details are provided in Note 24.

Valuation of repossessed assets

Repossessed assets are initially recognized at cost (net book value of the loan) and subsequently measured at the lower of carrying amount and fair value less costs to sell.

The valuation was carried out by an independent firm of valuators which holds a recognised and relevant professional qualification and who have recent experience in valuation of assets of similar location and category. In the process of comparison, they have used three comparative analogues (registered sale and/or offer for sale), by applied price adjustments based on the difference between subject assets and analogues. The values of most of the assets have been estimated using the market approach. Additional details are provided in Note 12.

5. Cash and cash equivalents

Cash and cash equivalents comprise:

	2020	***2019***
Cash on hand	27,479	16,965
Current accounts with the NBG	5,159	3,380
Current accounts with other credit institutions	62,002	108,236
Time deposits with credit institutions up to 90 days	43,815	19,037
Less − allowance for impairment	(54)	(20)
Cash and cash equivalents	**138,401**	**147,598**

As at 31 December 2020, current accounts and time deposit accounts with credit institutions denominated in USD, GEL and EUR represent 49%, 15% and 33% of total current and time deposit accounts respectively (31 December 2019: USD 65%, GEL 9%, EUR 25%).

All balances of cash equivalents are held at amortized cost and are allocated to Stage 1.

(thousands of Georgian lari)

6. Amounts due from credit institutions

Amounts due from credit institutions comprise:

	2020	*2019*
Mandatory reserve with the NBG	203,927	164,100
Time deposits for more than 90 days	7,807	4,848
Less − allowance for impairment	(51)	(43)
Amounts due from credit institutions	**211,683**	**168,905**

In 2020 the credit institutions are required to maintain a mandatory interest earning cash deposit with the NBG at the level of 5% and 25% (2019: 5% and 25%) of the average of funds attracted from customers and non–resident financial institutions for the appropriate two–week period in GEL and foreign currencies, respectively.

An analysis of changes in the gross carrying value and corresponding ECL in relation to amounts due from credit institutions during the year ended 31 December 2020 is as follows:

	Gross carrying value	*ECL*
As at 1 January 2020	**4,848**	**2**
New assets originated	2,305	–
Assets repaid	(51)	–
Foreign exchange and other movements	705	–
At 31 December 2020	**7,807**	**2**

An analysis of changes in the gross carrying value and corresponding ECL in relation to amounts due from credit institutions during the year ended 31 December 2019 is as follows:

	Gross carrying value	*ECL*
As at 1 January 2019	**11,836**	**12**
New assets originated	6,230	51
Assets repaid	(13,325)	(61)
Foreign exchange and other movements	107	–
At 31 December 2019	**4,848**	**2**

All balances of amounts due from credit institutions are held at amortized cost and are allocated to Stage 1.

7. Loans to customers

Loans to customers comprise:

	2020	*2019*
Corporate loans	1,158,960	960,744
Loans to individuals	31,331	32,153
Gross loans to customers at amortized cost	**1,190,291**	**992,897**
Less − allowance for impairment	(158,451)	(113,568)
Loans to customers at amortized cost	**1,031,840**	**879,329**

(thousands of Georgian lari)

7. Loans to customers (continued)

An analysis of changes in the gross carrying value in relation to corporate lending during the year ended 31 December 2020 is as follows:

Corporate loans at amortized cost, gross	**Stage 1**	**Stage 2**	**Stage 3**	**POCI**	**Total**
Gross carrying value as at 1 January 2020	**520,940**	**46,063**	**278,275**	**115,466**	**960,744**
New assets originated or purchased	430,311	1,770	45,377	–	**477,458**
Assets repaid or derecognised	(265,633)	(21,050)	(54,626)	(56,726)	**(398,035)**
Resegmentation	–	–	514	–	**514**
Transfers to Stage 1	15,878	(6,791)	(9,087)	–	**–**
Transfers to Stage 2	(62,742)	62,742	–	–	**–**
Transfers to Stage 3	(42,739)	(35,303)	78,042	–	**–**
Unwinding of discount	–	–	3,803	–	**3,803**
Changes to contractual cash flows due to modifications not resulting in derecognition	(1,281)	(575)	(508)	51	**(2,313)**
Recoveries	–	–	–	–	**–**
Amounts written off	–	–	(4,034)	–	**(4,034)**
Foreign exchange and other movements	57,241	3,739	41,613	18,230	**120,823**
At 31 December 2020	**651,975**	**50,595**	**379,369**	**77,021**	**1,158,960**

Corporate loans at amortized cost, allowance for ECL	***Stage 1***	***Stage 2***	***Stage 3***	***POCI***	***Total***
ECL as at 1 January 2020	**3,122**	**692**	**78,380**	**29,622**	**111,816**
New assets originated or purchased	6,561	23	14,707	–	**21,291**
Assets repaid or derecognised	(1,508)	(456)	(13,885)	(6,345)	**(22,194)**
Resegmentation	–	–	–	3	**3**
Transfers to Stage 1	2,953	(158)	(2,795)	–	**–**
Transfers to Stage 2	(145)	145	–	–	**–**
Transfers to Stage 3	(2,639)	(806)	3,445	–	**–**
Impact on period end ECL of exposures transferred between stages during the period	(2,900)	1,061	3,661	–	**1,822**
Unwinding of discount	–	–	3,803	–	**3,803**
Changes due to modifications not resulting in derecognition	(112)	(23)	(329)	(15)	**(479)**
Recoveries	–	–	–	–	**–**
Amounts written off	–	–	(4,033)	–	**(4,033)**
Foreign exchange and other movements	4,442	(239)	29,632	10,540	**44,375**
At 31 December 2020	**9,774**	**239**	**112,586**	**33,805**	**156,404**

An analysis of changes in the gross carrying value and corresponding ECL in relation to loans to individuals during the year ended 31 December 2020 is as follows:

Loans to individuals at amortized cost, gross	***Stage 1***	***Stage 2***	***Stage 3***	***Total***
Gross carrying value as at 1 January 2020	**25,382**	**733**	**6,038**	**32,153**
New assets originated	9,133	23	801	**9,957**
Assets repaid or derecognised	(11,438)	(310)	(2,032)	**(13,780)**
Resegmentation	–	–	(514)	**(514)**
Transfers to Stage 1	147	(147)	–	**–**
Transfers to Stage 2	(4,995)	5,089	(94)	**–**
Transfers to Stage 3	(570)	(2,631)	3,201	**–**
Unwinding of discount	–	–	85	**85**
Changes to contractual cash flows due to modifications not resulting in derecognition	(14)	(16)	(89)	**(119)**
Recoveries	–	–	5	**5**
Amounts written off	–	–	(639)	**(639)**
Foreign exchange and other movements	2,934	289	960	**4,183**
At 31 December 2020	**20,579**	**3,030**	**7,722**	**31,331**

(thousands of Georgian lari)

7. Loans to customers (continued)

Loans to individuals at amortized cost, allowance for ECL	***Stage 1***	***Stage 2***	***Stage 3***	***Total***
ECL as at 1 January 2020	**86**	**42**	**1,624**	**1,752**
New assets originated	133	3	14	**150**
Assets repaid or derecognised	(86)	(10)	(53)	**(149)**
Resegmentation	–	–	(3)	**(3)**
Transfers to Stage 1	6	(6)	–	**–**
Transfers to Stage 2	(44)	49	(5)	**–**
Transfers to Stage 3	(6)	(127)	133	**–**
Impact on period end ECL of exposures transferred between stages during the period	(5)	130	203	**328**
Unwinding of discount	–	–	85	**85**
Changes due to modifications not resulting in derecognition	–	(3)	(60)	**(63)**
Recoveries	–	–	5	**5**
Amounts written off	–	–	(638)	**(638)**
Foreign exchange and other movements	17	4	559	**580**
At 31 December 2020	**101**	**82**	**1,864**	**2,047**

An analysis of changes in the gross carrying value in relation to corporate lending during the year ended 31 December 2019 is as follows:

Corporate loans at amortized cost, gross	***Stage 1***	***Stage 2***	***Stage 3***	***POCI***	***Total***
Gross carrying value as at 1 January 2019	**412,446**	**107,288**	**350,720**	**–**	**870,454**
New assets originated or purchased	503,428	4,213	75,443	116,857	**699,941**
Assets repaid or derecognised	(393,242)	(27,050)	(230,006)	(285)	**(650,583)**
Transfers to Stage 1	19,916	(6,840)	(13,076)	–	**–**
Transfers to Stage 2	(25,989)	34,946	(8,957)	–	**–**
Transfers to Stage 3	(2,868)	(68,324)	71,192	–	**–**
Unwinding of discount	–	–	4,728	–	**4,728**
Changes to contractual cash flows due to modifications not resulting in derecognition	(858)	–	6	–	**(852)**
Recoveries	–	–	18,929	–	**18,929**
Amounts written off	–	–	(17,906)	–	**(17,906)**
Foreign exchange and other movements	8,107	1,830	27,202	(1,106)	**36,033**
At 31 December 2019	**520,940**	**46,063**	**278,275**	**115,466**	**960,744**

Corporate loans at amortized cost, allowance for ECL	***Stage 1***	***Stage 2***	***Stage 3***	***POCI***	***Total***
ECL as at 1 January 2019	**4,855**	**7,117**	**78,478**	**–**	**90,450**
New assets originated or purchased	4,685	20	16,197	29,685	**50,587**
Assets repaid or derecognised	(5,846)	(311)	(54,279)	(1)	**(60,437)**
Transfers to Stage 1	3,405	(155)	(3,250)	–	**–**
Transfers to Stage 2	(523)	2,025	(1,502)	–	**–**
Transfers to Stage 3	(256)	(8,834)	9,090	–	**–**
Impact on period end ECL of exposures transferred between stages during the period	(3,241)	79	2,567	–	**(595)**
Unwinding of discount	–	–	4,728	–	**4,728**
Changes due to modifications not resulting in derecognition	(7)	–	–	–	**(7)**
Recoveries	–	–	18,929	–	**18,929**
Amounts written off	–	–	(17,906)	–	**(17,906)**
Foreign exchange and other movements	50	751	25,328	(62)	**26,067**
At 31 December 2019	**3,122**	**692**	**78,380**	**29,622**	**111,816**

(thousands of Georgian lari)

7. Loans to customers (continued)

An analysis of changes in the gross carrying value and corresponding ECL in relation to loans to individuals during the year ended 31 December 2019 is as follows:

Loans to individuals at amortized cost, gross	***Stage 1***	***Stage 2***	***Stage 3***	***Total***
Gross carrying value as at 1 January 2019	**35,925**	**1,683**	**6,674**	**44,282**
New assets originated	19,224	1,131	548	**20,903**
Assets repaid or derecognised	(29,399)	(3,450)	(1,590)	**(34,439)**
Transfers to Stage 1	5	–	(5)	**–**
Transfers to Stage 2	(1,589)	1,609	(20)	**–**
Transfers to Stage 3	(19)	(446)	465	**–**
Unwinding of discount	–	–	65	**65**
Changes to contractual cash flows due to modifications not resulting in derecognition	(39)	–	–	**(39)**
Foreign exchange and other movements	1,274	206	(99)	**1,381**
At 31 December 2019	**25,382**	**733**	**6,038**	**32,153**

Loans to individuals at amortized cost, allowance for ECL	***Stage 1***	***Stage 2***	***Stage 3***	***Total***
ECL as at 1 January 2019	**100**	**141**	**2,150**	**2,391**
New assets originated	39	42	22	**103**
Assets repaid or derecognised	(27)	(44)	(316)	**(387)**
Transfers to Stage 1	–	–	–	**–**
Transfers to Stage 2	(3)	3	–	**–**
Transfers to Stage 3	–	(85)	85	**–**
Impact on period end ECL of exposures transferred between stages during the period	–	7	2	**9**
Unwinding of discount	–	–	65	**65**
Foreign exchange and other movements	(23)	(22)	(384)	**(429)**
At 31 December 2019	**86**	**42**	**1,624**	**1,752**

COVID-19 model adjustments

As at 31 December 2020, the Group introduced certain changes in its process of estimation of expected credit losses in the context of the ongoing COVID-19 pandemic. The Group also updated forward looking information, including forecasts of macroeconomic indicators and scenarios' weights.

COVID-19 model adjustments made in estimating the reported ECL as at 31 December 2020 are set out in the following table:

	Pre-COVID-19 model ECL	***COVID-19 model adjustments***	***Total ECL***	***Adjustments as a % of total ECL***
Corporate lending	139,526	16,881	156,407	12.0%
Consumer lending	1,570	476	2,046	0.3%
Total	**141,096**	**17,357**	**158,453**	**12.3%**

COVID-19 model adjustments represent adjustments in relation to data and model limitations as a result of the COVID-19 economic disruption. The adjustments are based on a combination of portfolio level credit risk analysis and an evaluation of ECL coverage at an exposure level.

The Group subjected financial performance of the borrowers to various stress scenarios based on the nature and the sector of the borrower, which resulted in the downgrading of their credit quality and resulted in reclassification of a significant number of stage 1 borrowers in stages 2 and 3. Furthermore, due to high depreciation of Georgian Lari to USD, the Group revised its approach to LGD calculation, to reflect increased risk of GEL/USD rate volatility caused by COVID-19 related economic downturn. In the previous models, the Group applied automatic update to GEL value of collateral based on the change of GEL to USD exchange rate from the date of valuation till the reporting date. Due to said volatility of exchange rates in 2020, the Group discontinued this practice and only updates values of collateral as a result of a full valuation exercise or uses latest values as assessed in GEL .

(thousands of Georgian lari)

7. Loans to customers (continued)

Modified and restructured loans

The Group derecognises a financial asset, such as a loan to a customer, when the terms and conditions have been renegotiated to the extent that, substantially, it becomes a new loan. The newly recognised loans are classified as Stage 1 for ECL measurement purposes, unless the new loan is deemed to be POCI.

If the modification does not result in cash flows that are substantially different, the modification does not result in derecognition. Based on the change in cash flows discounted at the original EIR, Group records a modification gain or loss, to the extent that an impairment loss has not already been recorded.

During 2020, the Group has modified the terms and conditions of certain mortgage and consumer loans, including introduction of payment holidays, as part of the measures related to consequences of COVID-19 pandemic. The Group considered these modifications to be non-substantial.

The table below includes Stage 2 and 3 assets that were modified during the period, with the related modification loss suffered by the Group.

	2020	*2019*
Loans modified during the period		
Amortised cost before modification	395,539	36,236
Net modification loss	(2,432)	(891)
Loans modified since initial recognition		
Gross carrying amount at 1 January of loans for which loss allowance has changed to 12–month measurement during the period	–	5,576

Collateral and other credit enhancements

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 types of collateral normally obtained are charges over real estate properties, also cash covers and guarantees, provided by borrowers or third parties.

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 loan impairment.

The following table provides the analysis of the loan portfolio by collateral types. For loans where various type of collateral is pledged, the most significant one is taken as a major type of collateral for the purpose of this allocation:

Type of collateral	***Gross carrying amount at 31 December 2020***	***ECL as at 31 December 2020***	***Net carrying amount as at 31 December 2020***
Loans collateralized by pledge of real estate	884,958	(99,867)	785,091
Loans collateralized by pledge of cash	56,773	–	56,773
Loans collateralized by pledge of equipment	92,866	(16,853)	76,013
Loans collateralized by pledge of Inventory	59,890	(2,951)	56,939
Other collateral	3,594	(2,843)	751
Unsecured loans	92,210	(35,937)	56,273
Total	**1,190,291**	**(158,451)**	**1,031,840**

Type of collateral	***Gross carrying amount at 31 December 2019***	***ECL as at 31 December 2019***	***Net carrying amount as at 31 December 2019***
Loans collateralized by pledge of real estate	**797,186**	**(78,689)**	**718,497**
Loans collateralized by pledge of cash	12,715	(9)	**12,706**
Loans collateralized by pledge of equipment	39,500	(8,382)	**31,118**
Loans collateralized by pledge of Inventory	80,323	(1,589)	**78,734**
Other collateral	3,374	(2,393)	**981**
Unsecured loans	59,799	(22,506)	**37,293**
Total	**992,897**	**(113,568)**	**879,329**

(thousands of Georgian lari)

7. Loans to customers (continued)

Collateral and other credit enhancements (continued)

Management estimates that the fair value of collateral at the inception of the loans is at least equal to the carrying amounts of corresponding secured loans. The fair value of collaterals are reassessed as at 31 December 2020 and 2019.

Concentration of loans to customers

As at 31 December 2020, the Group had a concentration of loans due from 6 major groups of borrowers in the total exposure of GEL 378,896 that represented 31.8% of the total gross loan portfolio (31 December 2019: GEL 308,703 with 31.2% of the gross loan portfolio). An allowance of GEL 18,939 (31 December 2019: an allowance of GEL 31,491) was recognised against these loans.

Loans are made within Georgia in the following industry sectors:

	2020	***2019***
Trade and services	467,797	381,108
Manufacturing	351,553	298,013
Construction	241,197	194,394
Agriculture	58,835	51,060
Individuals	31,330	32,153
Energy	238	14,572
Transport and communication	180	194
Other	39,161	21,403
	1,190,291	**992,897**

8. Investment securities

Investment securities comprise:

	2020	***2019***
Debt securities at amortised cost		
Treasury bills of the Ministry of Finance of Georgia	7,864	13,471
Certificates of deposit of the National Bank of Georgia	–	7,916
Treasury notes of the Ministry of Finance of Georgia	25,667	3,688
Debt securities of non–financial corporations	19,912	17,803
	53,443	**42,878**
Less: allowance for impairment	(474)	(409)
Debt securities at amortised cost	**52,969**	**42,469**

Equity securities at FVOCI	***% of ownership***	***2020***	***2019***
Investment in OJSC United Clearing Center	6.25%	54	54
Investment in JSC GSCD	0.27%	3	3
Investment in JSC United finance corporation	0.47%	–	–
Equity securities at FVOCI		**57**	**57**

As at 31 December 2020 and 2019, management estimated fair value of investment equity instruments and concluded that fair value approximates to its cost.

Debt securities at FVOCI	***2020***	***2019***
Treasury notes of the Ministry of Finance	9,312	–
Debt securities at FVOCI	**9,312**	**–**

(thousands of Georgian lari)

8. Investment securities (continued)

An analysis of changes in the gross carrying value and associated ECL in relation to debt securities at amortized cost is as follows:

	Treasury bills of the Ministry of Finance of Georgia	*Certificates of deposit of the National Bank of Georgia*	*Treasury notes of the Ministry of Finance of Georgia*	*Debt securities of non–financial corporations*	*Total*
Gross carrying value as at 1 January 2020	**13,471**	**7,916**	**3,688**	**17,803**	**42,878**
New assets originated	10,000	4,000	22,667	–	**36,667**
Assets repaid	(16,000)	(12,000)	(1,575)	–	**(29,575)**
Foreign exchange and other movements	393	84	887	2,109	**3,473**
At 31 December 2020	**7,864**	**–**	**25,667**	**19,912**	**53,443**

	Treasury bills of the Ministry of Finance of Georgia	*Certificates of deposit of the National Bank of Georgia*	*Treasury notes of the Ministry of Finance of Georgia*	*Debt securities of non–financial corporations*	*Total*
ECL as at 1 January 2020	**22**	**–**	**20**	**367**	**409**
New assets originated	21	–	72	–	**93**
Assets repaid	(4)	–	(4)	–	**(8)**
Foreign exchange and other movements	(34)	–	(19)	33	**(20)**
At 31 December 2020	**5**	**–**	**69**	**400**	**474**

An analysis of changes in the gross carrying in relation to debt securities at fair value through other comprehensive income is as follows:

	Treasury notes of the Ministry of Finance of Georgia
Gross Carrying value as at 1 January 2020	**–**
New assets originated	9,000
Changes in Fair Value	242
Foreign exchange and other movements	70
At 31 December 2020	**9,312**

	Treasury bills of the Ministry of Finance of Georgia	*Certificates of deposit of the National Bank of Georgia*	*Treasury notes of the Ministry of Finance of Georgia*	*Debt securities of non–financial corporations*	*Total*
Gross carrying value as at 1 January 2019	**13,724**	**5,585**	**–**	**–**	**19,309**
New assets originated	17,500	18,276	3,575	16,466	**55,817**
Assets repaid	(17,563)	(15,897)	–	–	**(33,460)**
Foreign exchange and other movements	(190)	(48)	113	1,337	**1,212**
At 31 December 2019	**13,471**	**7,916**	**3,688**	**17,803**	**42,878**

(thousands of Georgian lari)

8. Investment securities (continued)

	Treasury bills of the Ministry of Finance of Georgia	*Certificates of deposit of the National Bank of Georgia*	*Treasury notes of the Ministry of Finance of Georgia*	*Debt securities of non–financial corporations*	*Total*
ECL as at 1 January 2019	**14**	**–**	**–**	**–**	**14**
New assets originated	42	–	33	343	**418**
Assets repaid	(4)	–	–	–	**(4)**
Foreign exchange and other movements	(30)	–	(13)	24	**(19)**
At 31 December 2019	**22**	**–**	**20**	**367**	**409**

All balances of investment securities that are held at amortized cost are allocated to Stage 1.

9. Property and equipment

The movements in property and equipment were as follows:

	Buildings and other real estate	*Furniture and fixtures*	*Computers and equipment*	*Leasehold improvements and other*	*Construction in progress*	*Total*
Cost						
1 January 2019	**10,360**	**6,776**	**7,365**	**2,220**	**42**	**26,763**
Additions	–	19	396	1,337	697	**2,449**
Disposals	–	(14)	(1,062)	(1,821)	(473)	**(3,370)**
31 December 2019	**10,360**	**6,781**	**6,698**	**1,736**	**267**	**25,842**
Additions	–	87	493	15	92	**687**
Transfers	92	216	–	–	(308)	**–**
Disposals and write–offs	(392)	(608)	(52)	(87)	–	**(1,139)**
Transfers to other assets	(150)	–	–	–	–	**(150)**
31 December 2020	**9,910**	**6,476**	**7,139**	**1,664**	**51**	**25,240**
Accumulated depreciation						
1 January 2019	**2,149**	**5,372**	**5,084**	**1,575**	**–**	**14,180**
Depreciation charge	249	50	831	383	–	**1,513**
Disposals and write–offs	**–**	(14)	(1,057)	(1,800)	–	**(2,871)**
31 December 2019	**2,398**	**5,408**	**4,858**	**158**	**–**	**12,822**
Depreciation charge	253	354	802	201	–	**1,610**
Disposals and write–offs	(392)	(608)	(52)	(79)	–	**(1,131)**
31 December 2020	**2,259**	**5,154**	**5,608**	**280**	**–**	**13,301**
Net book value						
1 January 2019	**8,211**	**1,404**	**2,281**	**645**	**42**	**12,583**
31 December 2019	**7,962**	**1,373**	**1,840**	**1,578**	**267**	**13,020**
31 December 2020	**7,651**	**1,322**	**1,531**	**1,384**	**50**	**11,939**

As at 31 December 2020 fully depreciated items amounted GEL 6,627 (2019: GEL 5,162).

(thousands of Georgian lari)

10. Right of use assets

The movement in right–of–use assets and lease liabilities were as follows:

	Right of use assets – Buildings	***Lease liabilities***
As at 1 January 2020	**5,436**	**5,680**
Additions	158	158
Depreciation expense	(1,410)	–
Interest expense	–	487
Payments	–	(1,750)
As at 31 December 2020	**4,184**	**4,575**

The Group recognised rent expense of GEL 258 from short–term and other operating leases for the period ended 31 December 2020 (2019: GEL 258).

	Right of use assets – Buildings	***Lease liabilities***
As at 1 January 2019	**6,853**	**6,853**
Depreciation expense	(1,417)	
Interest expense	–	602
Payments	–	(1,775)
As at 31 December 2019	**5,436**	**5,680**

11. Intangible assets

The movements in intangible assets were as follows:

	Licenses	***Computer software***	***Total***
Cost			
1 January 2019	**7,237**	**2,177**	**9,414**
Additions	218	106	**324**
Disposals and write offs	(730)	(73)	**(803)**
31 December 2019	**6,725**	**2,210**	**8,935**
Additions	378	73	**451**
Disposals and write offs	(218)	(47)	**(265)**
31 December 2020	**6,885**	**2,236**	**9,121**
Accumulated amortization			
1 January 2019	**2,946**	**1,246**	**4,192**
Amortisation charge	931	220	**1,151**
Disposals and write offs	(730)	(73)	**(803)**
31 December 2019	**3,147**	**1,393**	**4,540**
Amortisation charge	1,120	165	**1,285**
Disposals and write offs	(217)	(48)	**(265)**
31 December 2020	**4,050**	**1,510**	**5,560**
Net book value			
1 January 2019	**4,291**	**931**	**5,222**
31 December 2019	**3,578**	**817**	**4,395**
31 December 2020	**2,835**	**726**	**3,561**

(thousands of Georgian lari)

12. Other assets and liabilities

Other assets comprise:

	2020	*2019*
Other non–financial assets		
Repossessed assets	61,015	60,702
Reinsurance receivable	3,500	2,958
Prepaid taxes other than income tax	1,892	1,892
Advances paid	1,091	707
Inventory	116	126
Other	119	120
	67,733	**66,505**
Other financial assets		
Insurance premium receivable	4,219	4,431
Accounts receivable	1,212	1,576
Claims for guarantees paid	1,664	1,764
Less: allowance for impairment of other assets	(2,720)	(1,242)
Total other assets	**72,108**	**73,034**

An analysis of changes in the ECLs for stage 3 other financial assets for the year ended 31 December 2020 and 2019 is as follows:

	2020	2019
ECL at 1 January 2019	**1,242**	**419**
ECL charge	3,510	823
Write-offs	(2,032)	–
At 31 December 2019	**2,720**	**1,242**

Repossessed assets as at 31 December 2020 include land and buildings in amount of GEL 54,485 (31 December 2019: GEL 54,056) and movable properties in amounts of GEL 6,530 (31 December 2019: GEL 6,646), which are measured at the lower of its carrying amount and fair value less cost to sell.

Other liabilities comprise:

	2020	2019
Other financial liabilities		
Payables for reinsurance liabilities	3,606	3,413
Accounts payable	4,198	2,281
Derivative financial liabilities	1,957	–
	9,761	**5,694**
Other non–financial liabilities		
Unearned premium	4,398	3,866
Advances received	926	–
Provision for insurance reserves	369	529
Taxes other than income tax	488	–
Other	284	275
	6,465	**4,670**
Total other liabilities	**16,226**	**10,364**

The table below shows the fair values of derivative financial instruments, recorded as assets or liabilities, together with their notional amounts. The notional amount, recorded gross, is the amount of a derivative's underlying asset, reference rate or index and is the basis upon which changes in the value of derivatives are measured. The notional amounts indicate the volume of transactions outstanding at the year end and are not indicative of the credit risk.

(thousands of Georgian lari)

12. Other assets and liabilities (continued)

	2020			
	Notional amount		*Fair values*	
	Asset	*Liability*	*Asset*	*Liability*
Foreign exchange contracts				
Forwards and swaps − foreign	78,247	80,204	–	1,957
Total derivative assets/ liabilities	**78,247**	**80,204**	**–**	**1,957**

13. Amounts due to credit institutions

Amounts due to credit institutions comprise:

	2020	2019
Current accounts from resident commercial banks	9	13
Amounts due to credit institutions	**9**	**13**

14. Amounts due to customers

The amounts due to customers include the following:

	2020	2019
Current and demand accounts	442,128	437,477
Time deposits (including certificates of deposit)	534,062	340,797
Amounts due to customers	**976,190**	**778,274**

As at 31 December 2020, amounts due to customers included balances with ten largest customers of GEL 509,564 that constituted 52% of the total of customer accounts (31 December 2019: GEL 441,014 that constituted 57% of the total of customer accounts).

An analysis of customer accounts by economic sector follows:

	2020	2019
Trade and service	421,868	328,985
Individuals	309,516	255,825
Transport and communication	51,665	76,772
Construction	20,614	24,039
Manufacturing	5,883	11,159
Energy	31,491	2,947
Agriculture	11,487	2,073
Other	123,666	76,474
Amounts due to customers	**976,190**	**778,274**

As at 31 December 2020 deposits by customers included balances classified in Trade and service and individual sectors amounting to GEL 225,912 (31 December 2019: GEL 197,140), that were freezed on the basis of a court decision dated as of 11 September 2015.

(thousands of Georgian lari)

15. Subordinated debt

Subordinated loans consisted of the following:

Facility provider	*Commencement date*	*Maturity date*	*Interest rate*	*Currency*	*Original contractual value*	*Carrying value as at 31 December 2020*
Fin Service XXI	31-Mar-11	31-Mar-27	5.50%	USD	51,177	98,298
Fin Service XXI	09-Oct-20	Perpetual	5.50%	USD	32,233	16,839
Cartu Group	24-Jun-19	Perpetual	5.50%	USD	17,144	22,957
Inter Consulting Plus	17-Oct-05	17-Oct-26	5.50%	USD	12,642	22,936
Inter Consulting Plus	22-May-18	22-May-43	5.50%	USD	3,898	5,243
Georgian Holding	21-Jun-04	21-Jun-29	5.50%	USD	19,200	32,766
						199,039

Facility provider	*Commencement date*	*Maturity date*	*Interest rate*	*Currency*	*Original contractual value*	*Carrying value as at 31 December 2019*
Fin Service XXI	31–Mar–11	31–Mar–26	4.5%	USD	51,177	81,989
Fin Service XXI	13–Dec–11	31–Mar–26	4.5%	USD	16,561	27,340
Fin Service XXI	15–Feb–13	31–May–28	4.5%	USD	16,574	27,015
Cartu Group	24–Jun–19	Perpetual	5.5%	USD	17,144	20,092
Inter Consulting Plus	22–May–18	22–May–43	4.5%	USD	3,898	4,064
Inter Consulting Plus	17–Oct–05	17–Oct–25	4.5%	USD	12,642	19,197
Georgian Holding	21–Jun–04	21–Jun–29	4.5%	USD	19,200	26,803
						206,500

In the event of bankruptcy or liquidation of the Group, repayment of these debts is subordinate to the repayments of the Group's liabilities to all other creditors.

The Group increased the interest rate on all the subordinated debt from 4.5% to 5.5%. The Group considered the effect of change by applying 10% threshold test and concluded that modification of subordinated debt is not substantial. Consequently, the effect of the changes has been accounted by reduction of paid in capital in amount of GEL 10,748.

On October 2020 the Group has agreed with Ltd Fin Service XXI to make changes in the contractual maturity of its lending agreement by making the debt perpetual. Also, the interest rate increased from 4.5% to 5.5%. The market interest rate has been defined at 11.15%. Consequently, the effect of the changes has been accounted as an increase in paid in capital of GEL 15,926.

The table below details changes in the Group's subordinated debts arising from financing activities. Liabilities arising from financing activities are those for which cash flows were, or future cash flows will be, classified in the Group's consolidated statement of cash flows as cash flows from financing activities.

	1 January 2020	*Repayment*	*Modification loss recognized in profit and loss*	*Modification gain recognized in additional paid in capital*	*Additional paid in capital recognised at initial recognition*	*Interest accrual during 2020*	*Interest paid during 2020*	*Foreign exchange loss during 2020*	*31 December 2020*
Subordinated debt	206,500	(32,233)	–	10,748	(15,926)	12,287	(11,987)	29,650	**199,039**

The table below details changes in the Group's subordinated debts arising from financing activities during 2019:

	1 January 2019	*Repayment*	*Modification loss recognized in profit and loss*	*Modification gain recognized in additional paid in capital*	*Additional paid in capital recognised at initial recognition*	*Interest accrual during 2019*	*Interest paid during 2019*	*Foreign exchange loss during 2019*	*31 December 2019*
Subordinated debt	190,595	–	1,074	–	–	10,882	(9,677)	13,626	206,500

The amortised value of the subordinated loan qualified for the inclusion in the Tier 2 capital under the NBG Basel III requirements, was GEL 159,243 corresponding to GEL 159,243 under IFRS 9 (31 December 2019: GEL 196,724 corresponding to GEL 186,408 under IFRS 9). The amortised value of the subordinated loan qualified for the inclusion in the additional Tier 1 capital under the NBG Basel III requirements, was GEL 55,702 corresponding to GEL 40,040 under IFRS 9 (31 December 2019: GEL 20,074 corresponding to GEL 20,083 under IFRS 9).

(thousands of Georgian lari)

16. Taxation

In June 2016 amendments to the Georgian tax law in respect of corporate income tax became enacted. The amendments became effective from 1 January 2017 for all Georgian companies except the banks, insurance companies and microfinance organization, for which the effective date was initially set at January 2019. On 5 May 2018 amendment was made in tax code and the date was revised to January 2023.Therefore the Group had recognized those deferred tax asset and deferred tax liability which are estimated to be realised before 2023. Under the new regulation, corporate income tax will be levied on profit distributed as dividends, rather than on profit earned as under the current regulation. The amount of tax payable on a dividend distribution will be calculated as 15/85 of the amount of net distribution. The companies will be able to offset corporate income tax liability arising from dividend distributions out of profits earned in 2008–2016 by the amount of corporate income tax paid for the respective period under the current regulation. Dividends distributions between Georgian resident companies will not be subject to corporate income tax.

Georgian tax legislation is subject to varying interpretations, and changes, which can occur frequently. Management's interpretation of such legislation as applied to the transactions and activity of the Group may be challenged by the relevant tax authorities. It is possible that transactions and activities that have not been challenged in the past may be challenged in the future. As such, significant additional taxes, penalties and interest may be assessed. Fiscal periods remain open to review by the authorities in respect of taxes for three calendar years preceding the year of review. Under certain circumstances reviews may cover longer periods.

Management believes that its interpretation of the relevant legislation as at 31 December 2020 is appropriate and that the Group's tax, currency and customs positions will be sustained.

The corporate income tax expense for the years ended 31 December 2020 and 2019 comprised:

	2020	*2019*
Current tax (benefit)/expense	–	5,022
Deferred tax expense/(benefit)	(1,234)	(1,183)
Income tax (benefit)/expense	**(1,234)**	**3,839**

In 2020 and 2019 the income tax rate applicable to most of the Group's income is 15%. The effective income tax rate differs from the statutory income tax rate. A reconciliation of the income tax benefit/expense on statutory rates with actual is as follows:

	2020	*2019*
Profit before income tax	**8,598**	**26,153**
Statutory tax rate	15%	15%
Theoretical income tax expense at the statutory rate	**1,290**	**3,923**
Tax exempt income	(846)	(592)
Non–deductible expenses	234	197
Unrecognized deferred taxes pertaining to years after 2023	(1,912)	446
Other	–	(135)
Income tax (benefit)/expense	**(1,234)**	**3,839**

Deferred tax liabilities and assets as at 31 December 2020 and 31 December 2019 and their movements for the respective period

	2018	**Through statement of profit and loss**	**2019**	**Through statement of profit and loss**	**2020**
Tax effect of temporary differences					
Cash and cash equivalents	10	(10)	–	–	–
Subordinated debt	(509)	(67)	(576)	576	–
Tax losses carried forward	–	329	329	2,343	2,672
Other Assets	973	174	1,147	1,505	2,652
Lease liabilities	–	759	759	(187)	572
Provisions	(148)	626	478	(111)	367
Amounts due to Customers	–	352	352	(161)	191
Investment Securities	2	362	364	(221)	143
Intangible assets	(89)	26	(63)	109	46
Amounts due from credit institutions	5	42	47	(41)	6
Deferred tax asset	**244**	**2,593**	**2,837**	**3,812**	**6,649**
Loans to customers	(8,340)	(276)	(8,616)	(1,578)	(10,194)
Other Liabilities	28	(223)	(195)	(1,138)	(1,333)
Property and Equipment	(570)	(130)	(699)	(69)	(768)
Right of use assets	–	(760)	(760)	201	(559)
Amounts due to Credit Institutions	(1)	(20)	(21)	6	(15)
Deferred tax Liability	**(8,883)**	**(1,409)**	**(10,291)**	**(2,578)**	**(12,869)**
Deferred tax (liability)/asset	**(8,639)**	**1,184**	**(7,454)**	**1,234**	**(6,220)**

(thousands of Georgian lari)

17. Equity

As at 31 December 2020 and 2019, authorized, issued and fully paid capital amounted to GEL 114,430 comprising of 114,430,000 common shares with nominal value of GEL 1 each. Each share entitles one vote to the shareholder.

In 2020 the Group has not declared and has not disbursed dividends (2019: GEL 45,000).

Additional paid–in capital represents the difference between a fair value and a nominal amount at initial recognition, and modification, which were deemed non-substantial, of the subordinated loans received from the Parent and entities under common control.

18. Commitments and contingencies

Commitments and contingencies

As at 31 December 2020 and 2019, the Group's commitments and contingencies comprised the following:

	2020	*2019*
Credit related commitments		
Unused credit lines	38,040	31,453
Guarantees issued	40,513	28,704
	78,553	**60,157**
Operating lease commitments		
Not later than 1 year	–	124
More than 1 year but less than 5 years	–	355
	–	**479**
Less − ECL for credit related commitments	(833)	(1,350)
Commitments and contingencies	**77,720**	**59,286**

An analysis of changes in the ECL allowances during the year is as follows:

Undrawn loan commitments	*Stage 1*	*Stage 2*	*Stage 3*	*Total*
ECLs as at 1 January 2020	**145**	**33**	**107**	**285**
New exposures	1,997	49	2,895	**4,941**
Amounts paid	(853)	(63)	(2,438)	**(3,354)**
Expired exposures	–	–	–	**–**
Transfers to Stage 1	362	(13)	(349)	**–**
Transfers to Stage 2	(10)	55	(45)	**–**
Transfers to Stage 3	(599)	(7)	606	**–**
POCI	–	3	3	**6**
Impact on period end ECL of exposures transferred between stages during the period	(353)	103	(490)	**(740)**
Unwinding of discount	–	–	–	**–**
Changes to models and inputs used for ECL calculations	–	–	–	**–**
Foreign exchange adjustments	(330)	(79)	(28)	**(437)**
At 31 December 2020	**359**	**81**	**261**	**701**

Financial guarantees	*Stage 1*	*Stage 2*	*Stage 3*	*Total*
ECLs as at 1 January 2020	**35**	**(1)**	**1,031**	**1,065**
New exposures	51	2	80	**133**
Amounts paid	(65)	(1)	(1,227)	**(1,293)**
Expired exposures	–	–	–	**–**
Transfers to Stage 1	–	–	–	–
Transfers to Stage 2	(2)	2	–	**–**
Transfers to Stage 3	–	(6)	6	**–**
Impact on period end ECL of exposures transferred between stages during the period	–	5	19	**24**
Unwind of discount	–	–	–	**–**
Changes to models and inputs used for ECL calculations	–	–	–	**–**
Foreign exchange adjustments	73	–	130	**203**
At 31 December 2020	**92**	**1**	**39**	**132**

(thousands of Georgian lari)

18. Commitments and contingencies (continued)

An analysis of changes in the ECLs during the year ended 31 December 2019 is as follows:

Undrawn loan commitments	*Stage 1*	*Stage 2*	*Stage 3*	*Total*
ECLs as at 1 January 2019	**302**	**5**	**48**	**355**
New exposures	1,587	17	967	**2,571**
Amounts paid	(526)	(41)	(861)	**(1,428)**
Expired exposures	–	–	–	**–**
Transfers to Stage 1	–	–	–	**–**
Transfers to Stage 2	(38)	38	–	**–**
Transfers to Stage 3		(6)	6	**–**
Impact on period end ECL of exposures transferred between stages during the period	(429)	(2)	5	**(426)**
Unwinding of discount	–	–	–	**–**
Changes to models and inputs used for ECL calculations	–	–	–	**–**
Foreign exchange adjustments	(751)	22	(58)	**(787)**
At 31 December 2019	**145**	**33**	**107**	**285**

Financial guarantees	*Stage 1*	*Stage 2*	*Stage 3*	*Total*
ECLs as at 1 January 2019	**776**	**20**	**518**	**1,314**
New exposures	2,871	541	2,180	**5,592**
Amounts paid	(1,211)	(589)	(3,314)	**(5,114)**
Expired exposures	–	–	–	**–**
Transfers to Stage 2	(1,429)	1,429	–	**–**
Transfers to Stage 3	(701)	(1,494)	2,195	**–**
Impact on period end ECL of exposures transferred between stages during the period	–	–	–	**–**
Unwind of discount	–	35	362	**397**
Changes to models and inputs used for ECL calculations	–	–	–	**–**
Foreign exchange adjustments	(272)	58	(910)	**(1,124)**
At 31 December 2019	**34**	**–**	**1,031**	**1,065**

ECL of letters of credit was nil during in 2020.

19. Credit loss expense and other impairment and provisions

The table below shows the ECL charges on financial instruments recorded in the consolidated statement of profit or loss for the year ended 31 December 2020:

	Notes	*Stage 1*	*Stage 2*	*Stage 3*	*POCI*	*Total*
Cash and cash equivalents		31	–	–	–	**31**
Amounts due from credit institutions		8	–	–	–	**8**
Loans to customers	7	6,667	(413)	35,229	4,183	**45,666**
Debt securities measured at amortised cost		65	–	–	–	**65**
Credit loss expense on interest bearing assets		**6,771**	**(413)**	**35,229**	**4,183**	**45,770**
Other financial assets	12	–	–	1,557	1,953	**3,510**
Financial guarantees	18	57	(1)	(989)	–	**(933)**
Undrawn loan commitments	18	215	50	151	–	**416**
Other impairment and provisions excluding repossessed assets		**272**	**49**	**719**	**1,953**	**2,993**
Provision reversal of repossessed assets						**(530)**
Other impairment and provisions						**2,463**

(thousands of Georgian lari)

19 Credit loss expense and other impairment and provisions (continued)

The table below shows the ECL charges on financial instruments recorded in the consolidated statement of profit or loss for the year ended 31 December 2019:

	Notes	*Stage 1*	*Stage 2*	*Stage 3*	*POCI*	*Total*
Cash and cash equivalents		(26)	–	–	–	**(26)**
Amounts due from credit institutions		(5)	–	–	–	**(5)**
Loans to customers	7	(1,747)	(6,523)	(6,440)	29,621	**14,911**
Debt securities measured at amortised cost		395	–	–	–	**395**
Credit loss expense on interest bearing assets		**(1,383)**	**(6,523)**	**(6,440)**	**29,621**	**15,275**
Other financial assets	12	–	–	823	–	**823**
Financial guarantees	18	(743)	(18)	512	–	**(249)**
Undrawn loan commitments	18	(157)	28	59	–	**(70)**
Other impairment and provisions excluding repossessed assets		**(900)**	**10**	**1,394**	**–**	**504**
Provision expense of repossessed assets						**3,207**
Other impairment and provisions						**3,711**

20. Fee and commission income and expense

Fee and commission income and expense comprise:

	2020	*2019*
Plastic card operations	2,187	3,033
Settlement operations	1,135	1,256
Cash operations	987	527
Guarantees and letters of credits issued	847	1,417
Documentary operations	27	26
Other	681	671
Fee and commission income	**5,864**	**6,930**
Plastic card operations	(3,737)	(4,411)
Settlement operations	(943)	(1,815)
Documentary operations	(30)	(158)
Guarantees and letters of credits issued	–	(14)
Other	(28)	(254)
Fee and commission expense	**(4,738)**	**(6,652)**

21. Other income, net

Other income/(expenses), net comprise:

	2020	*2019*
Net written premiums	7,326	8,661
Gain on disposal of repossessed assets	2,848	772
Change in provisions for reported but not settled claims	554	1,007
Income from operating lease	840	845
Fines and penalties received	104	101
Gain on disposal of property	28	62
Reinsurers' share of claims settled	(3,985)	(4,246)
Claims settled, net of reinsurance	(1,358)	(1,748)
Change in provisions for incurred but not reported claims	(540)	(811)
Other	(136)	132
Total other income, net	**5,681**	**4,775**

(thousands of Georgian lari)

22. Personnel and other operating expenses

Personnel and other operating expenses comprise:

	2020	*2019*
Salaries	13,161	12,814
Bonuses and other employee benefits	691	1,618
Personnel expenses	**13,852**	**14,432**
Communication	4,484	3,821
Charity costs	6	3,793
Maintenance and exploitation	618	774
Security expenses	804	768
Transportation and business trip expenses	356	490
Taxes other than income tax	980	464
Utilities	523	461
Professional services	711	451
Office supplies	162	273
Operating leases	258	258
Deposit insurance fee	191	148
Personnel training	20	104
Advertising costs	51	100
Membership fees	94	74
Insurance	105	59
Other expenses	1,095	1,394
Other operating expenses	**10,458**	**13,432**

Remuneration of the Group’s auditor for the years ended 31 December 2020 and 2019 comprises (net of VAT):

	2020	*2019*
Fees for the audit of the Group’s annual financial statements for the year ended 31 December	369	331
Expenditures for other professional service	61	43
Total fees and expenditures	**430**	**374**

Fees and expenditures payable to other auditors and audit firms in respect of other professional services comprised GEL 61 (2019: GEL 43).

The average number of the Group’s employees during 2020 was 328, including average 5 top management employees, average 22 middle management employees, and average 301 other full–time employees.

23. Risk management

Introduction

Risk is inherent in the Group’s activities but it is managed through a process of ongoing identification, measurement and monitoring, subject to risk limits and other controls. This process of risk management is critical to the Group’s continuing profitability and each individual within the Bank is accountable for the risk exposures relating to his or her responsibilities. The Group is exposed to credit risk, liquidity risk and market risk. It is also subject to operating risks.

The independent risk control process does not include business risks such as changes in the environment, technology and industry. They are monitored through the Group’s strategic planning process.

Risk management structure

Board of Directors

The Board of Directors is responsible for the overall risk management approach and for approving the risk strategies and principles. The Board of Directors is ultimately responsible for identifying and controlling risks and different departments and committees which are responsible for managing and monitoring risks.

(thousands of Georgian lari)

23. Risk management (continued)

Risk management structure (continued)

Risk management

The Risk Management Department is responsible for implementing and maintaining risk management framework.

Asset and Liability Committee

Asset and Liability Committee (ALCO) is responsible for managing the Group's assets and liabilities and the overall financial structure. It is also primarily responsible for the funding, liquidity, interest rate, and capital adequacy risks of the Group.

Internal Audit

Risk management processes throughout the Group are audited by the internal audit function on a constant basis, which examines the adequacy of the procedures, their design and operational effectiveness, and the Group's compliance both with the regulatory requirements and internal procedures. Internal Audit discusses the results of all assessments with management, and reports its findings and recommendations to the Audit Committee.

Audit Committee

The Audit Committee is responsible for the fundamental risk issues and manages and monitors relevant risk decisions and performance of control functions by other departments in the Group pertaining to general control environment, manual, IT dependent or application controls, intentional or unintentional misstatement risks, risk of fraud or misappropriation of assets, information security, anti–money laundering, etc. Audit committee is comprised of three members, out of which two are independent.

Risk measurement and reporting systems

Monitoring and controlling risks is primarily performed based on limits established by the Group. These limits reflect the business strategy and market environment of the Group as well as the level of risk that the Group is willing to accept. In addition the Group monitors and measures the overall risk bearing capacity in relation to the aggregate risk exposure across all risk types and activities. The main body to which the risks are reported is a risk management committee. The respective meetings are held once a month.

Excessive risk concentration

Concentrations arise when a number of counterparties are engaged in similar business activities, or activities in the same geographic region, or have similar economic features that would cause their ability to meet contractual obligations to be similarly affected by changes in economic, political or other conditions. Concentrations indicate the relative sensitivity of the Group's performance to developments affecting a particular industry or geographical location.

Credit risk

Credit risk is the risk that the Group will incur a loss because its customers, clients or counterparties failed to discharge their contractual obligations. The Group manages and controls credit risk by setting limits on the amount of risk it is willing to accept for individual counterparties and by monitoring exposures in relation to such limits.

The Group has established a credit quality review process to provide early identification of possible changes in the creditworthiness of counterparties, including regular collateral revisions. The credit quality review process allows the Group to assess the potential loss as a result of the risks to which it is exposed and take corrective action.

Actual exposure per borrower against limits is monitored on loans granted. The Credit Committee may initiate a change in the limits. Where appropriate, the Group obtains collateral and corporate guarantees. The credit risks are monitored on a continuous basis and are subject to annual or more frequent reviews.

Credit–related commitments risks

The Group makes available to its customers guarantees which may require that the Group make payments on their behalf. Such payments are collected from customers based on the terms of guarantee. They expose the Group to similar risks to loans and these are mitigated by the same control processes and policies.

(thousands of Georgian lari)

23. Risk management (continued)

Credit risk (continued)

Impairment assessment

From 1 January 2018, the Group calculates ECL based on several probability–weighted scenarios to measure the expected cash shortfalls, discounted at an approximation to the EIR. A cash shortfall is the difference between the cash flows that are due to the Group in accordance with the contract and the cash flows that the entity expects to receive. The mechanics of the ECL calculations are outlined below and the key elements are as follows:

PD The *Probability of Default* is an estimate of the likelihood of default over a given time horizon. A default may only happen at a certain time over the assessed period, if the facility has not been previously derecognised and is still in the portfolio.

EAD The *Exposure at Default* is an estimate of the exposure at a future default date, taking into account expected changes in the exposure after the reporting date, including repayments of principal and interest, whether scheduled by contract or otherwise, expected drawdowns on committed facilities, and accrued interest from missed payments.

LGD The *Loss Given Default* is an estimate of the loss arising in the case where a default occurs at a given time. It is based on the difference between the contractual cash flows due and those that the lender would expect to receive, including from the realisation of any collateral. It is usually expressed as a percentage of the EAD.

The ECL allowance is based on the 12 months' expected credit loss (12mECL), unless there has been significant increase in credit risk since origination or other impairment indicators were identified, in which case the ECL allowance is based on the credit losses expected to arise over the life of the asset (the lifetime expected credit loss or LTECL). The 12mECL is the portion of LTECL that represent the ECLs that result from default events on a financial instrument that are possible within the 12 months after the reporting date. Both LTECL and 12mECL are calculated on either an individual basis or a collective basis, depending on the nature of the underlying portfolio of financial instruments.

The Group has established a policy to perform an assessment, at the end of each reporting period, of whether a financial instrument's credit risk has increased significantly since initial recognition, by considering the change in the risk of default occurring over the remaining life of the financial instrument. Based on the above process, the Group groups its loans into Stage 1, Stage 2, Stage 3 and POCI, as described below:

Stage 1: When loans are first recognised, the Group recognises an allowance based on 12mECL. Stage 1 loans also include facilities where the credit risk has improved and the loan has been reclassified from Stage 2.

Stage 2: When a loan has shown a significant increase in credit risk since origination, the Group records an allowance for the LTECL. Stage 2 loans also include facilities, where the credit risk has improved and the loan has been reclassified from Stage 3.

Stage 3: Loans considered credit–impaired. The Group records an allowance for the LTECL.

POCI: Purchased or originated credit impaired (POCI) assets are financial assets that are credit impaired on initial recognition. POCI assets are recorded at fair value at original recognition and interest revenue is subsequently recognised based on a credit–adjusted EIR. ECL are only recognised or released to the extent that there is a subsequent change in the lifetime expected credit losses.

Definition of default and cure

The Group considers a financial instrument defaulted and therefore Stage 3 (credit–impaired) for ECL calculations in all cases when the borrower becomes 90 days past due on its contractual payments or classified as "non–performing" according to the NBG regulation on asset classification. The Group considers amounts due from Groups defaulted and takes immediate action when the required intraday payments are not settled by the close of business as outlined in the individual agreements.

As a part of a qualitative assessment of whether a customer is in default, the Group also considers a variety of instances that may indicate unlikeliness to pay. When such events occur, the Group carefully considers whether the event should result in treating the customer as defaulted and therefore assessed as Stage 3 for ECL calculations or whether Stage 2 is appropriate.

The Group has defined certain criteria which should be met in order to consider asset as cured. The decision whether to classify an asset as Stage 2 or Stage 1 once cured depends on the updated credit grade, at the time of the cure, and whether this indicates there has been a significant increase in credit risk compared to initial recognition.

(thousands of Georgian lari)

23. Risk management (continued)

Credit risk (continued)

PD model

To determine the PD rates for each group, the Group utilizes migration matrices based on "Markov chain" model. At the beginning of analysing 12–month period borrowers in each pool are grouped in 11 buckets by overdue days and the loan loss provision per the regulation of the NBG. The analysis is conducted on every 12–month period from December 2014 to the reporting date. The final PD used in the model represents the weighted average of the historical 12–month period PDs.

The Group has assessed the impact of the forward–looking information into collective assessment model as not material, thus, the results were not incorporated in ECLs.

As at 31 December 2020, 10% increase in average PD per each pool results in total ECL increase by 0.40% that represents GEL 639 and 10% decrease in average PD per each pool results in total ECL decrease by 1.97% that represents GEL 3,125 (31 December 2019: 10% increase in average PD per each pool results in total ECL increase by 0.23% that represents GEL 261 and 10% decrease in average PD per each pool results in total ECL decrease by 2.20% that represents GEL 2,500).

LGD model

Another component of impairment model is LGD (loss given default), that's is an estimate of the loss arising on default. To measure it, defaulted exposures by segments is reduced by deposits pledged and the discounted liquidation value of properties pledged using 2.5 years of time to collect period and valuation haircut. Impact of LGD is very material and ECL of the Group is heavily depended on the value of collateral.

As at 31 December 2020, 10% increase in valuation haircut results in ECL increase by 1.81% that represents GEL 2,864 and 10% decrease in valuation haircut results in ECL decrease by 1.80% that represents GEL 2,853 (31 December 2019: 10% increase in valuation haircut results in ECL increase by 1.4% that represents GEL 1,598 and 10% decrease in valuation haircut results in ECL decrease by 0.3% that represents GEL 348).

As at 31 December 2020,10% (three month) increase in time to collect period results in ECL increase by 3.86% that represents GEL 6,116 and 10% (three month) decrease in time to collect period results in ECL decrease by 3.93% that represents GEL 6,220 (31 December 2019: 10% (three month) increase in time to collect period results in ECL increase by 4.00% that represents GEL 4,576 and 10% (three month) decrease in time to collect period results in ECL decrease by 0.92% that represents GEL 1,047).

EAD model

The exposure at default (EAD) represents the gross carrying amount of the financial instruments subject to the impairment calculation, addressing both the client's ability to increase its exposure while approaching default and potential early repayments too. To calculate the EAD for a Stage 1 loan, the Group assesses the possible default events within 12 months for the calculation of the 12mECL. For Stage 2, Stage 3 and POCI financial assets, the exposure at default is considered for events over the lifetime of the instruments.

Significant increase in credit risk

The Group continuously monitors all assets subject to ECLs. In order to determine whether an instrument or a portfolio of instruments is subject to 12mECL or LTECL, the Group assesses whether there has been a significant increase in credit risk since initial recognition.

The Group also applies a secondary qualitative method for triggering a significant increase in credit risk for an asset, such as moving a customer/facility to the watch list, or the account becoming restructured due to credit event. Regardless of the change in credit grades, if contractual payments are more than 30 days past due, the credit risk is deemed to have increased significantly since initial recognition.

When estimating ECLs on a collective basis for a group of similar assets, the Group applies the same principles for assessing whether there has been a significant increase in credit risk since initial recognition.

To assess potential impact of ongoing COVID-19 pandemic on its ECL, the Group introduced certain changes in process of estimating expected credit losses. The Group has performed the analysis of portfolio using Covid-19 related stress scenarios agreed with the National Bank of Georgia (NBG). Portfolio was reviewed under the stress conditions included all the borrowers and sectors.

(thousands of Georgian lari)

23. Risk management (continued)

Credit risk (continued)

Treasury and interbank relationships, investment securities measured at amortized cost

The Group's treasury and interbank relationships and counterparties comprise financial services institutions, banks. For these relationships, the Group's risk management department analyses publicly available information such as financial information and other external data, e.g., the external ratings supplied by international rating agencies. The Group's investment securities measured at amortized cost are limited to T–bills and CDs issued by the Ministry of Finance of Georgia, thus credit rating of the country is used in estimation of the PDs for these instruments.

Corporate lending

For corporate loans, the borrowers are assessed by specialised credit risk employees of the Group. The credit risk assessment takes into account various historical, current and forward–looking information such as:

- Historical financial information together with forecasts and budgets prepared by the client. This financial information includes realised and expected results, solvency ratios, liquidity ratios and any other relevant ratios to measure the client's financial performance. Some of these indicators are captured in covenants with the clients and are, therefore, measured with greater attention;
- Any publicly available information on the clients from external parties. This includes external rating grades issued by rating agencies, independent analyst reports, publicly traded bond prices or press releases and articles;
- Any macro–economic or geopolitical information, e.g., GDP growth relevant for the specific industry and geographical segments where the client operates;
- Any other objectively supportable information on the quality and abilities of the client's management relevant for the company's performance.

Grouping financial assets measured on a collective basis

Dependent on the factors below, the Group calculates ECLs either on a collective or on an individual basis.

Asset classes where the Group calculates ECL on an individual basis include:

- All exposures higher than 1% of the Bank's regulatory capital (threshold as at 31 December 2020 and 2019: GEL 401 and GEL 427, respectively)
- Exposures that have been classified as POCI when the original loan was derecognised and a new loan was recognised as a result of a credit driven debt restructuring.

All other asset classes where The Group calculates ECL on a collective basis for all other asset classes except for those assessed individually.

The Group groups these exposures into smaller homogeneous portfolios, based on a combination of internal and external characteristics of the loans, for example overdue bucket, product type, or borrower's industry.

Forward–looking information and multiple economic scenarios

In its ECL models, the Group relies on a range of forward looking information as economic inputs, such as:

- GDP growth;
- Inflation rate;
- GEL/USD foreign exchange rate change.

The inputs and models used for calculating ECLs may not always capture all characteristics of the market at the date of the consolidated financial statements. To reflect this, qualitative adjustments or overlays are occasionally made as temporary adjustments when such differences are significantly material.

The Group obtains the forward–looking information from the sources published by the NBG, GeoStat, IMF, World and Regional Economic Outlooks, S&P Global Ratings and other. Experts of the Group's Risk Management Department determine the weights attributable to the multiple scenarios. The tables show the values of the key forward looking economic variables/assumptions used in each of the economic scenarios for the ECL calculations. The figures for "Subsequent years" represent a long–term average and so are the same for each scenario as at 31 December 2020.

(thousands of Georgian lari)

23. Risk management (continued)

Credit risk (continued)

Key drivers	*ECL scenario*	*Assigned probabilities, %*	*2021*	*2022*	*2023*	*Subsequent years*
GDP growth, %						
	Upside	25%	6.0%	5.0%	5.0%	5.0%
	Base case	50%	5.0%	4.5%	4.5%	4.5%
	Downside	25%	1.0%	4.0%	4.0%	4.0%
USD/GEL exchange rate						
	Upside	25%	3.11	2.96	2.96	2.96
	Base case	50%	3.28	3.28	3.28	3.28
	Downside	25%	3.60	3.42	3.42	3.42
Inflation rate, %						
	Upside	25%	3.0%	3.0%	3.0%	3.0%
	Base case	50%	0%	3.0%	3.0%	3.0%
	Downside	25%	0%	5.0%	5.0%	5.0%

Predicted relationship between the economic indicators and default and loss rates on loan portfolios have been developed based on analysing historical data over the past 5 years. Based on the Group's macro–economic model, there is no significant dependency between macro–economic variables and loan portfolio quality.

Credit quality per class of financial asset

Below table shows internal grades used in following tables:

	Internal grade	NBG classification
High grade	1	Standard
	2	
	3	
Standard grade	4	Standard
Sub–standard grade	5	Watch
Impaired	6	Substandard, Doubtful, Loss

The table below shows the credit quality by class of financial assets as at 31 December 2020:

31 December 2020	*Note*		*High grade*	*Standard grade*	*Sub–standard grade*	*Impaired*	*Total*
Cash and cash equivalents, except for cash on hand	5	Stage 1	104,922	6,000	–	–	**110,922**
Amounts due from credit institutions	6	Stage 1	211,683	–	–	–	**211,683**
Loans to customers at amortised cost	7						
		Stage 1	364,644	266,895	4,651	6,011	**642,201**
		Stage 2	–	21,328	18,285	10,743	**50,356**
		Stage 3	20,218	–	8,297	238,268	**266,783**
– Corporate lending		POCI	–	–	–	43,216	**43,216**
		Stage 1	19,420	253	805	–	**20,478**
		Stage 2	–	–	2,948	–	**2,948**
		Stage 3	–	–	–	5,858	**5,858**
– Loans to individuals							
Debt investment securities	8						
– measured at amortised cost		Stage 1	33,461	19,508	–	–	**52,969**
	18	Stage 1	20,573	14,615	993	–	**36,181**
		Stage 2	52	31	37	196	**316**
Undrawn loan commitments		Stage 3	5	–	–	837	**842**
	18	Stage 1	34,371	1,272	40	127	**35,810**
		Stage 2	–	–	–	–	**–**
Financial guarantees		Stage 3	40	–	–	4,531	**4,571**
Total			**809,389**	**329,902**	**36,056**	**309,787**	**1,485,134**

(thousands of Georgian lari)

23. Risk management (continued)

Credit risk (continued)

The table below shows the credit quality by class of financial assets as at 31 December 2019:

31 December 2019	*Note*		*High grade*	*Standard grade*	*Sub–standard grade*	*Impaired*	*Total*
Cash and cash equivalents, except for cash on hand	5	Stage 1	121,649	8,984	–	–	**130,633**
Amounts due from credit institutions	6	Stage 1	168,905	–	–	–	**168,905**
Loans to customers at amortised cost	7						
		Stage 1	295,698	161,210	60,910	–	**517,818**
		Stage 2	230	13,368	31,773	–	**45,371**
		Stage 3	–	–	809	199,086	**199,895**
– Corporate lending		POCI	–	–	–	85,844	**85,844**
		Stage 1	24,121	119	1,056	–	**25,296**
		Stage 2	–	–	691	–	**691**
		Stage 3	–	–	–	4,414	**4,414**
– Loans to individuals							
Debt investment securities	8						
– measured at amortised cost		Stage 1	25,036	17,433	–	–	**42,469**
	18	Stage 1	21,185	8,138	1,413	–	**30,736**
		Stage 2	–	–	244	–	**244**
Undrawn loan commitments		Stage 3	–	–	–	188	**188**
	18	Stage 1	15,185	5,055	5,030	–	**25,270**
		Stage 2	239	–	–	–	**239**
Financial guarantees		Stage 3	–	–	–	2,130	**2,130**
Total			**672,248**	**214,307**	**101,926**	**291,662**	**1,280,143**

See Note 7 for more detailed information with respect to the allowance for impairment of loans to customers.

Financial guarantees, letters of credit and loan commitments are assessed and a provision for expected credit losses is calculated in similar manner as for loans.

The geographical concentration of Group's financial assets and liabilities is set out below:

	2020				*2019*			
	Georgia	*OECD*	*Other Non–OECD*	*Total*	*Georgia*	*OECD*	*Other Non–OECD*	*Total*
Assets								
Cash and cash equivalents	128,285	6,383	3,733	**138,401**	140,641	2,636	4,321	**147,598**
Amounts due from credit institutions	206,703	4,816	164	**211,683**	164,707	1,177	3,021	**168,905**
Loans to customers	1,007,251	1,959	22,630	**1,031,840**	873,482	1,887	3,960	**879,329**
Investment securities	62,338	–	–	**62,338**	42,526	–	–	**42,526**
Other financial assets	4,375	–	–	**4,375**	2,097	–	4,432	**6,529**
	1,408,952	**13,158**	**26,527**	**1,448,637**	**1,223,453**	**5,700**	**15,734**	**1,244,887**
Liabilities								
Amounts due to credit institutions	9	–	–	**9**	13	–	–	**13**
Amounts due to customers	946,068	10,630	19,492	**976,190**	747,718	9,140	21,416	**778,274**
Lease liabilities	4,575	–	–	**4,575**	5,680	–	–	**5,680**
Other financial liabilities	9,761	–	–	**9,761**	2,281	–	3,413	**5,694**
Subordinated debt	199,039	–	–	**199,039**	206,500	–	–	**206,500**
	1,159,452	**10,630**	**19,492**	**1,189,574**	**962,192**	**9,140**	**24,829**	**996,161**
Net assets/(liabilities)	**249,500**	**2,528**	**7,035**	**259,063**	**261,261**	**(3,440)**	**(9,095)**	**248,726**

(thousands of Georgian lari)

23. Risk management (continued)

Liquidity risk and funding management

Liquidity risk is the risk that the Group will be unable to meet its payment obligations when they fall due under normal and stress circumstances.

On a monthly basis, the Assets and Liabilities Committee ("ALCO") controls liquidity risks by means of maturity analysis, determining the Group'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 Group 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 liquidity position is assessed and managed by the Group primarily on a standalone basis, based on certain liquidity ratios established by the NBG including Liquidity Coverage Ratio and Net Stable Funding Ratio. The Liquidity Coverage Ratio is calculated for GEL as well as the Foreign Currency and for both, total amount. The minimum required rates are as following: GEL requirement is at least 75% or more, for USD the minimum required rate equals to 100% and the same is for the total ratio. As of December 31, the LCR ratios were as following:

	2020, %			2019, %		
	GEL	**FX**	**Total**	**GEL**	**FX**	**Total**
Liquidity Coverage Ratio (Total Liquid Assets / Net Cashflow)	**278%**	**208%**	**219%**	**147%**	**389%**	**319%**

The Net Stable Funding Ratio is measuring Group's available stable funding and required stable funding. The minimum requirement for the ratio despite the currency equals to 100%. By the end of the financial year 2020, the ratio was as following:

	2020, %	**2019, %**
Net Stable Funding Ratio (NSFR) (Available Stable Funding / Required Stable Funding)	**124%**	**134%**

Analysis of financial liabilities by remaining contractual maturities

The tables below summarize the maturity profile of the Group's financial liabilities at 31 December based on contractual undiscounted repayment obligations. Repayments which are subject to notice are treated as if notice were to be given immediately. However, the Group expects that many customers will not request repayment on the earliest date the Group could be required to pay and the table does not reflect the expected cash flows indicated by the Group's deposit retention history.

As at 31 December 2020	***Less than 3 months***	***3 to 12 months***	***1 to 5 years***	***Over 5 years***	***Total***
Financial liabilities					
Amounts due to credit institutions	9	–	–	–	**9**
Amounts due to customers	292,631	293,753	329,670	146,656	**1,062,710**
Lease liabilities	445	1,334	3,470	–	**5,249**
Other financial liabilities	9,507	254	–	–	**9,761**
Subordinated debt	2,955	8,866	47,288	330,393	**389,502**
Total undiscounted financial liabilities	**305,547**	**304,207**	**380,428**	**477,049**	**1,467,231**

As at 31 December 2019	***Less than 3 months***	***3 to 12 months***	***1 to 5 years***	***Over 5 years***	***Total***
Financial liabilities					
Amounts due to credit institutions	13	–	–	–	**13**
Amounts due to customers	280,175	234,532	274,046	4,400	**793,153**
Lease liabilities	444	1,334	5,072	–	**6,850**
Other financial liabilities	2,059	3,635	–	–	**5,694**
Subordinated debt	2,485	7,498	39,851	263,881	**313,715**
Total undiscounted financial liabilities	**285,176**	**246,999**	**318,969**	**268,281**	**1,119,425**

(thousands of Georgian lari)

23. Risk management (continued)

Liquidity risk and funding management (continued)

The table below shows the contractual expiry by maturity of the Group's financial commitments and contingencies. Each undrawn loan commitment is included in the time band containing the earliest date it can be drawn down.

	Note	*Less than 3 months*	*3 to 12 months*	*1 to 5 years*	*Over 5 years*	*Total*
2020	18	16,239	35,505	23,938	2,871	**78,553**
2019	18	40,733	6,551	12,788	85	**60,157**

The Group expects that not all of the contingent liabilities or commitments will be drawn before expiry of the commitments. The maturity analysis does not reflect the historical stability of current accounts. Their liquidation has historically taken place over a longer period than indicated in the table above. These balances are included in amounts due in less than three months in the tables above.

Market risk

Market risk is the risk that the fair value or future cash flows of financial instruments will fluctuate due to changes in market variables such as interest rates, foreign exchanges, and equity prices.

Currency risk

Currency risk is the risk that the value of a financial instrument will fluctuate due to changes in foreign exchange rates. The Group has set limits on positions by currency based on the NBG regulations. Positions are monitored on a daily basis.

The tables below indicate the currencies to which the Group had significant exposure at 31 December on its monetary assets and liabilities. The analysis calculates the effect of a reasonably possible movement of the currency rate against the GEL, with all other variables held constant on the statement of profit or loss. The effect on equity does not differ from the effect on the statement of profit or loss. A negative amount in the table reflects a potential net reduction in the statement of profit or loss or equity, while a positive amount reflects a net potential increase.

Currency	*Change in currency rate 2020*	*Effect on profit before tax 2020*	*Change in currency rate 2019*	*Effect on profit before tax 2019*
USD	20%/(20%)	(2,185)/2,185	20%/(20%)	10,386/(10,386)
EUR	20%/(20%)	226/(226)	20%/(20%)	1,380/(1,380)

Prepayment risk

Prepayment risk is the risk that the Group will incur a financial loss because its customers and counterparties repay or request repayment earlier or later than expected.

The effect on profit before tax for one year assuming 10% of repayable financial instruments were to prepay at the beginning of the year, with all other variables held constant, is as follows:

	Decrease of net interest income
2020	9,743
2019	8,449

Interest rate risk

Interest rate risk arises from the possibility that changes in interest rates will affect future cash flows or the fair values of financial instruments. The following table demonstrates the sensitivity to a reasonable possible change in interest rates, with all other variables held constant, of the Group's statement of profit or loss.

The sensitivity of the statement of profit or loss is the effect of the assumed changes in interest rates on the net interest income for one year, based on the floating rate non–trading financial assets and financial liabilities held at 31 December.

(thousands of Georgian lari)

23. Risk management (continued)

Interest rate risk (continued)

Currency	***Increase/(decrease) in basis points 2020***	***Sensitivity of net interest income 2020***
GEL	100/(100)	1,832/(1,832)
EUR	100/(100)	278/(278)
USD	100/(100)	301/(301)

Currency	***Increase/(decrease) in basis points 2019***	***Sensitivity of net interest income 2019***
GEL	100/(100)	1,106/(1,106)
EUR	100/(100)	117/(117)
USD	100/(100)	170/(170)

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 Group cannot expect to eliminate all operational risks, but a control framework and monitoring and responding to potential risks could be effective tools to manage the risks. Controls include effective segregation of duties, access, authorisation and reconciliation procedures, staff education and assessment processes, including the use of internal audit.

24. Fair value measurements

Fair value hierarchy

The Group uses the following hierarchy for determining and disclosing the fair value of financial instruments by valuation technique:

- Level 1: quoted (unadjusted) prices in active markets for identical assets or liabilities;
- Level 2: techniques for which all inputs which have a significant effect on the recorded fair value are observable, either directly or indirectly; and
- Level 3: techniques which use inputs which have a significant effect on the recorded fair value that are not based on observable market data.

The following table shows an analysis of financial instruments recorded at fair value by level of the fair value hierarchy:

	Fair value measurement using			
At 31 December 2020	***Level 1***	***Level 2***	***Level 3***	***Total***
Assets for which fair values are disclosed				
Cash and cash equivalents	138,401	–	–	**138,401**
Amounts due from credit institutions	–	211,683	–	**211,683**
Loans to customers	–	–	1,130,021	**1,130,021**
Investment securities at amortized cost	18,434	41,886	–	**60,320**
Assets measured at fair value				
Investment securities at FVOCI – Equity Security	–	–	57	**57**
Investment securities at FVOCI -Debt Security			9,070	**9,070**

	Fair value measurement using			
At 31 December 2020	***Level 1***	***Level 2***	***Level 3***	***Total***
Liabilities for which fair values are disclosed				
Amounts due to credit institutions	–	9	–	**9**
Amounts due to customers	–	–	980,671	**980,671**
Lease liabilities	–	–	4,575	**4,575**
Subordinated debt	–	–	199,039	**199,039**

(thousands of Georgian lari)

24. Fair value measurements (continued)

Fair value hierarchy (continued)

	Fair value measurement using			
At 31 December 2019	***Level 1***	***Level 2***	***Level 3***	***Total***
Assets for which fair values are disclosed				
Cash and cash equivalents	147,598	–	–	**147,598**
Amounts due from credit institutions	–		168,905	**168,905**
Loans to customers	–	–	955,857	**955,857**
Investment securities at amortized cost	16,500	27,949	–	**44,449**
Assets measured at fair value				
Investment securities at FVOCI	–	–	57	**57**

	Fair value measurement using			
At 31 December 2019	***Level 1***	***Level 2***	***Level 3***	***Total***
Liabilities for which fair values are disclosed				
Amounts due to credit institutions	–	13	–	**13**
Amounts due to customers	–	–	790,269	**790,269**
Lease liabilities	–	–	5,680	**5,680**
Subordinated debt	–	–	206,500	**206,500**

The fair value of investment securities at FVOCI has changed by 242 during 2020 .

Fair value of financial assets and liabilities not carried at fair value

Set out below is a comparison by class of the carrying amounts and fair values of the Group's financial instruments that are not carried at fair value in the statement of financial position. The table does not include the fair values of non–financial assets and non–financial liabilities.

	Carrying value 2020	***Fair value 2020***	***Unrecognised gain/(loss) 2020***	***Carrying value 2019***	***Fair value 2019***	***Unrecognised gain/(loss) 2019***
Financial assets						
Cash and cash equivalents	138,401	138,401	–	147,598	147,598	–
Amounts due from credit institutions	211,683	211,683	–	168,905	168,905	–
Loans to customers	1,031,840	1,130,021	98,181	879,329	955,857	76,528
Investment securities	52,969	60,320	7,351	42,526	44,506	1,980
Other financial assets	4,375	4,375	–	6,529	6,529	–
Financial liabilities						
Amounts due to credit institutions	9	9	–	13	13	–
Amounts due to customers	976,190	980,671	(4,481)	778,274	790,269	(11,995)
Other financial liabilities	7,804	7,804	–	5,694	5,694	–
Lease liabilities	4,575	4,575	–	5,680	5,680	–
Subordinated debt	199,039	199,039	–	206,500	206,500	–
Total unrecognised change in fair value			**101,051**			**66,513**

(thousands of Georgian lari)

24. Fair value measurements (continued)

Valuation techniques and assumptions

The following describes the methodologies and assumptions used to determine fair values for those financial instruments which are not already recorded at fair value in the consolidated financial statements.

Assets for which fair value approximates carrying value

For financial assets and financial liabilities that are liquid or having a short–term maturity (less than three months) it is assumed that the carrying amounts approximate to their fair value. This assumption is also applied to demand deposits and savings accounts without a specific maturity.

Financial assets and financial liabilities carried at amortised cost

The fair value of loans to customers, customer deposits, amounts due from/(to) credit institutions and other financial assets and liabilities, investment securities, obligations under finance leases is estimated by discounting future cash flows using rates currently available for debt on similar terms, credit risk and remaining maturities.

25. Maturity analysis of assets and liabilities

The table below shows an analysis of assets and liabilities according to when they are expected to be recovered or settled. See Note 23 “Risk management” for the Group’s contractual undiscounted repayment obligations.

	2020			***2019***		
	Within one year	***More than one year***	***Total***	***Within one year***	***More than one year***	***Total***
Cash and cash equivalents	138,401	–	**138,401**	147,598	–	**147,598**
Amounts due from credit institutions	205,844	5,839	**211,683**	164,707	4,198	**168,905**
Loans to customers	435,270	596,570	**1,031,840**	401,536	477,793	**879,329**
Investment securities	19,239	43,099	**62,338**	21,997	20,529	**42,526**
Property and equipment	–	11,939	**11,939**	–	13,020	**13,020**
Right of use assets	–	4,184	**4,184**	–	5,436	**5,436**
Intangible assets	–	3,561	**3,561**	–	4,395	**4,395**
Deferred tax asset	–	83	**83**	–	333	**333**
Income tax asset	7,333	–	**7,333**	2,311	–	**2,311**
Other assets	10,939	61,169	**72,108**	12,014	61,020	**73,034**
Total	**817,026**	**726,444**	**1,543,470**	**750,163**	**586,724**	**1,336,887**
Amounts due to credit institutions	9	–	**9**	13	–	**13**
Amounts due to customers	576,061	400,129	**976,190**	508,223	270,051	**778,274**
Provisions	558	1,887	**2,445**	1,329	1,859	**3,188**
Current income tax liability	–	–	**–**	1,650	–	**1,650**
Deferred income tax liability	–	6,303	**6,303**	–	7,787	**7,787**
Lease liabilities	1,407	3,168	**4,575**	1,286	4,394	**5,680**
Other liabilities	16,226	–	**16,226**	10,364	–	**10,364**
Subordinated debt	21	199,018	**199,039**	125	206,375	**206,500**
Total	**594,282**	**610,505**	**1,204,787**	**522,990**	**490,466**	**1,013,456**
Net	**222,744**	**115,939**	**338,683**	**227,173**	**96,258**	**323,431**

(thousands of Georgian lari)

26. Related party disclosures

In accordance with IAS 24 *Related Party Disclosures*, parties are considered to be related if one party has the ability to control the other party or exercise significant influence over the other party in making financial or operational decisions. In considering each possible related party relationship, attention is directed to the substance of the relationship, not merely the legal form.

Related parties may enter into transactions which unrelated parties might not, and transactions between related parties may not be effected on the same terms, conditions and amounts as transactions between unrelated parties.

The outstanding balances of related party transactions are as follows:

	2020			
	The Parent	***Entities under common control***	***Other related parties***	***Key management personnel***
Loans to customers, gross	11,505	30,681	41,469	522
(Allowance for expected credit losses)	(100)	(246)	(319)	(2)
Amounts due to customers	(377)	(9,129)	(48,076)	(441)
Insurance and reinsurance receivables	–	–	151	–
Other assets	–	–	178	–
Subordinated debt	–	(199,039)	–	–
Commitments and guarantees issued	–	(4,762)	(249)	(1)
Right of use asset	–	3,643	444	–
Lease Liabilities	–	(3,975)	(503)	–

	2019			
	The Parent	***Entities under common control***	***Other related parties***	***Key management personnel***
Loans to customers, gross	8,183	–	62,793	546
(Allowance for expected credit losses)	(4)	–	(40)	(1)
Amounts due to credit institutions	–	–	–	–
Amounts due to customers	–	(12)	(63,716)	(452)
Insurance and reinsurance receivables	–	–	108	–
Other assets	–		(178)	
Subordinated debt	(20,092)	(186,408)	–	–
Commitments and guarantees issued	–	–	(2,649)	–

The income and expense arising from related party transactions are as follows:

	2020				*2019*			
	The Parent	***Entities under common control***	***Other related parties***	***Key management personnel***	***The Parent***	***Entities under common control***	***Other related parties***	***Key management personnel***
Interest income on loans to customers	162	3,068	5,145	53	376	–	6,483	46
Interest expense on amounts due to customers	–	(34)	(202)	(10)	–	–	(376)	(6)
Interest expense on subordinated debt	–	(12,287)		–	(2,122)	(9,834)	–	–
Charity and sponsorship	–	–	–	–	–	–	(3,585)	–
Gross written premiums on insurance contracts	–	–	(1,012)	–	–	–	(1,145)	–
Gross earned premiums	–	–	(1,049)	–	–	–	–	–
Insurance claims and loss adjustment expenses	–	–	(153)	–	–	–	(261)	–
Fee and commission income	12	219	221	2	3	–	280	2
Other income	–	–		–	–	–	15	–
Other expenses	–	–	(209)	–	(2)	–	(234)	–
Interest expense on lease liabilities	–	(428)	(56)	–	–	–	–	–

Compensation of key management personnel was comprised of the following:

	2020	*2019*
Salaries and other short–term benefits	1,449	1,556

Key management personnel as at 31 December 2020 and 2019 was 10 and includes members of the Group's Supervisory board, Board of Directors and other key executives of the Group.

(thousands of Georgian lari)

27. Capital adequacy

The Group maintains an actively managed capital base to cover risks inherent in the business. The adequacy of the Group's capital is monitored using, among other measures, the ratios established by the NBG in supervising the Group.

During the year ended 31 December 2020, the Bank and the Group complied in full with all its externally imposed capital requirements.

The primary objectives of the Group's capital management are to ensure that the Bank complies with externally imposed capital requirements set by the NBG and that Group maintains healthy capital ratios in order to support its business and maximize shareholders' value.

The Group manages its capital structure and makes adjustments to it in the light of changes in economic conditions and the risk characteristics of its activities. In order to maintain or adjust the capital structure the Group may adjust the amount of dividend payment to shareholders, return capital to shareholders or issue capital securities. No changes were made in the objectives, policies and processes from the previous years.

NBG capital adequacy ratio

Regulatory capital consists of Tier 1 capital, which comprises common shares, reserve fund and retained earnings excluding current year profit or loss less amount of property revaluation reserve transferred to authorised capital, and intangible assets. The other component of regulatory capital is Tier 2 capital, which includes profit or loss of current year, general reserves (not more than 1.25% of risk weighted assets) and subordinated long-term debt.

Starting from 30 June 2014 the NBG requires that all banks comply with Basel II regulations in their capital adequacy assessment. In December 2017, the NBG adopted amendments to the regulations introduced amendment relating to capital adequacy requirements, including amendments to the regulation on capital adequacy requirements for commercial banks, and introduced new requirements on the determination of the countercyclical buffer rate, on the identification of systematically important banks, on determining systemic buffer requirements and on additional capital buffer requirements for commercial banks within Pillar II.

As at 31 December 2020 the NBG requires the Bank to maintain a minimum Total egulatory capital adequacy ratio, Tier 1 capital adequacy ratio and Common equity tier 1 Capital Adequacy Ratio of 21.43%, 12.08% and 9.68%, respectively (December 2019: Minimum regulatory capital adequacy ratio, Tier 1 capital coefficient and common Tier 1 coefficient of 20.16%, 11.64% and 9.35%, respectively).

As at 31 December 2020 and 2019 capital adequacy ratios based on the Group's reports prepared in accordance with the NBG accounting rules and capital adequacy framework were as follows:

	31 December 2020	***31 December 2019***
Common Equity Tier 1 Capital	**171,026**	**199,035**
Additional Tier 1 Capital	55,702	20,074
Tier 1 Capital	**226,728**	**219,109**
Convertible subordinated debt	159,243	196,724
Special purpose funds	600	600
General Loan Loss Provisions (up to 1.25% of Risk–Weighted Assets)	14,012	10,783
Total Regulatory Capital	**400,583**	**427,216**
Risk Weighted Assets	**1,448,539**	**1,439,273**
Common Equity Tier 1 Capital Adequacy Ratio	11.81%	13.83%
Tier 1 Capital Adequacy Ratio	15.65%	15.22%
Total Regulatory Capital Adequacy Ratio	27.65%	29.68%

During the years ended 31 December 2020 and 2019 the Group complied in full with all of its externally imposed capital requirements.

(thousands of Georgian lari)

28. Events after the reporting period

On 19 April 2021 the Group repaid subordinated loan agreements with Inter Consulting Plus and Georgian Holding in the amount of USD 1,600 and USD 10,000, respectively.

On 19 April 2021 the Group amended subordinated loan agreements with Fin Service XXI and Inter Consulting Plus. The loan agreement in the amount of USD 30,000 with Fin Service XXI has been split into USD 10,000 with perpetual maturity, that satisfies the terms of Tier 1 capital, and USD 20,000 with extended maturity to 31 March 2028, that remains in Tier 2 capital requirements. The loan agreement in the amount of USD 7,000 with Inter Consulting Plus was extended to 17 October 2027 and it continues to satisfy the relevant terms and is included in Tier 2 regulatory capital.