

# JSC ProCredit Bank

International Financial Reporting Standards  
Consolidated and Separate Financial Statements and  
Independent Auditors' Report  
31 December 2019

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KPMG Georgia LLC  
GMT Plaza  
5th Floor, 4, Liberty square  
Tbilisi, Georgia 0105  
Telephone +995 322 93 5713  
Internet www.kpmg.ge

# Independent Auditors' Report

## To the Shareholders and Management of JSC ProCredit Bank

### Opinion

We have audited the consolidated and separate financial statements of JSC ProCredit Bank (the "Bank") and its subsidiary (The "Group"), which comprise the consolidated and the separate statements of financial position as at 31 December 2019, the consolidated and the separate statements of profit or loss and other comprehensive income, changes in equity and cash flows for the year then ended, and notes, comprising significant accounting policies and other explanatory information.

In our opinion, the accompanying consolidated and separate financial statements present fairly, in all material respects, the consolidated and separate financial position of the Group and Bank, respectively, as at 31 December 2019, and its consolidated and separate financial performance and its consolidated and separate cash flows for the year then ended in accordance with International Financial Reporting Standards (IFRS).

### 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 *Auditors' Responsibilities for the Audit of the Consolidated and Separate Financial Statements* section of our report. We are independent of the Group and the Bank in accordance with the International Code of Ethics for Professional Accountants (including International Independence Standards) together with the ethical requirements that are relevant to our audit of the consolidated and separate financial statements in Georgia, and we have fulfilled our other ethical responsibilities in accordance with these requirements and the International Code of Ethics. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

### Statement of Management Report

Management is responsible for the Management Report. Our opinion on the consolidated and separate financial statements does not cover the Management Report.

In connection with our audit of the consolidated and separate financial statements, our responsibility is to read the Management Report and, in doing so, consider whether the Management Report is materially inconsistent with the consolidated and separate financial statements or our knowledge obtained in the audit, or otherwise appears to be materially misstated.

We do not express any form of assurance conclusion on the Management Report. We have read the Management Report and based on the work performed, we conclude that the Management Report:

- is consistent with the consolidated and separate financial statements and does not contain material misstatement;
- contains all information that is required by and is compliant with the Law of Georgia on Accounting, Reporting and Auditing.



## **Responsibilities of Management and Those Charged with Governance for the Consolidated and the Separate Financial Statements**

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

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

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

## **Auditors' Responsibilities for the Audit of the Consolidated and the Separate Financial Statements**

Our objectives are to obtain reasonable assurance about whether the consolidated and separate financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditors' 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 and separate financial statements.

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

- Identify and assess the risks of material misstatement of the consolidated and separate 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 and the Bank's internal control.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management.
- Conclude on the appropriateness of management's use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Group's and the Bank's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditors' report to the related disclosures in the consolidated and separate 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 auditors' report. However, future events or conditions may cause the Group and the Bank to cease to continue as a going concern.



- Evaluate the overall presentation, structure and content of the consolidated and separate financial statements, including the disclosures, and whether the consolidated and separate 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 those charged with governance regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

The engagement partner on the audit resulting in this independent auditors' report is:

Karen Safaryan:

A handwritten signature in blue ink, appearing to read 'Karen Safaryan'. The signature is stylized with a large, sweeping initial 'K' and a long horizontal line extending to the right.

KPMG Georgia LLC  
15 May 2020

# PROCREDIT BANK GROUP

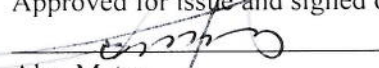
## Consolidated and Separate Statements of Financial Position

in '000 GEL

	Notes	Consolidated		Separate	
		31 December 2019	31 December 2018*	31 December 2019	31 December 2018*
<b>Assets</b>					
Cash and balances with the NBG	7	86,983	167,842	86,983	167,842
Mandatory reserve deposits with NBG		175,926	170,806	175,926	170,806
Investments in debt securities	9	21,917	29,767	21,917	29,767
Investments in equity securities	10	234	234	234	234
Investments in subsidiary	10	-	-	6,100	6,100
Due from banks	8	83,489	32,143	83,489	32,143
Loans and advances to customers	11	1,070,120	1,023,256	1,070,120	1,023,256
Current tax asset		1,553	-	1,553	-
Investment properties	12	8,592	9,875	5,247	5,401
Intangible assets	13	544	1,287	544	1,287
Property and equipment	14	50,998	55,591	50,998	55,591
Right-of-use assets	15	2,871	-	2,871	-
Other assets	16	8,521	8,108	8,201	7,831
<b>Total assets</b>		<b>1,511,748</b>	<b>1,498,909</b>	<b>1,514,183</b>	<b>1,500,258</b>
<b>Liabilities</b>					
Due to banks	17	70,407	71,608	70,407	71,608
Financial liabilities at fair value through profit or loss		1,258	224	1,258	224
Customer accounts	18	767,297	696,377	771,385	699,694
Other borrowed funds	19	406,707	457,234	406,707	457,234
Subordinated debt	22	45,314	82,978	45,314	82,978
Lease liabilities	15	2,938	-	2,938	-
Current tax liability		-	1,775	-	1,775
Other liabilities	20	1,439	1,322	1,173	1,197
Other provisions		430	813	430	813
Deferred tax liability	21	1,604	639	1,604	639
<b>Total liabilities</b>		<b>1,297,394</b>	<b>1,312,970</b>	<b>1,301,216</b>	<b>1,316,162</b>
<b>Equity</b>					
Share capital	23	100,352	88,915	100,352	88,915
Share premium	23	51,324	36,388	51,324	36,388
Retained earnings		62,678	60,636	61,291	58,793
<b>Total equity</b>		<b>214,354</b>	<b>185,939</b>	<b>212,967</b>	<b>184,096</b>
<b>Total equity and liabilities</b>		<b>1,511,748</b>	<b>1,498,909</b>	<b>1,514,183</b>	<b>1,500,258</b>

\*The Group and Bank initially applied IFRS 16 at 1 January 2019, using the modified retrospective approach. Under this approach, comparative information is not restated and the cumulative effect of initially applying IFRS 16 is recognised in retained earnings at the date of initial application.

Approved for issue and signed on behalf of the Board of Directors on 15 May 2020.

  
Alex Matua  
General Director

  
Nana Chikvaizde  
Chief Accountant

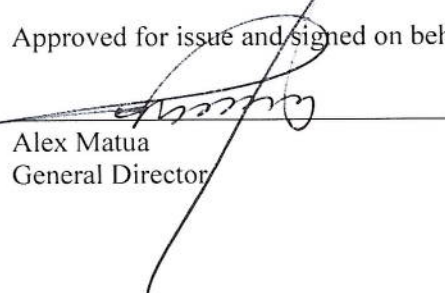
# PROCREDIT BANK GROUP

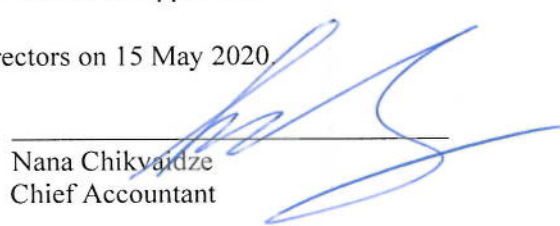
## Consolidated and Separate Statements of Profit or Loss and Other Comprehensive Income

in '000 GEL	Notes	Consolidated		Separate	
		2019	2018*	2019	2018*
Interest income calculated using effective interest rate method		90,882	86,339	90,882	86,339
Interest expense		(42,710)	(34,732)	(42,710)	(34,732)
<b>Net interest income</b>	<b>25</b>	<b>48,172</b>	<b>51,607</b>	<b>48,172</b>	<b>51,607</b>
Reversal of impairment losses on loans	11	2,960	311	2,960	311
<b>Net interest income after provision for loan impairment</b>		<b>51,132</b>	<b>51,918</b>	<b>51,132</b>	<b>51,918</b>
Fee and commission income	26	12,793	11,586	12,793	11,586
Fee and commission expenses	26	(7,835)	(6,057)	(7,835)	(6,057)
Net gain from trading in foreign currency		16,579	9,255	16,579	9,255
Net foreign exchange translation gain		(3,553)	(926)	(3,553)	(918)
Personnel expenses		(13,371)	(12,320)	(13,294)	(12,244)
Other administrative expenses	27	(24,577)	(22,991)	(24,510)	(22,919)
Other operating income	28(a)	5,229	3,613	4,245	2,499
Other operating expense	28(b)	(3,261)	(3,021)	(1,965)	(2,891)
<b>Profit before income tax</b>		<b>33,136</b>	<b>31,057</b>	<b>33,592</b>	<b>30,229</b>
Income tax expense	21	(4,721)	(4,659)	(4,721)	(4,849)
<b>Profit and total comprehensive income for the year</b>		<b>28,415</b>	<b>26,398</b>	<b>28,871</b>	<b>25,380</b>

\*The Group and Bank initially applied IFRS 16 at 1 January 2019, using the modified retrospective approach. Under this approach, comparative information is not restated and the cumulative effect of initially applying IFRS 16 is recognised in retained earnings at the date of initial application.

Approved for issue and signed on behalf of the Board of Directors on 15 May 2020.

  
 Alex Matua  
 General Director

  
 Nana Chikvaidze  
 Chief Accountant



# PROCREDIT BANK GROUP

## Consolidated and Separate Statements of Changes in Equity

in '000 GEL

	Notes	Consolidated				Separate			
		Share capital	Share premium	Retained earnings	Total	Share capital	Share premium	Retained earnings	Total
<b>Balance at 1 January 2018*</b>		88,915	36,388	72,799	198,102	88,915	36,388	71,974	197,277
Change on initial application of IFRS 9		-	-	(8,238)	(8,238)	-	-	(8,238)	(8,238)
<b>Restated balance at 1 January 2018</b>		88,915	36,388	64,561	189,864	88,915	36,388	63,736	189,039
<b>Total comprehensive income</b>									
Profit for the year		-	-	26,398	26,398	-	-	25,380	25,380
<b>Total comprehensive income for the year</b>		-	-	26,398	26,398	-	-	25,380	25,380
<b>Transactions with owners, recorded directly in equity</b>									
Dividends declared	23	-	-	(30,323)	(30,323)	-	-	(30,323)	(30,323)
<b>Transactions with owners, recorded directly in equity</b>		-	-	(30,323)	(30,323)	-	-	(30,323)	(30,323)
<b>Balance at 31 December 2018</b>		88,915	36,388	60,636	185,939	88,915	36,388	58,793	184,096
<b>Balance at 1 January 2019</b>		88,915	36,388	60,636	185,939	88,915	36,388	58,793	184,096
<b>Total comprehensive income</b>									
Profit for the year		-	-	28,415	28,415	-	-	28,871	28,871
<b>Total comprehensive income for the year</b>		-	-	28,415	28,415	-	-	28,871	28,871
<b>Transactions with owners, recorded directly in equity</b>									
Dividends declared	23	-	-	(26,373)	(26,373)	-	-	(26,373)	(26,373)
Shares issued	23	11,437	14,936	-	26,373	11,437	14,936	-	26,373
<b>Transactions with owners, recorded directly in equity</b>		11,437	14,936	(26,373)	-	11,437	14,936	(26,373)	-
<b>Balance at 31 December 2019</b>		100,352	51,324	62,678	214,354	100,352	51,324	61,291	212,967

\*The Group and Bank initially applied IFRS 16 at 1 January 2019, using the modified retrospective approach. Under this approach, comparative information is not restated and the cumulative effect of initially applying IFRS 16 is recognised in retained earnings at the date of initial application.

Approved for issue and signed on behalf of the Board of Directors on 15 May 2020.

Alex Mattia  
General Director

Nana Chikvaidze  
Chief Accountant



# PROCREDIT BANK GROUP

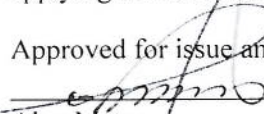
## Consolidated and Separate Statements of Cash Flows

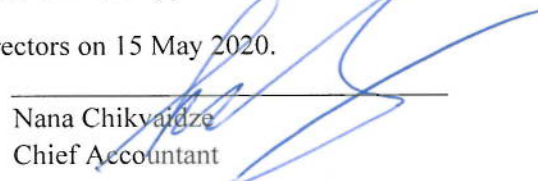
in '000 GEL.

	Notes	Consolidated		Separate	
		2019	2018*	2019	2018*
<b>Profit before income tax</b>		<b>33,136</b>	<b>31,057</b>	<b>33,592</b>	<b>30,229</b>
Accrual/(release) of provision for loan impairment	11	(2,960)	(311)	(2,960)	(311)
Depreciation and amortization		5,837	4,805	5,812	4,775
Loss on write off of repossessed property		1,627	-	780	-
Net foreign exchange translation loss		3,553	926	3,553	918
Accrual/reversal of other provisions		38	164	(383)	164
(Gain)/loss from disposal of property and equipment		(28)	4,043	-	4,043
Net interest income		(48,172)	(51,607)	(48,172)	(51,607)
<b>Operating cash flows before changes in operating assets and liabilities</b>		<b>(6,969)</b>	<b>(10,923)</b>	<b>(7,778)</b>	<b>(11,789)</b>
<i>Net change in assets and liabilities from operating activities after non-cash items:</i>					
Mandatory reserve deposit with the NBG		5,667	(40,415)	5,667	(40,415)
Loans and advances to customers		(1,665)	(16,298)	(1,665)	(16,298)
Other assets		(932)	(1,053)	(335)	(1,818)
Due to banks		(4,780)	22,969	(4,780)	22,969
Financial liabilities at fair value through profit or loss		1,035	562	1,035	562
Customer accounts		36,580	54,379	37,322	55,633
Other liabilities		-	(2,989)	(142)	(2,957)
<b>Total net change in assets and liabilities from operating activities after non-cash items</b>		<b>35,905</b>	<b>17,155</b>	<b>37,103</b>	<b>17,676</b>
Interest received		95,649	85,788	95,649	86,254
Interest paid		(42,066)	(34,678)	(42,066)	(34,678)
Income tax paid		(7,084)	(1,650)	(7,083)	(1,801)
<b>Net cash from operating activities</b>		<b>75,435</b>	<b>55,692</b>	<b>75,824</b>	<b>55,662</b>
Purchase of property and equipment and intangible assets		(2,167)	(2,065)	(2,167)	(1,239)
Purchase of investment properties		-	(609)	-	(585)
Proceeds from sale of property and equipment and investment properties		2,157	1,611	1,769	785
Purchase of investments in debt securities	9	(72,700)	(87,227)	(72,700)	(87,227)
Proceeds from sale of investments in debt securities	9	80,710	62,609	80,710	62,609
<b>Cash flows from/(used in) investing activities</b>		<b>8,000</b>	<b>(25,681)</b>	<b>7,612</b>	<b>(25,657)</b>
Dividends paid	23	(26,373)	(30,323)	(26,373)	(30,323)
Shares issued		26,373	-	26,373	-
Payment of lease liabilities		(711)	-	(711)	-
Proceeds from other borrowed funds		169,416	139,789	169,415	139,789
Repayments of other borrowed funds		(245,018)	(89,396)	(245,018)	(89,396)
Proceeds of subordinated debts		-	15,218	-	15,218
Payments of subordinated debts		(43,229)	-	(43,229)	-
<b>Cash flows (used in)/from financing activities</b>		<b>(119,542)</b>	<b>35,288</b>	<b>(119,543)</b>	<b>35,288</b>
<b>Net (decrease)/increase in cash and cash equivalents</b>		<b>(36,107)</b>	<b>65,299</b>	<b>(36,107)</b>	<b>65,293</b>
Cash and cash equivalents at the beginning of the year		200,203	156,312	200,203	156,310
Effects of exchange rate changes		6,379	(21,408)	6,379	(21,400)
<b>Cash and cash equivalents at the end of the year</b>	<b>7</b>	<b>170,475</b>	<b>200,203</b>	<b>170,475</b>	<b>200,203</b>

\*The Group and Bank initially applied IFRS 16 at 1 January 2019, using the modified retrospective approach. Under this approach, comparative information is not restated and the cumulative effect of initially applying IFRS 16 is recognised in retained earnings at the date of initial application.

Approved for issue and signed on behalf of the Board of Directors on 15 May 2020.

  
Alex Matua  
General Director

  
Nana Chikvaidze  
Chief Accountant

# PROCREDIT BANK GROUP

## Notes to the Financial Statements - 31 December 2019

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### 1. ORGANIZATION AND OPERATIONS

These consolidated and separate financial statements (hereafter the “Financial Statements”) include the financial statements of JSC ProCredit Bank (the Bank) and its subsidiary (together referred to as the Group). The Bank and its subsidiary are joint stock and limited liability companies, respectively, as it is defined under the Law of Georgia on Entrepreneurs and are incorporated and domiciled in Georgia. The Bank was registered by Vake District Court on 04 January 1999, registration number is 204851197.

JSC ProCredit Bank is a development-oriented bank specialized for small and medium enterprises operating on the territory of Georgia. For supervisory purposes the Bank has the general banking licence number 233 issued on 13 May 1999 and is therefore supervised by the National Bank of Georgia (the NBG).

The address of the Bank’s registered office is: 21 Al. Kazbegi Avenue, 0160, Tbilisi, Georgia. The Bank’s head office is located in Tbilisi. The Bank serves its clients through 4 branches, 5 service points and 12 self-service areas in Tbilisi, Kutaisi, Batumi and Zugdidi.

The Bank has one wholly-owned subsidiary, LLC ProCredit Properties, which was formed as a limited liability company under Georgian law on 23 July 2007 with the principal activity of holding and managing movable and immovable properties acquired through auctions resulting from defaults of the Bank’s customers.

The Bank is wholly owned by its immediate and ultimate parent company ProCredit Holding AG & Co. KGaA (Parent). As of 31 December 2019 and 31 December 2018, the following shareholders directly owned more than 5% of the total outstanding shares of the Parent. Other shareholders individually owned less than 5% of the outstanding shares. As at 31 December 2019 and 31 December 2018 the Group and Bank had no ultimate controlling party.

	% of ownership interest held as of	
	31 December	
	2019	2018
Zeitinger Invest GmbH	17	17
KfW - Kreditanstalt für Wiederaufbau	13.2	13.2
DOEN Foundation	12.5	12.5
IFC - International Finance Corporation	10	10
TIAA-CREF - Teachers Insurance and Annuity Association	8.6	8.6
Other	38.7	38.7
<b>Total</b>	<b>100</b>	<b>100</b>

Refer to Note 32 for related party transactions.

### 2. BUSINESS ENVIRONMENT

The Group’s and Bank’s operations are located in Georgia. Consequently, the Group and Bank are exposed to the economic and financial markets of Georgia, which display characteristics of an emerging market. The legal, tax and regulatory frameworks continue development, but are subject to varying interpretations and frequent changes which together with other legal and fiscal impediments contribute to the challenges faced by entities operating in Georgia. The consolidated and separate financial statements reflect management’s assessment of the impact of the Georgian business environment on the operations and the financial position of the Group and Bank. The future business environment may differ from management’s assessment. For COVID-19 impact please refer to Note 33.

### **3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

#### **Basis of preparation**

These Financial Statements have been prepared in accordance with International Financial Reporting Standards (“IFRSs”).

This is the first set of the Group’s/Bank’s annual Financial Statements in which IFRS 16 Leases has been applied. The related changes to significant accounting policies are described in Note 5.

The Financial Statements are prepared on the historical cost basis except that financial instruments at fair value through profit or loss (FVTPL). Group and Bank accounts for derivative (foreign currency contracts) as fair value through profit or loss and investment in equity shares of as fair value through other comprehensive income.

#### **Basis of consolidation**

Subsidiaries are those investees, including structured entities, that the Group controls because the Group (i) has power to direct relevant activities of the investees that significantly affect their returns, (ii) has exposure, or rights, to variable returns from its involvement with the investees, and (iii) has the ability to use its power over the investees to affect the amount of investor’s returns. The existence and effect of substantive rights, including substantive potential voting rights, are considered when assessing whether the Group has power over another entity. For a right to be substantive, the holder must have practical ability to exercise that right when decisions about the direction of the relevant activities of the investee need to be made. The Group may have power over an investee even when it holds less than majority of voting power in an investee. In such a case, the Group assesses the size of its voting rights relative to the size and dispersion of holdings of the other vote holders to determine if it has de-facto power over the investee. Protective rights of other investors, such as those that relate to fundamental changes of investee’s activities or apply only in exceptional circumstances, do not prevent the Group from controlling an investee. Subsidiaries are consolidated from the date on which control is transferred to the Group, and are deconsolidated from the date on which control ceases.

Intercompany transactions, balances and unrealised gains on transactions between group companies are eliminated; unrealised losses are also eliminated unless the cost cannot be recovered. The Bank and all of its subsidiaries use uniform accounting policies consistent with the Group’s and Bank’s policies.

#### **Subsidiaries**

Subsidiaries are investees controlled by the Group and Bank. The Group and Bank controls an investee when it is exposed to, 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. In particular, the Group consolidates investees that it controls on the basis of de facto circumstances, including cases when protective rights arising from collateral agreements on lending transactions become significant. The financial statements of subsidiaries are included in the consolidated financial statements from the date that control commences until the date that control ceases.

The Bank accounts for its investments in subsidiaries at cost and consistently applies same accounting policies for each category of investments. Investments in subsidiaries is measured at acquisition cost less impairment losses.

The Bank accounts for investment in subsidiaries from the date that control effectively commences until the date that control effectively ceases.

**Financial instruments - key measurement terms**

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 best evidence of fair value is price in an active market. An active market is one in which transactions for the asset or liability take place with sufficient frequency and volume to provide pricing information on an ongoing basis. Fair value of financial instruments traded in an active market is measured as the product of the quoted price for the individual asset or liability and the quantity held by the entity. This is the case even if a market's normal daily trading volume is not sufficient to absorb the quantity held and placing orders to sell the position in a single transaction might affect the quoted price.

A portfolio of financial derivatives or other financial assets and liabilities that are not traded in an active market is measured at the fair value of a group of financial assets and financial liabilities on the basis of the price that would be received to sell a net long position (i.e. an asset) for a particular risk exposure or paid to transfer a net short position (i.e. a liability) for a particular risk exposure in an orderly transaction between market participants at the measurement date.

Valuation techniques such as discounted cash flow models or models based on recent arm's length transactions or consideration of financial data of the investees, are used to measure fair value of certain financial instruments for which external market pricing information is not available. Fair value measurements are analysed by level in the fair value hierarchy as follows: (i) level one are measurements at quoted prices (unadjusted) in active markets for identical assets or liabilities, (ii) level two measurements are valuations techniques with all material inputs observable for the asset or liability, either directly (that is, as prices) or indirectly (that is, derived from prices), and (iii) level three measurements are valuations not based on solely observable market data (that is, the measurement requires significant unobservable inputs).

Transaction costs are incremental costs that are directly attributable to the acquisition, issue or disposal of a financial instrument. An incremental cost is one that would not have been incurred if the transaction had not taken place. Transaction costs include fees and commissions paid to agents (including employees acting as selling agents), advisors, brokers and dealers, levies by regulatory agencies and securities exchanges, and transfer taxes and duties. Transaction costs do not include debt premiums or discounts, financing costs or internal administrative or holding costs.

Amortised cost ("AC") is the amount at which the financial instrument was recognised at initial recognition less any principal repayments, plus accrued interest, and for financial assets less any allowance for expected credit losses. Accrued interest includes amortisation of transaction costs deferred at initial recognition and of any premium or discount to maturity amount using the effective interest method. Accrued interest income and accrued interest expense, including both accrued coupon and amortised discount or premium (including fees deferred at origination, if any), are not presented separately and are included in the carrying values of related items in the statement of financial position.

The effective interest method is a method of allocating interest income or interest expense over the relevant period, so as to achieve a constant periodic rate of interest (effective interest rate) on the carrying amount. The effective interest rate is the rate that exactly discounts estimated future cash payments or receipts (excluding future credit losses) through the expected life of the financial instrument or a shorter period, if appropriate, to the gross carrying amount of the financial instrument.

The effective interest rate discounts cash flows of variable interest instruments to the next interest repricing date, except for the premium or discount, which reflects the credit spread over the floating rate specified in the instrument, or other variables that are not reset to market rates. Such premiums or discounts are amortised over the whole expected life of the instrument. The present value calculation includes all fees paid or received between parties to the contract that are an integral part of the effective interest rate. For assets that are purchased or originated credit impaired ("POCI") at initial recognition, the effective interest rate is adjusted for credit risk, i.e. it is calculated based on the expected cash flows on initial recognition instead of contractual payments.

**Financial instruments – initial recognition**

Trade receivables and debt securities issued are initially recognised when they are originated. All other financial assets and financial liabilities are initially recognised when the Group and/or Bank becomes a party to the contractual provisions of the instrument.

A financial asset (unless it is a trade receivable without a significant financing component) or financial liability is initially measured at fair value plus, for an item not at FVTPL, transaction costs that are directly attributable to its acquisition or issue. A trade receivable without a significant financing component is initially measured at the transaction price.

All purchases and sales of financial assets that require delivery within the time frame established by regulation or market convention (“regular way” purchases and sales) are recorded at trade date, which is the date on which the Group and Bank commits to deliver a financial asset. All other purchases are recognised when the entity becomes a party to the contractual provisions of the instrument.

**Financial assets – classification and subsequent measurement – measurement categories**

The Group and Bank classifies financial assets in the following measurement categories: Fair value through profit or loss (“FVTPL”), fair value through other comprehensive income (“FVOCI”) and amortised cost (“AC”). The classification and subsequent measurement of debt financial assets depends on: (i) the Group’s and Bank’s business model for managing the related assets portfolio and (ii) the cash flow characteristics of the asset.

**Financial assets – classification and subsequent measurement – business model**

The business model reflects how the Group and Bank manages the assets in order to generate cash flows – whether the Group’s and Bank’s objective is: (i) solely to collect the contractual cash flows from the assets (“hold to collect contractual cash flows”), or (ii) to collect both the contractual cash flows and the cash flows arising from the sale of assets (“hold to collect contractual cash flows and sell”) or, if neither of (i) and (ii) is applicable, the financial assets are classified as part of “other ” business model and measured at FVTPL.

Business model is determined for a group of assets (on a portfolio level) based on all relevant evidence about the activities that the Group and Bank undertakes to achieve the objective set out for the portfolio available at the date of the assessment. Factors considered by the Group and Bank in determining the business model include the purpose and composition of a portfolio, past experience on how the cash flows for the respective assets were collected, and how risks are assessed and managed. Refer to Note 4 for critical judgements applied by the Group and Bank in determining the business models for its financial assets.

On initial recognition of an equity investment that is not held for trading, the Group/Bank may irrevocably elect to present subsequent changes in the investment’s fair value in OCI. This election is made on an investment-by-investment basis. Group/Bank has elected to account as such Investments in equity securities.

**Financial assets – classification and subsequent measurement – cash flow characteristics**

Where the business model is to hold assets to collect contractual cash flows or to hold contractual cash flows and sell, the Group and Bank assesses whether the cash flows represent solely payments of principal and interest (“SPPI”). Financial assets with embedded derivatives are considered in their entirety when determining whether their cash flows are consistent with the SPPI feature. In making this assessment, the Group and Bank considers whether the contractual cash flows are consistent with a basic lending arrangement, i.e. interest includes only consideration for credit risk, time value of money, other basic lending risks and profit margin.

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Where the contractual terms introduce exposure to risk or volatility that is inconsistent with a basic lending arrangement, the financial asset is classified and measured at FVTPL. The SPPI assessment is performed on initial recognition of an asset and it is not subsequently reassessed. Refer to Note 4 for critical judgements applied by the Group and Bank in performing the SPPI test for its financial assets.

#### **Financial assets – reclassification**

Financial instruments are reclassified only when the business model for managing the portfolio as a whole changes. The reclassification has a prospective effect and takes place from the beginning of the first reporting period that follows after the change in the business model.

#### **Expected Credit Losses – ECL**

The Group and Bank assesses, on a forward-looking basis, the ECL for debt instruments measured at AC and FVOCI and for the exposures arising from loan commitments and financial guarantee contracts. The Group and Bank measures ECL and recognises credit loss allowance at each reporting date. The measurement of ECL reflects: (i) an unbiased and probability weighted amount that is determined by evaluating a range of possible outcomes, (ii) time value of money and (iii) all reasonable and supportable information that is available without undue cost and effort at the end of each reporting period about past events, current conditions and forecasts of future conditions.

Debt instruments measured at AC are presented in the consolidated statement of financial position net of the allowance for ECL. For loan commitments and financial guarantees, a separate provision for ECL is recognised as a liability in the consolidated and separate statement of financial position. For debt instruments at FVOCI, changes in amortised cost, net of allowance for ECL, are recognised in profit or loss and other changes in carrying value are recognised in OCI as gains less losses on debt instruments at FVOCI.

The Group and Bank applies a three stage model for impairment, based on changes in credit quality since initial recognition. A financial instrument that is not credit-impaired on initial recognition is classified in Stage 1. Financial assets in Stage 1 have their ECL measured at an amount equal to the portion of lifetime ECL that results from default events possible within the next 12 months or until contractual maturity, if shorter (“12 Months ECL”). If the Group and Bank identifies a significant increase in credit risk (“SICR”) since initial recognition, the asset is transferred to Stage 2 and its ECL is measured based on ECL on a lifetime basis, that is, up until contractual maturity but considering expected prepayments, if any (“Lifetime ECL”). Refer to Note 29 for a description of how the Group and Bank determines when a SICR has occurred. If the Group and Bank determines that a financial asset is credit-impaired, the asset is transferred to Stage 3 and its ECL is measured as a Lifetime ECL. The Group’s and Bank’s definition of credit impaired assets and definition of default is explained in Note 29. For financial assets that are purchased or originated credit-impaired (“POCI Assets”), the ECL is always measured as a Lifetime ECL. Note 29 provides information about inputs, assumptions and estimation techniques used in measuring ECL, including an explanation of how the Group and Bank incorporates forward-looking information in the ECL models.

As an exception, for certain financial instruments, such as credit cards, that may include both a loan and an undrawn commitment component, the Group and Bank measures expected credit losses over the period that the Group and Bank is exposed to credit risk, that is, until the expected credit losses would be mitigated by credit risk management actions, even if that period extends beyond the maximum contractual period. This is because contractual ability to demand repayment and cancel the undrawn commitment does not limit the exposure to credit losses to such contractual notice period.

#### **Financial assets – write-off**

Financial assets are written-off, in whole or in part, when the Group and Bank exhausted all practical recovery efforts and has concluded that there is no reasonable expectation of recovery. The write-off represents a derecognition event. The Group and Bank may write-off financial assets that are still subject to enforcement activity when the Group and Bank seeks to recover amounts that are contractually due, however, there is no reasonable expectation of recovery.



### **Financial assets – derecognition**

The Group and Bank derecognises financial assets when (a) the assets are redeemed or the rights to cash flows from the assets otherwise expired or (b) the Group and Bank has transferred the rights to the cash flows from the financial assets or entered into a qualifying pass-through arrangement while (i) also transferring substantially all risks and rewards of ownership of the assets or (ii) neither transferring nor retaining substantially all risks and rewards of ownership, but not retaining control. Control is retained if the counterparty does not have the practical ability to sell the asset in its entirety to an unrelated third party without needing to impose restrictions on the sale.

### **Financial assets – modification**

The Group and Bank sometimes renegotiates or otherwise modifies the contractual terms of the financial assets. The Group and Bank assesses whether the modification of contractual cash flows is substantial considering, among other, the following factors: any new contractual terms that substantially affect the risk profile of the asset, significant change in interest rate, change in the currency denomination, new collateral or credit enhancement that significantly affects the credit risk associated with the asset or a significant extension of a loan when the borrower is not in financial difficulties.

If the modified terms are substantially different, the rights to cash flows from the original asset expire and the Group and Bank derecognises the original financial asset and recognises a new asset at its fair value. The date of renegotiation is considered to be the date of initial recognition for subsequent impairment calculation purposes, including determining whether a SICR has occurred. The Group and Bank also assesses whether the new loan or debt instrument meets the SPPI criterion. Any difference between the carrying amount of the original asset derecognised and fair value of the new substantially modified asset is recognised in profit or loss, unless the substance of the difference is attributed to a capital transaction with owners.

In a situation where the renegotiation was driven by financial difficulties of the counterparty and inability to make the originally agreed payments, the Group and Bank compares the original and revised expected cash flows to assets whether the risks and rewards of the asset are substantially different as a result of the contractual modification. If the risks and rewards do not change, the modified asset is not substantially different from the original asset and the modification does not result in derecognition. The Group and Bank recalculates the gross carrying amount by discounting the modified contractual cash flows by the original effective interest rate (or credit-adjusted effective interest rate for POCI financial assets), and recognises a modification gain or loss in profit or loss.

### **Financial liabilities – measurement categories**

Financial liabilities are classified as subsequently measured at AC, except for (i) financial liabilities at FVTPL: this classification is applied to derivatives, financial liabilities held for trading (e.g. short positions in securities), contingent consideration recognised by an acquirer in a business combination and other financial liabilities designated as such at initial recognition and (ii) financial guarantee contracts and loan commitments.

### **Financial liabilities – derecognition**

Financial liabilities are derecognised when they are extinguished (i.e. when the obligation specified in the contract is discharged, cancelled or expires).

An exchange between the Group and Bank and its original lenders of debt instruments with substantially different terms, as well as substantial modifications of the terms and conditions of existing financial liabilities, are accounted for as an extinguishment of the original financial liability and the recognition of a new financial liability. The terms are substantially different if the discounted present value of the cash flows under the new terms, including any fees paid net of any fees received and discounted using the original effective interest rate,

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is at least 10% different from the discounted present value of the remaining cash flows of the original financial liability. If an exchange of debt instruments or modification of terms is accounted for as an extinguishment, any costs or fees incurred are recognised as part of the gain or loss on the extinguishment. If the exchange or modification is not accounted for as an extinguishment, any costs or fees incurred adjust the carrying amount of the liability and are amortised over the remaining term of the modified liability.

Modifications of liabilities that do not result in extinguishment are accounted for as a change in estimate using a cumulative catch up method, with any gain or loss recognised in profit or loss, unless the economic substance of the difference in carrying values is attributed to a capital transaction with owners.

#### **Financial instruments – offsetting**

Financial assets and liabilities are offset and the net amount 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 realise the asset and settle the liability simultaneously.

#### **Foreign currency translation**

##### ***(a) Functional and presentation currency***

The national currency of Georgia is the Georgian lari (GEL), which is the Bank's and its subsidiary's functional currency and the currency in which these Financial Statements are presented. Management has determined the functional currency to be the GEL as it reflects the economic substance of the underlying events and circumstances of the Group and Bank. The GEL is not convertible outside Georgia.

All financial information presented in GEL has been rounded to the nearest thousand except when otherwise indicated.

##### ***(b) Transactions and balances***

Foreign currency transactions are translated into the functional currency using the exchange rates prevailing at the dates of the transactions. Foreign exchange gains and losses resulting from the settlement of such transactions and from the translation at year-end exchange rates of monetary assets and liabilities denominated in foreign currencies are recognised in the profit or loss.

Monetary items denominated in foreign currency are translated with the closing rate as at the reporting date. The foreign currency gain or loss on monetary items is the difference between amortised cost in the functional currency at the beginning of the period, adjusted for effective interest and payments during the period, and the amortised cost in foreign currency translated at the exchange rate at the end of the reporting period.

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.

Non-monetary items measured at historical cost denominated in foreign currency are translated with the exchange rate as of the date of initial recognition.

Foreign currency differences arising on retranslation are recognized in profit or loss. However, foreign currency differences arising from the translation of the following items are recognised in OCI:

- an investment in equity securities designated as at FVOCI (except on impairment, in which case foreign currency differences that have been recognised in OCI are reclassified to profit or loss).

The reporting exchange rates and average rates for the period used in the statement of financial position and the statement of profit or loss and other comprehensive income are listed in Note 29.

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#### **Cash and cash equivalents**

Cash and cash equivalents are items which are readily convertible to known amounts of cash and are subject to an insignificant risk of changes in value. Cash and cash equivalents include cash on hand, amounts due from the National Bank of Georgia (NBG), excluding mandatory reserves, and all interbank placements and interbank receivables with original maturities of less than three months. Funds restricted for a period of more than three months on origination are excluded from cash and cash equivalents. Cash and cash equivalents are carried at AC because: (i) they are held for collection of contractual cash flows and those cash flows represent SPPI, and (ii) they are not designated at FVTPL.

The payments or receipts presented in the statement of cash flows represent the Group's and Bank's transfers of cash and cash equivalents, including amounts charged or credited to current accounts of the Group and Bank's counterparties held with the Group and Bank, such as loan interest income or principal collected by charging the customer's current account or interest payments or disbursement of loans credited to the customer's current account, which represent cash or cash equivalent from the customer's perspective.

#### **Mandatory reserve deposits with the National Bank of Georgia**

Mandatory reserve deposits with the NBG are carried at AC and are not available to finance the Group's and Bank's day to day operations. Hence they are not considered as part of cash and cash equivalents for the purposes of the consolidated statement of cash flows.

#### **Due from banks**

Amounts due from banks include placements with the banks with original maturities of more than three months. Amounts due from banks are recorded when the Group and Bank advances money to counterparty banks. Amounts due from banks are carried at AC when: (i) they are held for the purposes of collecting contractual cash flows and those cash flows represent SPPI, and (ii) they are not designated at FVTPL. Otherwise they are carried at Fair value ("FV").

#### **Repossessed collateral**

Repossessed collateral represents financial and non-financial assets acquired by the Group and Bank in settlement of overdue loans. The Group and Bank recognises repossessed assets in the statement of financial position when it has the full and final settlement rights to the collateral, and when it is entitled to retain any excess proceeds from the realisation of the collateral.

At initial recognition repossessed assets are measured at the lower of the cost and the fair value less costs to sell and are included in premises and equipment, other financial assets or inventories within other assets depending on their nature and the Group's and Bank's intention with respect to recovery of these assets. They are subsequently re-measured and accounted for in accordance with the accounting policies for these categories of assets.

The carrying amount of the repossessed assets is measured based on the carrying value of the defaulted loan, including expenditure incurred in the process of collateral foreclosure. Fair value less costs to sell is the estimated selling price of the collateral in the ordinary course of business, less the related selling costs.

#### **Investments in debt securities**

Based on the business model and the cash flow characteristics, the Group and Bank classifies investments in debt securities as carried at AC, these are initially measured at fair value plus incremental transaction costs, and subsequently at their amortised cost using the effective interest method. Debt securities are carried at AC if they are held for collection of contractual cash flows and where those cash flows represent SPPI, and if they are not voluntarily designated at FVTPL in order to significantly reduce an accounting mismatch.

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The Group and Bank considers investment securities to have low credit risk. If a debt security had low credit risk at the date of initial application of IFRS 9, then the Group has assumed that credit risk on the asset had not increased significantly since its initial recognition.

The Group and Bank measures loss allowances at an amount equal to 12-month ECL. ECL for exposures in Stage 1 is calculated by multiplying the 12-month PD by LGD and EAD.

For PD purposes, counterparties (financial institutions, sovereigns) and countries, rating information provided by Fitch is used. As empirical default rates are not available for all rating classes, PDs for classes without empirical information are linearly interpolated from the next available empirical rates above or below the considered class. For Financial Institutions, country-specific LGDs published by Fitch are used.

#### Release of loss allowances

In the event of decrease of credit risk, the already recognised loss allowance is reduced accordingly.

#### Write-offs, recoveries and direct write-offs

When a loan is uncollectible, it is written off against the related loss allowance set aside. Such write-offs occur after all the necessary procedures have been completed and the amount of the loss has been determined. Subsequent recoveries of amounts previously written off are recognised in the Statement of Profit or Loss under “Loss allowances”. Uncollectible loans for which no loss allowances have been set aside in full are recognised as direct write-offs.

#### Non-substantial modification

Non-substantial modification is a modification event that does not result in derecognition of the original asset. The effect is recognised through profit or loss as a modification gain or modification loss. The modification gain or loss is calculated as the difference between the original gross carrying amount and the present value of the modified contractual cash flows discounted at the original effective interest rate.

### **Property and equipment**

All property and equipment are stated at historical cost less accumulated depreciation and impairment losses. Historical cost includes expenditure that is directly attributable to the acquisition of the items. Component parts of an asset are recognised separately if they have different useful lives or provide benefits to the enterprise in a different pattern.

Subsequent costs are included in the asset’s carrying amount or are recognised as a separate asset, as appropriate, only when it is probable that future economic benefits associated with the item will flow to the Group and Bank and the cost of the item can be measured reliably. All other repairs and maintenance are charged to the profit or loss during the financial period in which they are incurred.

Land and assets under construction are not depreciated. Depreciation on other major classes of assets is calculated using the straight-line method to allocate their cost to their residual values over their estimated useful lives, as follows:

- Buildings 2-3%
- Furniture and fixtures 20-25%
- IT and other equipment 20-25%

The assets’ residual carrying values and useful lives are reviewed, and adjusted if appropriate, at each reporting date.

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Gains and losses on disposals are determined by comparing proceeds with the carrying amount. These are included in the statement of profit or loss and other comprehensive income.

**Assets held for sale**

Non-current assets that are expected to be recovered primarily through sale rather than through continuing use are classified as held for sale. Immediately before classification as held for sale, the assets are remeasured in accordance with the Group and Bank's accounting policies. Thereafter generally the assets are measured at the lower of their carrying amount and fair value less cost to sell.

**Investment properties**

Investment properties are properties which are held either to earn rental income or for capital appreciation, or for both. These include properties with currently undetermined future use. Investment properties are measured initially at cost, including transaction costs. The carrying amount includes the cost of replacing part of an existing investment property at the time that cost is incurred if the recognition criteria are met, and excludes the costs of day-to-day servicing of an investment property. Subsequent to initial recognition, investment properties are stated at cost less accumulated depreciation and any impairment.

Investment properties are derecognised when either they have been disposed of or when the investment property is permanently withdrawn from use and no future economic benefit is expected from its disposal. Any gains or losses on the retirement or disposal of an investment property are recognised in profit or loss in the year of retirement or disposal.

Transfers are made to investment property when, and only when, there is a change in use, evidenced by ending of owner-occupation or commencement of an operating lease to another party. Transfers are made from investment properties when, and only when, there is a change in use, evidenced by commencement of owner-occupation or commencement of development with a view to sale.

**Intangible assets**

Acquired computer software licences are capitalised on the basis of the costs incurred to acquire and bring to use the specific software. Acquired intangible assets are stated at cost less accumulated amortisation and impairment losses.

Amortisation is charged to profit or loss on a straight-line basis over the estimated useful lives of intangible assets. Software has an expected useful life of five to eight years.

**Impairment of non-financial assets**

Assets that are subject to amortization are assessed at each reporting date for any indications of impairment. The recoverable amount of non-financial assets is the greater of their fair value less costs to sell and value in use. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset. For an asset that does not generate cash inflows largely independent of those from other assets, the recoverable amount is determined for the cash-generating unit to which the asset belongs. An impairment loss is recognised when the carrying amount of an asset or its cash-generating unit exceeds its recoverable amount.

All impairment losses in respect of non-financial assets are recognized in profit or loss and reversed only if there has been a change in the estimates used to determine the recoverable amount. Any impairment loss is only reversed to the extent that the asset's carrying amount does not exceed the carrying amount that would have been determined, net of depreciation or amortisation, if no impairment loss had been recognised.

### **Income tax**

Income tax expense comprises current and deferred tax. Income tax is recognised in profit or loss except to the extent that it relates to items recognised directly in equity or in other comprehensive income.

Current tax expense is the expected tax payable on the taxable income for the year, using tax rates enacted or substantially enacted at the reporting date, and any adjustment to tax payable in respect of previous years. Current tax payable also includes any tax liability arising from dividends.

On 13 May 2016 the Parliament of Georgia passed the bill on corporate income tax reform (also known as the Estonian model of corporate taxation), which mainly moves the moment of taxation from when taxable profits are earned to when they are distributed. The law has entered into force in 2016 and is effective for tax periods starting after 1 January 2017 for all entities except for financial institutions (such as banks, insurance companies, microfinance organizations, pawnshops), for which the law used to be entered into force from 1 January 2019, but the Government postponed the launch of the 'Estonian model' of taxation for the financial sector till 2023.

The new system of corporate income taxation does not imply exemption from Corporate Income Tax (CIT), rather CIT taxation is shifted from the moment of earning the profits to the moment of their distribution; i.e. the main tax object is distributed earnings. The Tax Code of Georgia defines Distributed Earnings (DE) to mean profit distributed to shareholders as a dividend. However some other transactions are also considered as DE, for example non-arm's length cross-border transactions with related parties and/or with persons exempted from tax are also considered as DE for CIT purposes. In addition, the tax object includes expenses or other payments not related to the entity's economic activities, free of charge supply and over-limit representative expenses.

The corporate income tax arising from the payment of dividends is accounted for as an expense in the period when dividends are declared, regardless of the actual payment date or the period for which the dividends are paid.

### **Deferred tax**

Deferred tax is provided for temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes. The following temporary differences are not provided for: goodwill not deductible for tax purposes, the initial recognition of assets or liabilities that affect neither accounting nor taxable profit and temporary differences related to investments in subsidiaries, branches and associates where the parent is able to control the timing of the reversal of the temporary difference and it is probable that the temporary difference will not reverse in the foreseeable future. The amount of deferred tax provided is based on the expected manner of realisation or settlement of the carrying amount of assets and liabilities until 1 January 2023, using tax rates enacted or substantially enacted at the reporting date.

A deferred tax asset is recognised only to the extent that it is probable that future taxable profits will be available until 1 January 2023 against which the temporary differences, unused tax losses and credits can be utilised. Deferred tax assets are reviewed at each reporting date and are reduced to the extent that it is no longer probable that the related tax benefit will be realised.

Due to the nature of the new taxation system described above, the financial institutions registered in Georgia will not have any differences between the tax bases of assets and their carrying amounts from 1 January 2023 and hence, no deferred income tax assets and liabilities will arise, there on.

### **Liabilities to banks and customers and other borrowed funds**

Liabilities to banks and customers and other borrowed funds are recognised initially at fair value net of transaction costs incurred. Borrowings are subsequently stated at amortised cost; any difference between proceeds net of transaction costs and the redemption value is recognised in the profit or loss over the period of the borrowings using the effective interest method.



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All financial liabilities are derecognised when they are extinguished – that is, when the obligation is discharged, cancelled or expired.

#### **Provisions**

Provisions are recognised if:

- there is a present legal or constructive obligation resulting from past events;
- it is more likely than not that an outflow of resources will be required to settle the obligation;
- and the amount can be reliably estimated.

Where there are a number of similar obligations, the likelihood that an outflow of resources will be required in a settlement is determined by considering the class of obligations as a whole.

Provisions for which the timing of the outflow of resources is known are measured at the present value of the expenditures, if the outflow will be no earlier than in one year's time. The increase in the present value of the obligation due to the passage of time is recognised as interest expense.

#### **Credit related commitments**

The primary purpose of these instruments is to ensure that funds are available to a customer as required. Guarantees and standby letters of credit, which represent irrevocable assurances that the Group and Bank will make payments in the event that a customer cannot meet its obligations to third parties, carry the same credit risk as loans. Documentary and commercial letters of credit, which are written undertakings by the Group and Bank on behalf of a customer authorising a third party to draw drafts on the Group and Bank up to a stipulated amount under specific terms and conditions, are collateralised by the underlying shipments of goods to which they relate or cash deposits and, therefore, carry less risk than a direct borrowing.

Commitments to extend credit represent unused portions of authorisations to extend credit in the form of loans, guarantees or letters of credit. With respect to credit risk on commitments to extend credit, the Group and Bank is potentially exposed to loss in an amount equal to the total unused commitments, if the unused amounts were to be drawn down. However, the likely amount of loss is less than the total unused commitments since most commitments to extend credit are contingent upon customers maintaining specific credit standards.

#### **Subordinated debt**

Subordinated debt consists mainly of liabilities to shareholders and other international financial institutions which in the event of insolvency or liquidation are not repaid until all non-subordinated creditors have been satisfied. There is no obligation to repay early.

Following initial recognition at fair value, the subordinated debt is measured at amortised cost. Premiums and discounts are accounted for over the respective terms in the profit or loss under "net interest income".

#### **Share capital and share premium**

Ordinary shares are classified as equity. Incremental costs directly attributable to the issue of ordinary shares and share options are recognized as a deduction from equity, net of any tax effects. When share capital is increased, any difference between the registered amount of share capital and the actual consideration received is recognized as share premium.

#### **Dividends**

Dividends on ordinary shares are recognised as a distribution from equity in the period in which they are approved by the Bank's shareholders.

### **Interest income and expense**

Interest income and expense are recorded for all debt instruments, other than those at FVTPL, on an accrual basis using the effective interest method. As part of interest income or expense this method defers all fees paid or received between the parties to the contract that are an integral part of the effective interest rate, transaction costs and all other premiums or discounts. The Group and Bank does not have interest income on debt instruments at FVTPL calculated at nominal interest rate during 2018.

Fees integral to the effective interest rate include origination fees received or paid by the entity relating to the creation or acquisition of a financial asset or issuance of a financial liability, for example fees for evaluating creditworthiness, evaluating and recording guarantees or collateral, negotiating the terms of the instrument and for processing transaction documents. Commitment fees received by the Group and Bank to originate loans at market interest rates are integral to the effective interest rate if it is probable that the Group and Bank will enter into a specific lending arrangement and does not expect to sell the resulting loan shortly after origination. The Group and Bank does not designate loan commitments as financial liabilities at FVTPL.

Interest income is calculated by applying the effective interest rate to the gross carrying amount of financial assets, except for (i) financial assets that have become credit impaired (Stage 3), for which interest income is calculated by applying the effective interest rate to their AC, net of the ECL, and (ii) financial assets that are purchased or originated credit impaired, for which the original credit-adjusted effective interest rate is applied to the AC.

All other fees, commissions and other income and expense items are generally recorded on an accrual basis by reference to completion of the specific transaction assessed on the basis of the actual service provided as a proportion of the total services to be provided.

### **Fee and commission income and expenses**

Fee and commission income and expenses are generally recorded on an accrual basis by reference to completion of the specific transaction assessed on the basis of the actual service provided as a proportion of the total services to be provided.

Commissions for payment transfers and cash transactions and debit/credit card issuance fees, which are earned on execution of the underlying transaction, are recorded upon completion of the transaction. Account maintenance, internet bank and SMS service fees are recognized based on the applicable service contracts, usually on a time-proportion basis.

Loan commitment fees for loans that are likely to be drawn down are deferred (together with related direct costs) and recognised as an adjustment to the effective interest rate of the loan. Loan syndication fees are recognised as revenue when the syndication has been completed and the Group and Bank have retained no part of the loan package for itself or has retained a part at the same effective interest rate as the other participants.

## **4. USE OF ESTIMATES AND JUDGEMENTS**

The preparation of consolidated and separate financial statements in conformity with IFRSs requires management to make judgements, estimates and assumptions that affect the application of accounting policies and the reported amounts of assets, liabilities, income and expenses. Actual results may differ from those estimates.

Estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the period in which the estimates are revised and in any future periods affected.

## **Judgements**

Information about critical judgements in applying accounting policies that have the most significant effect on the amounts recognised in the consolidated financial statements is included in the following judgements:

- **Classification of financial assets:** assessment of the business model within which the assets are held and assessment of whether the contractual terms of the financial asset are solely payments of principal and interest on the principal amount outstanding.
- **Modification of financial assets:** When financial assets are contractually modified (e.g. renegotiated), the Group and Bank assesses whether the modification is substantial and should result in derecognition of the original asset and recognition of a new asset at fair value. This assessment is based primarily on qualitative factors, described in the relevant accounting policy and it requires significant judgment. In particular, the Group and Bank applies judgment in deciding whether credit impaired renegotiated loans should be derecognised and whether the new recognised loans should be considered as credit impaired on initial recognition. The derecognition assessment depends on whether the risks and rewards, that is, the variability of expected (rather than contractual) cash flows, change as a result of such modifications. Management determined that risks and rewards did not change as a result of modifying such loans and therefore in substantially all such modifications, the loans were neither derecognised nor reclassified out of the credit-impaired stage.
- Establishing the criteria for determining whether credit risk on the financial asset has increased significantly since initial recognition, determining methodology for incorporating forward-looking information into measurement of ECL and selection and approval of models used to measure ECL.
- COVID 19 impact assessment – Management’s assessment of the impact of COVID 19 pandemic on Group’s and Bank’s operations.

## **Assumptions and estimations uncertainty**

Information about assumptions and estimation uncertainties that have a significant risk of resulting in a material adjustment in the next financial year is included in the following notes:

- impairment of financial instruments: determining inputs into the ECL measurement model – Note 29(a);
- estimates of fair values of financial assets and liabilities – Note 30;
- COVID 19 impact assessment on expected credit losses – Note 33.

## **5. CHANGES IN SIGNIFICANT ACCOUNTING POLICIES**

**Adoption of IFRS 16 “Leases”.** The Group and Bank has applied IFRS 16 using the modified retrospective approach and therefore the comparative information has not been restated and continues to be reported under IAS 17. At the time of initial application, there were no effects on the opening balance of retained earnings. Accordingly, no adjustment was made to the comparative information for 2018. The Group and Bank applies the definition of a lease under IFRS 16 for all agreements at the date of initial application. There are no leases that were previously classified as finance leases. Leases with a term ending less than 12 months after the date of initial application are treated as short-term leases and are not recognised in the balance sheet. Likewise, no assets of low value are recognised. For contracts with extension and termination options, the term of the lease was determined retrospectively. IFRS 16 is applicable for annual periods beginning on or after 1 January 2019.

### **Right-of-use assets under lease**

From time to time, the Group and Bank leases particular assets for its operating purposes. The Group and Bank have applied IFRS 16 using the modified retrospective approach and therefore the comparative information has not been restated and continues to be reported under IAS 17 and IFRIC 4.

## **PROCREDIT BANK GROUP**

### **Notes to the Financial Statements - 31 December 2019**

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#### **Policy applicable before 1 January 2019**

Operating leases were not recognised in the Group's and Bank's statement of financial position. Payments made under operating leases are recognised in profit or loss on a straight-line basis over the term of the lease.

The Group and Bank did not have any finance leases under IAS 17.

#### **Policy applicable from 1 January 2019**

Group and Bank recognise a right-of-use asset and a lease liability at a lease commencement date. The right-of-use asset is initially measured at cost, which comprises the initial amount of the lease liability adjusted for any lease payments made at or before the commencement date, plus any initial direct costs incurred and an estimate of costs to dismantle and remove any improvements made.

The right-of-use asset is subsequently depreciated using the straight-line method from the commencement date to the end of the lease term. In addition, the right-of-use asset is periodically reduced by impairment losses, if any, and adjusted for certain remeasurements of the lease liability.

The lease liability is initially measured at the present value of the lease payments that are not paid at the commencement date, discounted using the interest rate implicit in the lease or, if that rate cannot be readily determined, the Group's/Bank's incremental borrowing rate. Generally, incremental borrowing rate is used as the discount rate.

The lease liability is measured at amortised cost using the effective interest method. It is remeasured when there is a change in future lease payments or in assessment of whether the Bank will exercise extension or termination option. A corresponding adjustment is made to the carrying amount of the right-of-use asset, or the amount is recorded in profit or loss if the carrying amount of the right-of-use asset has been reduced to zero.

The Bank presents right-of-use assets as separate line-item and lease liabilities in 'other liabilities' in the statement of financial position.

The Bank has elected not to recognise right-of-use assets and lease liabilities for leases of low-value assets and short-term leases. The Bank recognises the lease payments associated with these leases as an expense on a straight-line basis over the lease term.

#### **IFRS 16**

The Group and Bank initially applied IFRS 16 Leases from 1 January 2019.

The Group and Bank applied IFRS 16 using the modified retrospective approach, under which the cumulative effect of initial application is recognised in retained earnings at 1 January 2019. Accordingly, the comparative information presented for 2018 is not restated – i.e. it is presented, as previously reported, under IAS 17 and related interpretations. The details of the changes in accounting policies are disclosed below. Additionally, the disclosure requirements in IFRS 16 have not generally been applied to comparative information.

#### **Definition of a lease**

Previously, the Group and Bank determined at contract inception whether an arrangement was or contained a lease under IAS 17 *Leases* and IFRIC 4 *Determining Whether an Arrangement contains a Lease*.

The Group and Bank now assesses whether a contract is or contains a lease based on the new definition of a lease. Under IFRS 16, a contract is, or contains, a lease if the contract conveys a right to control the use of an identified asset for a period of time in exchange for a consideration.

**PROCREDIT BANK GROUP**  
**Notes to the Financial Statements - 31 December 2019**

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**As a lessee**

The Group and Bank previously classified leases as operating or finance leases based on its assessment of whether the lease transferred significantly all of the risks and rewards incidental to ownership of the underlying asset to the Group and Bank. Under IFRS 16, the Group and Bank recognises right-of-use assets and lease liabilities for most of these leases – i.e. these leases are on-balance sheet. The Group and Bank recognises the lease payments associated with these leases as an expense on a straight-line basis over the lease term.

**(a) Leases classified as operating leases under IAS 17**

Previously, the Group and Bank classified property leases as operating leases under IAS 17. On transition, for these leases, lease liabilities were measured at the present value of the remaining lease payments, discounted at the Group's and Bank's incremental borrowing rate as at 1 January 2019.

The Group and Bank used a number of practical expedients when applying IFRS 16 to leases previously classified as operating leases under IAS 17. In particular, the Group and Bank:

- did not recognise right-of-use assets and liabilities for leases for which the lease term ends within 12 months of the date of initial application;
- did not recognise right-of-use assets and liabilities for leases of low value

**As a lessor**

The Group and Bank leases out its investment property. The Group and Bank has classified these leases as operating leases.

The Group and Bank is not required to make any adjustments on transition to IFRS 16 for leases in which it acts as a lessor.

***Impact on transition***

On transition to IFRS 16, the Group and Bank recognised a right of use asset of GEL 1,778 thousand against a corresponding lease liability on 1 January 2019. The impact on transition is summarised below:

in '000 GEL	1 January 2019
Operating lease commitments at 31 December 2018 as disclosed under IAS 17 in the financial statements	2,038
Discounted using the incremental borrowing rate at 1 January 2019	(260)
Lease liabilities recognised at 1 January 2019	1,778
Right-of-use assets	1,778

**6. NEW STANDARDS AND INTERPRETATIONS NOT YET ADOPTED**

A number of new standards are effective for annual periods beginning after 1 January 2019 and earlier application is permitted; however, the Group and Bank has not early adopted the new or amended standards in preparing these consolidated financial statements.

The following amended standards and interpretations are not expected to have a significant impact on the Group's and Bank's consolidated/seperate financial statements.

- Amendments to References to Conceptual Framework in IFRS Standards.
- Definition of a Business (Amendments to IFRS 3).
- Definition of Material (Amendments to IAS 1 and IAS 8).
- IFRS 17 Insurance Contracts.

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**Notes to the Financial Statements - 31 December 2019**

**7. CASH AND BALANCES WITH THE NBG**

**Consolidated and Separate**

The cash and balances with the National Bank of Georgia (NBG) comprise the following items:

in '000 GEL	31 December 2019	31 December 2018
Cash on hand	46,722	51,948
Balances at the NBG excluding mandatory reserves	4,396	21,539
Nostro accounts other than with NBG	35,868	94,577
Loss allowance for balances with NBG and Nostro accounts	(3)	(222)
<b>Total cash and balances with the NBG in the statement of financial position</b>	<b>86,983</b>	<b>167,842</b>

In 2019, Fitch Ratings affirmed the Government of Georgia's short term Issuer Default Rating of "B" and long-term Issuer Default Rating of "BB+" with the positive outlook (2018: short term "B" and long-term "BB-").

The following cash and equivalents were considered as cash for the cash flow statement:

in '000 GEL	31 December 2019	31 December 2018
Cash and balances with NBG	86,983	167,842
Due from banks with a maturity up to three months (Note 8)	83,489	32,143
Loss allowance for balances with NBG and Nostro accounts	3	218
<b>Total cash and cash equivalents in the statement of cash flows</b>	<b>170,475</b>	<b>200,203</b>

Balances with the NBG above exclude the mandatory reserve deposit which is a non-interest bearing deposit calculated in accordance with regulations issued by the NBG. Refer to Note 30 for the estimated fair value of cash and cash equivalents. The interest rate analysis of cash and cash equivalents is disclosed in Note 29. As at 31 December 2019 the Group and Bank has one bank (2018: no banks), whose balance exceeds 10% of equity. The gross amount of the balance as at 2019 was GEL 33,018 thousand (2018: nil). As at 31 December 2019 the Group and Bank allocates cash equivalents under Stage 1 for the purposes of identifying expected credit loss under IFRS 9 (31 January 2018: Stage 1). Management estimates that ECL is immaterial at reporting dates.

**8. DUE FROM BANKS**

**Consolidated and Separate**

in '000 GEL	31 December 2019	31 December 2018
Due from Banks in OECD* countries	43,370	15,796
Due from Banks in non-OECD countries	40,120	16,395
Loss allowance for loans to banks	(1)	(48)
<b>Total due from banks</b>	<b>83,489</b>	<b>32,143</b>

\* Organisation for Economic Cooperation and Development

The following table details the credit ratings of due from banks as assessed by Fitch Ratings:

in '000 GEL	AA-	A-	BBB	B-	B	Total
Neither past due nor impaired						
<b>31 December 2019</b>	28,646	14,324	479	500	39,540	<b>83,489</b>
<b>31 December 2018</b>	471	10,724	5,339	643	14,966	<b>32,143</b>

As at 31 December 2019 the Group and Bank had 1 related party bank, whose balance of GEL 34,904 thousand (including Nostro accounts and deposits) exceeded 10% of equity. As at 31 December 2018 the Group and Bank had 1 related party bank, whose balance of GEL 39,282 thousand exceeded 10% of equity.

Refer to Note 30 for the estimated fair value of each class of amounts due from banks. The interest rate analysis is disclosed in Note 29. Information on related party balances is disclosed in Note 32.



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**Notes to the Financial Statements - 31 December 2019**

**9. INVESTMENTS IN DEBT SECURITIES**

**Consolidated and Separate**

Figures below represent Investment securities measured at amortized cost.

in '000 GEL	31 December 2019	31 December 2018
Certificates of deposit of the NBG	16,993	24,824
Treasury bills issued by the Government of Georgia	4,924	4,943
<b>Total investments in debt securities</b>	<b>21,917</b>	<b>29,767</b>

No investment in debt securities are past due or impaired. As at 31 December 2019 the Group and Bank allocates investment securities under Stage 1 for the purposes of identifying expected credit loss under IFRS 9 (31 December 2018: Stage 1). Management estimates that ECL is immaterial at reporting dates.

**10. INVESTMENTS**

**Investments in subsidiaries**

**Separate**

Investment in subsidiaries (related to separate financial statements)

Investment in subsidiaries as at the reporting dates were as follows:

Subsidiary	Country of incorporation	Ownership as at 31 December 2019	Investment as at 31 December 2019 ('000 GEL)
LLC ProCredit Property	Georgia	100.00%	6,100

Subsidiary	Country of incorporation	Ownership as at 31 December 2018	Investment as at 31 December 2018 ('000 GEL)
LLC ProCredit Property	Georgia	100.00%	6,100

LLC Procredit Property is a wholly-owned subsidiary of Procredit Bank Georgia, which was formed under Georgian Law on 23 July 2007. The principal operations of the company are holding and managing movable and immovable properties acquired through auctions from the Bank's defaulted customers. As at 31 December 2019 net assets of the Subsidiary is GEL 9,443 thousand (2018: GEL 5,561 thousand).

**Investments in equity securities**

**Consolidated and Separate**

Equity investments comprise shares in the following companies:

in '000 GEL	Ownership interest	Amount At 31 December 2019	Ownership interest	Amount At 31 December 2018
JSC Creditinfo Georgia	21.08%	95	21.08%	95
JSC United Clearing Center Georgia	6.25%	54	6.25%	54
JSC American Academy in Tbilisi	4.73%	50	4.85%	50
S.W.I.F.T.SCRL	0.12%	35	0.01%	35
<b>Total</b>		<b>234</b>		<b>234</b>

The Bank does not have significant influence over JSC Creditinfo Georgia.

**PROCREDIT BANK GROUP**  
**Notes to the Financial Statements - 31 December 2019**

**11. LOANS AND ADVANCES TO CUSTOMERS**

**Consolidated and Separate**

The table below presents contractual size and outstanding amounts of loans and advances to customers as at 31 December 2019:

in '000 GEL (except for number of outstanding loans and loan sizes) At 31 December 2019	Gross amount	ECL allowance for impairment	Net amount	Share of total portfolio
<b>Wholesale and trade loans</b>				
loan size up to USD 50,000	24,050	(1,235)	22,815	2.13%
loan size USD 50,000 to USD 250,000	136,278	(2,499)	133,779	12.50%
loan size more than USD 250,000	181,180	(1,471)	179,709	16.79%
<b>Total wholesale and trade loans</b>	<b>341,508</b>	<b>(5,205)</b>	<b>336,303</b>	<b>31.43%</b>
<b>Agricultural, forestry and fishing loans</b>				
loan size up to USD 50,000	3,020	(35)	2,985	0.28%
loan size USD 50,000 to USD 250,000	16,944	(463)	16,481	1.54%
loan size more than USD 250,000	18,629	(120)	18,509	1.73%
<b>Total agricultural, forestry and fishing loans</b>	<b>38,593</b>	<b>(618)</b>	<b>37,975</b>	<b>3.55%</b>
<b>Production loans</b>				
loan size up to USD 50,000	11,220	(370)	10,850	1.01%
loan size USD 50,000 to USD 250,000	60,433	(2,694)	57,739	5.40%
loan size more than USD 250,000	81,338	(1,411)	79,927	7.47%
<b>Total production loans</b>	<b>152,991</b>	<b>(4,475)</b>	<b>148,516</b>	<b>13.88%</b>
<b>Transportation and storage loans</b>				
loan size up to USD 50,000	2,769	(217)	2,552	0.24%
loan size USD 50,000 to USD 250,000	12,047	(159)	11,888	1.11%
loan size more than USD 250,000	7,186	(31)	7,155	0.67%
<b>Total transportation and storage loans</b>	<b>22,002</b>	<b>(407)</b>	<b>21,595</b>	<b>2.02%</b>
<b>Other economic activities</b>				
loan size up to USD 50,000	26,493	(571)	25,922	2.42%
loan size USD 50,000 to USD 250,000	132,138	(4,586)	127,552	11.92%
loan size more than USD 250,000	272,475	(4,472)	268,003	25.04%
<b>Total other economic activities loans</b>	<b>431,106</b>	<b>(9,629)</b>	<b>421,477</b>	<b>39.39%</b>
<b>Total Business loans</b>	<b>986,200</b>	<b>(20,334)</b>	<b>965,866</b>	<b>90.26%</b>
<b>Housing loans</b>				
loan size up to USD 50,000	33,385	(774)	32,611	3.05%
loan size USD 50,000 to USD 250,000	67,980	(2,337)	65,643	6.13%
loan size more than USD 250,000	2,432	(17)	2,415	0.23%
<b>Total housing loans</b>	<b>103,797</b>	<b>(3,128)</b>	<b>100,669</b>	<b>9.41%</b>
<b>Investment loans</b>				
loan size up to USD 50,000	3,203	(91)	3,112	0.29%
loan size USD 50,000 to USD 250,000	351	(2)	349	0.03%
<b>Total investment loans</b>	<b>3,554</b>	<b>(93)</b>	<b>3,461</b>	<b>0.32%</b>
<b>Other loans</b>	<b>129</b>	<b>(5)</b>	<b>124</b>	<b>0.01%</b>
<b>Total Private loans</b>	<b>107,480</b>	<b>(3,226)</b>	<b>104,254</b>	<b>9.74%</b>
<b>Total</b>	<b>1,093,680</b>	<b>(23,560)</b>	<b>1,070,120</b>	<b>100.00%</b>

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The table below presents contractual size and outstanding amounts of loans and advances to customers as at 31 December 2018:

in '000 GEL (except for number of outstanding loans and loan sizes) <b>At 31 December 2018</b>	<b>Gross amount</b>	<b>ECL allowance for impairment</b>	<b>Net amount</b>	<b>Share of total portfolio</b>
<b>Wholesale and trade loans</b>				
loan size up to USD 50,000	31,614	(1,706)	29,908	2.92%
loan size USD 50,000 to USD 250,000	145,150	(4,997)	140,153	13.70%
loan size more than USD 250,000	169,598	(1,690)	167,908	16.41%
<b>Total wholesale and trade loans</b>	<b>346,362</b>	<b>(8,393)</b>	<b>337,969</b>	<b>33.03%</b>
<b>Agricultural, forestry and fishing loans</b>				
loan size up to USD 50,000	2,655	(109)	2,546	0.25%
loan size USD 50,000 to USD 250,000	14,105	(1,256)	12,849	1.26%
loan size more than USD 250,000	29,737	(280)	29,457	2.88%
<b>Total agricultural, forestry and fishing loans</b>	<b>46,497</b>	<b>(1,645)</b>	<b>44,852</b>	<b>4.38%</b>
<b>Production loans</b>				
loan size up to USD 50,000	11,801	(634)	11,167	1.09%
loan size USD 50,000 to USD 250,000	61,871	(2,879)	58,992	5.77%
loan size more than USD 250,000	69,200	(496)	68,704	6.71%
<b>Total production loans</b>	<b>142,872</b>	<b>(4,009)</b>	<b>138,863</b>	<b>13.57%</b>
<b>Transportation and storage loans</b>				
loan size up to USD 50,000	3,562	(130)	3,432	0.34%
loan size USD 50,000 to USD 250,000	14,961	(224)	14,737	1.44%
loan size more than USD 250,000	2,849	(25)	2,824	0.28%
<b>Total transportation and storage loans</b>	<b>21,372</b>	<b>(379)</b>	<b>20,993</b>	<b>2.05%</b>
<b>Other economic activities</b>				
loan size up to USD 50,000	29,158	(788)	28,370	2.77%
loan size USD 50,000 to USD 250,000	145,519	(5,519)	140,000	13.68%
loan size more than USD 250,000	203,609	(2,828)	200,781	19.62%
<b>Total other economic activities loans</b>	<b>378,286</b>	<b>(9,135)</b>	<b>369,151</b>	<b>36.08%</b>
<b>Total Business loans</b>	<b>935,389</b>	<b>(23,561)</b>	<b>911,828</b>	<b>89.11%</b>
<b>Housing loans</b>				
loan size up to USD 50,000	36,573	(707)	35,866	3.51%
loan size USD 50,000 to USD 250,000	71,029	(2,123)	68,906	6.73%
loan size more than USD 250,000	2,851	(26)	2,825	0.28%
<b>Total housing loans</b>	<b>110,453</b>	<b>(2,856)</b>	<b>107,597</b>	<b>10.52%</b>
<b>Investment loans</b>				
loan size USD 50,000 to USD 250,000	3,405	(129)	3,276	0.32%
loan size more than USD 250,000	340	(3)	337	0.03%
<b>Total investment loans</b>	<b>3,745</b>	<b>(132)</b>	<b>3,613</b>	<b>0.35%</b>
<b>Other loans</b>	<b>225</b>	<b>(7)</b>	<b>218</b>	<b>0.02%</b>
<b>Total Private loans</b>	<b>114,423</b>	<b>(2,995)</b>	<b>111,428</b>	<b>10.89%</b>
<b>Total</b>	<b>1,049,812</b>	<b>(26,556)</b>	<b>1,023,256</b>	<b>100.00%</b>

The size categories above refer to the amounts originally disbursed to one single borrower.

As at 31 December 2019 and 2018 the Group and the Bank had no borrowers or groups of connected borrowers whose loan balances exceeded 10% of equity.

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The following table discloses the changes in the expected credit loss allowance and gross carrying amount for loans and advances to customers carried at amortised cost between the beginning and the end of the reporting period

**Consolidated and Separate**

in '000 GEL	Stage 1	Stage 2	Stage 3	POCI	Total
<b>Gross outstanding amount as at 1 January 2019</b>	<b>997,060</b>	<b>23,986</b>	<b>28,768</b>	-	<b>1,049,814</b>
New financial assets originated	662,317	14,518	3,140	1,148	681,123
Modification of contractual cash flows of financial assets	157	(33)	54	-	178
Derecognitions	(434,728)	(18,530)	(14,132)	-	(467,390)
Write-offs	-	-	(9,492)	-	(9,492)
Changes in interest accrual	1,681	272	975	29	2,957
Repayments	(199,892)	(6,870)	(4,303)	(42)	(211,107)
Transfer from Stage 1 to Stage 2	(54,269)	54,269	-	-	-
Transfer from Stage 1 to Stage 3	(10,398)	-	10,398	-	-
Transfer from Stage 2 to Stage 1	17,708	(17,708)	-	-	-
Transfer from Stage 2 to Stage 3	-	(15,926)	15,926	-	-
Transfer from Stage 3 to Stage 2	-	1,156	(1,156)	-	-
Transfer from Stage 3 to Stage 1	67	-	(67)	-	-
Foreign exchange and other movements.	45,915	1,299	381	2	47,597
<b>Gross outstanding amount as at 31 December 2019</b>	<b>1,025,618</b>	<b>36,433</b>	<b>30,492</b>	<b>1,137</b>	<b>1,093,680</b>

in '000 GEL	Stage 1	Stage 2	Stage 3	POCI	Total
<b>Gross outstanding amount as at 1 January 2018</b>	<b>942,132</b>	<b>32,758</b>	<b>31,171</b>	<b>51</b>	<b>1,006,112</b>
New financial assets originated	433,718	1,735	300	-	435,753
Modification of contractual cash flows of financial assets	(230)	-	(19)	-	(249)
Derecognitions	(281,553)	(10,406)	(7,467)	(51)	(299,477)
Write-offs	(68)	(127)	(6,744)	-	(6,939)
Changes in interest accrual	213	139	(111)	-	241
Repayments	(105,113)	(3,981)	(2,831)	-	(111,925)
Transfer from Stage 1 to Stage 2	(8,077)	8,077	-	-	-
Transfer from Stage 1 to Stage 3	(6,622)	-	6,622	-	-
Transfer from Stage 2 to Stage 1	4,522	(4,522)	-	-	-
Transfer from Stage 2 to Stage 3	-	(4,090)	4,090	-	-
Transfer from Stage 3 to Stage 2	-	1,035	(1,035)	-	-
Transfer from Stage 3 to Stage 1	785	-	(785)	-	-
Foreign exchange and other movements	17,353	3,368	5,577	-	26,298
<b>Gross outstanding amount as at 31 December 2018</b>	<b>997,060</b>	<b>23,986</b>	<b>28,768</b>	<b>-</b>	<b>1,049,814</b>

The total amount of loans recoveries of amounts previously written off during the year 2019 was GEL 7,690 thousand (2018: GEL 6,399 thousand).

Further analysis loans is detailed in Note 29.

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The table below show reconciliations from the opening to the closing balances of the expected credit loss allowance of loans to customers:

**Consolidated and Separate**

	Stage 1	Stage 2	Stage 3	(POCI)	Total
<b>Balance at 1 January 2019</b>	<b>(8,683)</b>	<b>(2,690)</b>	<b>(15,183)</b>	<b>-</b>	<b>(26,556)</b>
New financial assets originated	(5,373)	(257)	(22)	-	(5,652)
Release due to derecognition	3,848	1,680	6,384	-	11,912
Transfer from Stage 1 to Stage 2	455	(455)	-	-	-
Transfer from Stage 1 to Stage 3	76	-	(76)	-	-
Transfer from Stage 2 to Stage 1	(177)	177	-	-	-
Transfer from Stage 2 to Stage 3	-	2,060	(2,060)	-	-
Transfer from Stage 3 to Stage 2	-	(175)	175	-	-
Transfer from Stage 3 to Stage 1	(1)	-	1	-	-
Increase in PDs/LGDs/EaDs	(1,637)	(6,358)	(15,128)	(97)	(23,220)
Decrease in PDs/LGDs/EaDs	5,462	5,022	3,653	-	14,137
Usage of allowance	-	-	9,492	-	9,492
Increase due to modification without derecognition	(51)	(201)	(2,013)	-	(2,265)
Decrease due to modification without derecognition	66	49	13	-	128
Foreign exchange and other movements	(304)	(419)	(813)	-	(1,536)
<b>Balance at 31 December 2019</b>	<b>(6,319)</b>	<b>(1,567)</b>	<b>(15,577)</b>	<b>(97)</b>	<b>(23,560)</b>

	Stage 1	Stage 2	Stage 3	(POCI)	Total
<b>Balance at 1 January 2018</b>	<b>(10,847)</b>	<b>(3,934)</b>	<b>(11,897)</b>	<b>-</b>	<b>(26,678)</b>
New financial assets originated	(3,588)	(267)	(141)	-	(3,996)
Release due to derecognition	3,258	1,162	2,635	-	7,055
Transfer from Stage 1 to Stage 2	99	(99)	-	-	-
Transfer from Stage 1 to Stage 3	82	-	(82)	-	-
Transfer from Stage 2 to Stage 1	(656)	656	-	-	-
Transfer from Stage 2 to Stage 3	-	483	(483)	-	-
Transfer from Stage 3 to Stage 2	-	(368)	368	-	-
Transfer from Stage 3 to Stage 1	(349)	-	349	-	-
Increase in PDs/LGDs/EaDs	(138)	(1,135)	(14,346)	-	(15,619)
Decrease in PDs/LGDs/EaDs	2,636	1,148	2,492	-	6,276
Usage of allowance	68	127	6,744	-	6,939
Foreign exchange and other movements	752	(463)	(822)	-	(533)
<b>Balance at 31 December 2018</b>	<b>(8,683)</b>	<b>(2,690)</b>	<b>(15,183)</b>	<b>-</b>	<b>(26,556)</b>

Analysis by credit quality of loans outstanding at 31 December 2019 is as follows:

in '000 GEL	Wholesale Agriculture, and retail forestry and trade		Production	Transportation and storage	Other economic activities	Housing	Investment	Other	Total
<b>Stage 1</b>									
Not in Arrears	323,801	37,026	136,536	21,073	402,362	98,004	3,299	122	1,022,223
- less than 30 days overdue	63	48	591	465	1,702	521	4	1	3,395
<b>Total Stage 1 loans</b>	<b>323,864</b>	<b>37,074</b>	<b>137,127</b>	<b>21,538</b>	<b>404,064</b>	<b>98,525</b>	<b>3,303</b>	<b>123</b>	<b>1,025,618</b>
<b>Stage 2</b>									
Not in Arrears	10,390	1,105	6,564	39	11,721	1,119	41	0	30,979
- less than 30 days overdue	938	-	344	-	664	-	110	-	2,056
- 31 to 90 days overdue	199	-	1,487	-	1,019	676	16	1	3,398
<b>Total Stage 2 loans</b>	<b>11,527</b>	<b>1,105</b>	<b>8,395</b>	<b>39</b>	<b>13,404</b>	<b>1,795</b>	<b>167</b>	<b>1</b>	<b>36,433</b>
<b>Stage 3</b>									
Not in Arrears	1,883	52	5,137	-	1,430	907	24	4	9,437
- less than 30 days overdue	254	-	139	17	-	544	-	-	954
- 31 to 90 days overdue	1,844	-	-	224	3,235	822	-	-	6,125
- over 90 days overdue	2,135	360	2,193	184	7,837	1,204	62	1	13,976
<b>Total Stage 3 loans</b>	<b>6,116</b>	<b>412</b>	<b>7,469</b>	<b>425</b>	<b>12,502</b>	<b>3,477</b>	<b>86</b>	<b>5</b>	<b>30,492</b>

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in '000 GEL	Wholesale trade	Agriculture, and retail forestry and fishing	Production	Transport ation and storage	Other economic activities	Housing	Investment	Other	Total
<b>POCI</b>									
Not in Arrears	-	2	-	-	-	-	-	-	2
- over 90 days overdue	-	-	-	-	1,135	-	-	-	1,135
<b>Total POCI loans</b>	-	2	-	-	1,135	-	-	-	1,137
<b>Less impairment provisions</b>	(5,205)	(618)	(4,475)	(407)	(9,628)	(3,128)	(95)	(4)	(23,560)
<b>Total loans and advances to customers</b>	<b>336,302</b>	<b>37,975</b>	<b>148,516</b>	<b>21,595</b>	<b>421,477</b>	<b>100,669</b>	<b>3,461</b>	<b>125</b>	<b>1,070,120</b>

Analysis by credit quality of loans outstanding at 31 December 2018 is as follows:

in '000 GEL	Wholesale trade	Agriculture, and retail forestry and fishing	Production	Transport ation and storage	Other economic activities	Housing	Investment	Other	Total
<b>Stage 1</b>									
Not in Arrears	332,045	39,903	135,328	19,206	352,012	103,929	3,390	213	986,026
- less than 30 days overdue	1,621	2,798	120	1,180	4,264	1,040	5	4	11,032
<b>Total Stage 1 loans</b>	<b>333,666</b>	<b>42,701</b>	<b>135,448</b>	<b>20,386</b>	<b>356,276</b>	<b>104,969</b>	<b>3,395</b>	<b>217</b>	<b>997,058</b>
<b>Stage 2</b>									
Not in Arrears	2,145	1,936	2,137	-	11,205	2,147	168	1	19,739
- less than 30 days overdue	761	-	-	143	80	262	9	-	1,255
- 31 to 90 days overdue	1,111	-	24	597	1,119	125	14	2	2,992
<b>Total Stage 2 loans</b>	<b>4,017</b>	<b>1,936</b>	<b>2,161</b>	<b>740</b>	<b>12,404</b>	<b>2,534</b>	<b>191</b>	<b>3</b>	<b>23,986</b>
<b>Stage 3</b>									
Not in Arrears	3,375	235	2,128	127	2,207	806	31	1	8,910
- less than 30 days overdue	173	343	1,048	-	492	623	-	-	2,679
- 31 to 90 days overdue	1,052	830	383	34	729	50	31	-	3,109
- over 90 days overdue	4,078	451	1,705	86	6,179	1,472	93	6	14,070
<b>Total Stage 3 loans</b>	<b>8,678</b>	<b>1,859</b>	<b>5,264</b>	<b>247</b>	<b>9,607</b>	<b>2,951</b>	<b>155</b>	<b>7</b>	<b>28,768</b>
<b>Less impairment provisions</b>	(8,393)	(1,645)	(4,009)	(379)	(9,135)	(2,856)	(132)	(7)	(26,556)
<b>Total loans and advances to customers</b>	<b>337,968</b>	<b>44,851</b>	<b>138,864</b>	<b>20,994</b>	<b>369,152</b>	<b>107,598</b>	<b>3,609</b>	<b>220</b>	<b>1,023,256</b>

Loans in arrears more than 90 days are classified as impaired loans. Loans in arrears with less than or equal to 30 days overdue are considered unimpaired.

The size categories above refer to the amounts originally disbursed to the groups of connected borrowers.

**Key assumptions and judgments for estimating allowance for loan impairment**

Key assumptions used by the Group and Bank in estimation of the expected credit loss on loans to customers are as follows:

- Probability of default(PD)
- Loss given default (LGD)

Change in these estimates by 10% increase/decrease could affect the expected credit loss on loans to customers for 2019 by GEL 2,500 thousand.

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**Collateral**

The general creditworthiness of a customer tends to be the most relevant indicator of credit quality of the loan extended to it. However, collateral provides additional security and the Group and Bank generally requests the borrowers to provide it.

For loans to customers which are performing, the fair value of collateral was estimated at the inception of the loans and was not adjusted for subsequent changes to the reporting date. The recoverability of these loans is primarily dependent on the creditworthiness of the borrowers rather than the value of collateral, and the Group and Bank does not necessarily update the valuation of collateral as at each reporting date.

The following tables provide information on collateral securing loans and advances to customers by type of collateral as at 31 December 2019 and 2018:

in '000 GEL At 31 December 2019	Real estate	Financial guarantees	Cash collateral	Other	No collateral	Total
Wholesale and trade	312,099	10,273	332	8,268	5,331	336,303
Agriculture, forestry and fishing	34,657	880	724	704	1,010	37,975
Production	118,133	9,480	911	17,253	2,739	148,516
Transportation and storage	17,056	459	-	3,827	253	21,595
Other economic activities	392,846	6,848	828	12,841	8,114	421,477
Housing	100,604	-	65	-	-	100,669
Investment loans	1,500	-	576	-	1,385	3,461
Other	1	-	-	-	123	124
<b>Total</b>	<b>976,896</b>	<b>27,940</b>	<b>3,436</b>	<b>42,893</b>	<b>18,955</b>	<b>1,070,120</b>

As at 31 December 2019 and 2018 'Other' collateral consists from: Shares in companies, Movable properties (Vehicles, Equipment), Household Goods, Livestock, Inventory, Receivables.

in '000 GEL At 31 December 2018	Real estate	Financial guarantees	Cash collateral	Other	No collateral	Total
Wholesale and trade	302,686	13,117	628	8,480	13,058	337,969
Agriculture, forestry and fishing	38,815	143	936	4,372	585	44,851
Production	115,135	9,361	-	10,748	3,619	138,863
Transportation and storage	17,436	1,134	-	2,028	395	20,993
Other economic activities	343,831	6,815	765	5,109	12,631	369,151
Housing	106,153	-	302	-	1,142	107,597
Investment loans	2,539	-	75	-	998	3,612
Other	3	-	-	-	217	220
<b>Total</b>	<b>926,598</b>	<b>30,570</b>	<b>2,706</b>	<b>30,737</b>	<b>32,645</b>	<b>1,023,256</b>

The tables above exclude overcollateralization and include value of collateral (mainly real estate) for Stage 3 loans, which exceeds the carrying amount of the Stage 3 loans at each reporting date.

If loan is collateralized by multiple type of collateral the collateral should be considered in the indicated order: Cash collateral, Financial Guarantees, Real estate and only last Movable collateral.

Refer to Note 30 for the estimated fair value of each class of loans and advances to customers. For more information on credit risk management and interest rate analysis of loans and advances to customers refer to Note 29.

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**12. INVESTMENT PROPERTIES**

**Consolidated**

in '000 GEL	2019	2018
<b>Net book value at 1 January</b>	<b>9,875</b>	<b>10,965</b>
Additions	1,004	1,383
Disposals	(2,168)	(2,434)
Depreciation for the year	(179)	(184)
Disposal of depreciation	60	145
<b>Net book value at 31 December</b>	<b>8,592</b>	<b>9,875</b>
Total acquisition costs	9,694	10,858
Accumulated depreciation	(1,102)	(983)
<b>Net book value at 31 December</b>	<b>8,592</b>	<b>9,875</b>

Rental income in 2019 under operating leases was GEL 1,238 thousand (2018: GEL 951 thousand).

**Separate**

in '000 GEL	2019	2018
<b>Net book value at 1 January</b>	<b>5,401</b>	<b>5,513</b>
Additions	-	584
Disposals	-	(686)
Depreciation for the year	(154)	(155)
Disposal of depreciation	-	145
<b>Net book value at 31 December</b>	<b>5,247</b>	<b>5,401</b>
Total acquisition costs	6,281	6,281
Accumulated depreciation	(1,034)	(880)
<b>Net book value at 31 December</b>	<b>5,247</b>	<b>5,401</b>

Management estimates that the fair value of the investment properties approximates their carrying amount. The fair value estimate is categorized into Level 3 of the fair value hierarchy, because of significant unobservable adjustments used in the valuation method. The fair value was determined based on market prices in recent transactions or announced asking prices of similar properties. Key unobservable input used for sales comparison approach is price per square meter of similar properties. Adjustments are applied to the observable prices based on the difference between subject assets and analogues.

**13. INTANGIBLE ASSETS**

The development of intangible assets is shown in the following table:

**Consolidated and Separate**

in '000 GEL	2019	2018
<b>Net book value as at 1 January</b>	1,287	1,393
Additions	600	320
Disposal	(5,904)	-
Amortisation for the year	(563)	(426)
Disposal of amortisation	5,124	-
<b>Net book value as at 31 December</b>	<b>544</b>	<b>1,287</b>
Total acquisition costs as at 31 December	4,572	9,876
Accumulated amortisation as at 31 December	(4,028)	(8,589)
<b>Net book value as at 31 December</b>	<b>544</b>	<b>1,287</b>

During 2019, the Group and Bank have written off unused Microsoft licenses GEL 5,904 thousand (2018: Nil)



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**14. PROPERTY AND EQUIPMENT**

The development of property and equipment was as follows:

**Consolidated and Separate**

in '000 GEL	Land & buildings, assets under construction	Other fixed assets	Total PPE
<b>Net book value at 1 January 2018</b>	<b>48,823</b>	<b>14,329</b>	<b>63,152</b>
Additions	502	1,242	1,744
Disposals - at cost	(5,063)	(8,349)	(13,412)
Depreciation for the year	(1,175)	(3,162)	(4,337)
Disposals - accumulated depreciation	1,346	7,098	8,444
<b>Net book value at 31 December 2018</b>	<b>44,433</b>	<b>11,158</b>	<b>55,591</b>
Total acquisition costs	51,927	31,681	83,608
Accumulated depreciation	(7,494)	(20,523)	(28,017)
<b>Net book value at 1 January 2019</b>	<b>44,433</b>	<b>11,158</b>	<b>55,591</b>
Additions	280	1,446	1,726
Disposals - at cost	(2,245)	(1,916)	(4,161)
Depreciation for the year	(1,116)	(3,330)	(4,446)
Disposals - accumulated depreciation	385	1,903	2,288
<b>Net book value at 31 December 2019</b>	<b>41,737</b>	<b>9,261</b>	<b>50,998</b>
Total acquisition costs	49,962	31,211	81,173
Accumulated depreciation	(8,225)	(21,950)	(30,175)
<b>Net book value at 31 December 2019</b>	<b>41,737</b>	<b>9,261</b>	<b>50,998</b>

**15. RIGHT-OF-USE ASSETS AND LEASE LIABILITY**

**Consolidated and Separate**

**(a) Right-of-use assets**

in '000 GEL	2019
<b>Net book value at 1 January</b>	<b>1,778</b>
Additions	1,940
Disposals	(329)
Depreciation for the year	(650)
Disposals - accumulated depreciation	132
<b>Net book value at 31 December 2019</b>	<b>2,871</b>

**(b) Lease liability**

in '000 GEL	2019
<b>Lease liabilities recognised at 1 January 2019</b>	<b>1,778</b>
Payments of lease liability 2019	(711)
Additions 2019	1,768
Unwinding discount using the incremental borrowing rate	103
<b>Lease liabilities recognised at 31 December 2019</b>	<b>2,938</b>

When measuring lease liabilities for lease that were classified as operating leases, the Group and Bank discounted lease payments using its incremental borrowing rate at 1 January 2019. The weighted-average rate applied is 5.3% term of lease contracts very from 2020 to 2024.

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**16. OTHER ASSETS**

At 31 December 2019 and 2018, other assets were as follows:

**Consolidated**

in '000 GEL	31 December 2019	31 December 2018
Accounts receivable from credit card and online payment system companies and money transfer agencies	3,914	3,598
Security deposit	514	471
Other	138	132
Loss allowance for account receivables	(48)	(81)
<b>Total other financial assets</b>	<b>4,518</b>	<b>4,120</b>
<i>Non-current</i>		
Prepayments for court fees and charges, net of provision	892	927
Prepayments for fixed assets	476	90
Repossessed property	127	-
<i>Current</i>		
Prepayments for various services	2,134	2,014
Assets classified as held for sale	-	192
Inventory and other	374	765
<b>Total other non-financial assets</b>	<b>4,003</b>	<b>3,988</b>
<b>Total</b>	<b>8,521</b>	<b>8,108</b>

**Separate**

in '000 GEL	31 December 2019	31 December 2018
Accounts receivable from credit card and online payment system companies and money transfer agencies	3,730	3,598
Security deposit	514	471
Other	138	132
Loss allowance for account receivables	(48)	(81)
<b>Total other financial assets</b>	<b>4,334</b>	<b>4,120</b>
<i>Non-current</i>		
Repossessed properties	127	-
Prepayments for court fees and charges, net of provision	892	927
Prepayments for fixed assets	476	90
<i>Current</i>		
Prepayments for various services	2,000	1,738
Assets classified as held for sale	-	192
Inventory and other	372	764
<b>Total other non-financial assets</b>	<b>3,867</b>	<b>3,711</b>
<b>Total</b>	<b>8,201</b>	<b>7,831</b>

As at the date of initial recognition and as at 31 December 2019 and 31 December 2018, management believes that the carrying value of the assets held for sale was not materially different from their fair value less costs to sell at those dates. The fair value estimate is categorized into Level 3 of the fair value hierarchy, because of significant unobservable adjustments used in the valuation method. The fair value was determined based on market prices in recent transactions or announced asking prices of similar properties.

Group and Bank allocates other assets under Stage 1 for the purposes of identifying expected credit loss under IFRS 9 (31 January 2018: Stage 1). ECL at the year ends is shown in the above table.

Refer to Note 30 for the estimated fair value of other financial assets. Information on related party balances is disclosed in Note 32.

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**17. DUE TO BANKS**

Due to banks consists of short-term loans obtained on the interbank market, as well as funds kept by other banks on correspondent accounts with the Bank.

**Consolidated and Separate**

in '000 GEL	31 December 2019	31 December 2018
Banks in OECD countries	69,801	51,763
Banks in non-OECD countries	606	19,845
<b>Total</b>	<b>70,407</b>	<b>71,608</b>

Refer to Note 30 for the estimated fair value of due to banks. Information on related party balances is disclosed in Note 32.

**18. CUSTOMER ACCOUNTS**

Customer accounts consist of deposits due on demand, savings deposits and term deposits. The following table shows a breakdown by customer groups:

**Consolidated**

in '000 GEL	31 December 2019	31 December 2018
<b>Current accounts</b>	<b>224,775</b>	<b>221,694</b>
- private individuals	56,399	56,994
- legal entities	168,376	164,700
<b>Savings accounts</b>	<b>249,314</b>	<b>230,271</b>
- private individuals	158,694	148,883
- legal entities	90,620	81,388
<b>Term deposit accounts</b>	<b>289,152</b>	<b>238,302</b>
- private individuals	234,817	186,616
- legal entities	54,335	51,686
<b>Other liabilities to customers</b>	<b>4,056</b>	<b>6,110</b>
<b>Total</b>	<b>767,297</b>	<b>696,377</b>

**Separate**

in '000 GEL	31 December 2019	31 December 2018
<b>Current accounts</b>	<b>228,864</b>	<b>225,012</b>
- private individuals	56,399	56,994
- legal entities	172,465	168,018
<b>Savings accounts</b>	<b>249,313</b>	<b>230,271</b>
- private individuals	158,693	148,883
- legal entities	90,620	81,388
<b>Term deposit accounts</b>	<b>289,152</b>	<b>238,302</b>
- private individuals	234,817	186,616
- legal entities	54,335	51,686
<b>Other liabilities to customers</b>	<b>4,056</b>	<b>6,109</b>
<b>Total</b>	<b>771,385</b>	<b>699,694</b>

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At 31 December 2019, the Group and Bank had included pending client transfers of GEL 4,056 thousand (2018: GEL 6,100 thousand) in other liabilities to customers.

The category “legal entities” includes liabilities to non-governmental organisations (NGOs) and public-sector institutions.

The following table shows a breakdown of customer accounts by economic sector:

**Consolidated**

in '000 GEL	31 December 2019	31 December 2018
Private individuals	449,909	392,493
Trade and services	222,703	209,327
Transportation and communications	29,809	27,344
Construction	25,144	20,571
Manufacture	14,281	13,207
Agriculture and forestry	12,045	10,621
Mining and mineral processing	832	1,147
Government	-	4,760
Other	12,574	16,907
<b>Total</b>	<b>767,297</b>	<b>696,377</b>

**Separate**

in '000 GEL	31 December 2019	31 December 2018
Private individuals	449,909	392,493
Trade and services	226,792	212,644
Transportation and communications	29,809	27,344
Construction	25,144	20,571
Manufacture	14,281	13,207
Agriculture and forestry	12,045	10,621
Mining and mineral processing	832	1,147
Government	-	4,760
Other	12,573	16,907
<b>Total</b>	<b>771,385</b>	<b>699,694</b>

At 31 December 2019, the Group and Bank had 91 customers (2018: 84 customers) with balances above GEL 1,000 thousand. The aggregate balance of these customers was GEL 263,390 thousand (2018: GEL 234,927 thousand) or 34 % (2018: 33 %) of total customer accounts.

At 31 December 2019, customer accounts included deposits of GEL 3,436 thousand (2018: GEL 2,706 thousand) held as collateral for on-balance exposures and GEL 5,691 thousand (2018: GEL 5,898 thousand) held as collateral for irrevocable commitments under financial and performance guarantees and letters of credit refer to Note 31.

Interest rate analysis is disclosed in Note 29. Information on related party balances is disclosed in Note 32. Refer to Note 30 for the estimated fair value of each class of customer accounts.

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**19. OTHER BORROWED FUNDS**

**Consolidated and Separate**

Liabilities to international financial institutions are an important source of financing for the Group and Bank. Below are reported medium- to long-term loans from international financial institutions:

in '000 GEL

<b>Liabilities with fixed interest rates</b>	<b>Due</b>	<b>31 December 2019</b>	<b>31 December 2018</b>
Ministry of Finance of Georgia	December 2026	2,044	2,228
European Investment Bank (EIB)	March 2023	24,831	29,871
European Investment Bank (EIB)	April 2024	19,281	22,050
European Investment Bank (EIB)	July 2022	17,513	21,848
European Investment Bank (EIB)	October 2024	16,999	15,905
European Investment Bank (EIB)	February 2024	4,732	5,325
European Investment Bank (EIB)	April 2022	3,829	5,016
Council of Europe Development Bank (CEB)	August 2022	9,291	11,623
ProCredit Holding AG & Co. KGaA	May 2024	50,336	-
ProCredit Holding AG & Co. KGaA	April 2024	14,539	-
ProCredit Holding AG & Co. KGaA	April 2024	14,538	-
ProCredit Holding AG & Co. KGaA	August 2027	14,533	13,598
ProCredit Holding AG & Co. KGaA	August 2027	14,533	13,598
ProCredit Holding AG & Co. KGaA	June 2021	-	13,484
ProCredit Holding AG & Co. KGaA	May 2021	-	13,450
ProCredit Holding AG & Co. KGaA	May 2021	-	26,974
ProCredit Holding AG & Co. KGaA	June 2021	-	18,812
ProCredit Holding AG & Co. KGaA	July 2021	-	27,846
ProCredit Bank AG, Frankfurt am Main	June 2021	11,489	-
ProCredit Bank AG, Frankfurt am Main	June 2021	-	16,082
<b>Total liabilities with fixed interest rates</b>		<b>218,488</b>	<b>257,710</b>
<b>Liabilities with variable interest rates</b>			
European Bank for Reconstruction and Development (EBRD)	February 2024	49,791	47,177
European Bank for Reconstruction and Development (EBRD)	September 2023	30,813	30,790
GREEN FOR GROWTH FUND, SOUTHEAST EUROPE S.A., SICAV-SIF (GGF)	January 2019	-	32,755
ProCredit Bank AG, Frankfurt am Main	July 2024	29,183	21,442
Council of Europe Development Bank (CEB)	August 2021	6,162	8,657
Oesterreichische Entwicklungsbank AG (OEeB)	January 2026	37,242	-
Oesterreichische Entwicklungsbank AG (OEeB)	February 2024	35,028	-
ProCredit Holding AG & Co. KGaA	March 2019	-	9,242
ProCredit Holding AG & Co. KGaA	March 2019	-	16,285
ProCredit Holding AG & Co. KGaA	April 2019	-	33,176
<b>Total liabilities with variable interest rates</b>		<b>188,219</b>	<b>199,524</b>
<b>Total liabilities</b>		<b>406,707</b>	<b>457,234</b>

Below table shows maturity analysis of other borrowed funds as at 31 December 2019 and 31 December 2018 based on carrying amount.

<b>As at 31 December 2019 (in '000 GEL)</b>	<b>less than 1 year</b>	<b>1 - 5 years</b>	<b>More than 5 years</b>	<b>Total</b>
Other borrowed funds	43,338	311,329	52,040	<b>406,707</b>
<b>As at 31 December 2018 (in '000 GEL)</b>	<b>less than 1 year</b>	<b>1 - 5 years</b>	<b>More than 5 years</b>	<b>Total</b>
Other borrowed funds	132,371	295,897	28,966	<b>457,234</b>

Refer to Note 30 for the estimated fair value of other borrowed funds. The interest rate analysis is disclosed in Note 29. Information on related party balances is disclosed in Note 32.

**PROCREDIT BANK GROUP**  
**Notes to the Financial Statements - 31 December 2019**

**20. OTHER LIABILITIES**

**Consolidated and Separate**

in '000 GEL	31 December 2019	31 December 2018
Accounts payable	963	940
Other	182	190
<b>Total other financial liabilities</b>	<b>1,145</b>	<b>1,130</b>
Received prepayments and deferred fees from guarantees issued	294	192
<b>Total other liabilities</b>	<b>1,439</b>	<b>1,322</b>

Refer to Note 30 for the estimated fair value of other financial liabilities.

Note for the separate other liabilities is not materially different from consolidated note, hence one schedule is presented above which provides consolidated balances of other liability as at 31 December 2019 and 2018.

**21. INCOME TAXES**

The applicable income tax rate is 15% for Georgian companies. Income tax expenses recorded in profit or loss for the year comprise the following:

**Consolidated and Separate**

in '000 GEL	2019	2018
Current tax charge	3,756	4,857
Deferred tax charge (benefit)	965	(198)
<b>Income tax expense for the year</b>	<b>4,721</b>	<b>4,659</b>

Reconciliation between the expected and the actual taxation charge is provided below:

in '000 GEL	2019	2018
<b>Profit before tax</b>	<b>33,136</b>	<b>31,057</b>
Theoretical tax charge at statutory rate of 15%	4,970	4,659
Tax effect of items which are not deductible:		
– Non-tax deductible expenses/(income)/effects of change of tax legislation	(249)	-
<b>Income tax expense for the year</b>	<b>4,721</b>	<b>4,659</b>

The tax effect of the movements in the temporary differences is detailed below and is recorded at the rate of 15% (2018:15%).

in '000 GEL	31 December 2019	Charge to profit or loss	31 December 2018	Credit to profit or loss	1 January 2018
<b>Deferred tax on:</b>					
IFRS 9 adjustment as at 1 January					
Directly to retained earnings.	(100)	-	(100)	-	(100)
Allowances for losses on loans and advances to customers	1,535	655	880	249	631
Other temporary differences	169	310	(141)	(447)	306
<b>Total deferred tax liability</b>	<b>1,604</b>	<b>965</b>	<b>639</b>	<b>(198)</b>	<b>837</b>

There are no material unrecognised deferred tax assets or liabilities, or any taxes recognised directly in equity or other comprehensive income.

Note for the separate income tax is not materially different from the consolidated note, hence one schedule is presented above which includes consolidated balances related to income taxes as at and for the year ended 2019 and 2018.

**PROCREDIT BANK GROUP**  
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**22. SUBORDINATED DEBT**

**Consolidated and Separate**

The subordinated debt can be broken down as follows:

in '000 GEL	Due	31 December 2019	31 December 2018
<b>Subordinated debt with variable interest rates</b>			
Overseas Private Investment Corporation (OPIC)	December 2019	-	40,293
<b>Subordinated debt with fixed interest rates</b>			
ProCredit Holding AG & Co. KGaA	April 2025	21,913	20,504
ProCredit Holding AG & Co. KGaA	April 2025	7,305	6,835
ProCredit Holding AG & Co. KGaA	September 2028	16,096	15,346
<b>Sub-total: ProCredit Holding AG &amp; Co. KGaA</b>		<b>45,314</b>	<b>42,685</b>
<b>Total</b>		<b>45,314</b>	<b>82,978</b>

Creditors' claims to repayment of these liabilities are subordinated to the claims of other creditors. There is no obligation to repay early. In the case of liquidation or insolvency, these creditors will only be paid after the claims of all non-subordinated creditors have first been satisfied.

Refer to Note 30 for the disclosure of the fair value of subordinated debt. The interest rate analysis is disclosed in Note 29. Information on related party balances is disclosed in Note 32.

**23. SHARE CAPITAL AND SHARE PREMIUM**

Shareholder structure is as follows:

in '000 GEL (except for the number of shares)	31 December 2019			31 December 2018		
Shareholder	Size of stake in %	Number of shares	Amount of share capital	Size of stake in %	Number of shares	Amount of share capital
ProCredit Holding AG & Co. KGaA	100%	20,070,275	100,352	100%	17,782,963	88,915
<b>Total</b>	<b>100%</b>	<b>20,070,275</b>	<b>100,352</b>	<b>100%</b>	<b>17,782,963</b>	<b>88,915</b>

At 24 October 2019, Group and Bank Issued additional 2,287,312 ordinary shares, the par value per share is GEL 5.00. The purchase price per share is GEL 11.53

in '000 GEL (except for the number of shares)	Number of ordinary shares issued	Share capital Amount	Share premium Amount
<b>At 31 December 2018</b>	<b>17,782,963</b>	<b>88,915</b>	<b>36,388</b>
Issue of shares	2,287,312	11,437	14,936
<b>At 31 December 2019</b>	<b>20,070,275</b>	<b>100,352</b>	<b>51,324</b>

in '000 GEL (except for the number of shares)	Number of ordinary shares issued	Share capital Amount	Share premium Amount
<b>At 31 December 2018</b>	<b>17,782,963</b>	<b>88,915</b>	<b>36,388</b>
<b>At 31 December 2019</b>	<b>20,070,275</b>	<b>100,352</b>	<b>51,324</b>

**Dividends**

The holders of ordinary shares are entitled to receive dividends as declared from time to time and are entitled to one vote per share at annual and general meetings of the Bank. The Bank may determine the distribution of annual and interim profits in the form of dividends.

In 2019 dividend of GEL 26,373 thousand (GEL 1.3 per share) were declared and paid (2018: GEL 30,323 thousand, GEL 1.7 per share).

**PROCREDIT BANK GROUP**  
**Notes to the Financial Statements - 31 December 2019**

**24. NET DEBT RECONCILIATION**

**Consolidated and Separate**

The table below sets out an analysis of our debt and the movements in our debt for each of the periods presented. The debt items are those that are reported as financing in the statement of cash flows.

	<b>Liabilities from financing activities</b>			<b>Total</b>
	<b>Other borrowed funds</b>	<b>Subordinated debt</b>	<b>Lease Liabilities</b>	
<b>Balance at 1 January 2019</b>				
<b>Changes from financing cash flows</b>	457,234	82,978	1,778	541,990
Proceeds	169,416	-	-	169,416
Repayments	(245,018)	(43,229)	(711)	(288,958)
<b>Total changes from financing cash flows</b>	<b>(75,602)</b>	<b>(43,229)</b>	<b>(711)</b>	<b>(119,542)</b>
<b>The effect of changes in foreign exchange rates</b>	<b>25,205</b>	<b>5,692</b>	<b>-</b>	<b>30,897</b>
<b>Other changes</b>				
Interest expense	19,427	5,427	103	24,957
New lease liability			1,768	1,768
Interest paid	(19,557)	(5,554)	-	(25,111)
<b>Balance at 31 December 2019</b>	<b>406,707</b>	<b>45,314</b>	<b>2,938</b>	<b>454,959</b>

	<b>Liabilities from financing activities</b>		
	<b>Other borrowed funds</b>	<b>Subordinated debt</b>	<b>Total</b>
<b>Balance at 1 January 2018</b>			
<b>Changes from financing cash flows</b>	411,946	64,967	476,913
Proceeds	139,789	15,218	155,007
Repayments	(89,396)		(89,396)
<b>Total changes from financing cash flows</b>	<b>50,393</b>	<b>15,218</b>	<b>65,611</b>
<b>The effect of changes in foreign exchange rates</b>	<b>(5,583)</b>	<b>2,755</b>	<b>(2,828)</b>
<b>Other changes</b>			
Interest expense	19,220	1,954	21,174
Interest paid	(18,742)	(1,916)	(20,658)
<b>Balance at 31 December 2018</b>			
<b>Changes from financing cash flows</b>	<b>457,234</b>	<b>82,978</b>	<b>540,212</b>



**PROCREDIT BANK GROUP**  
**Notes to the Financial Statements - 31 December 2019**

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**25. NET INTEREST INCOME**

**Consolidated and Separate**

Included within “net interest income” are interest income and expenses, as well as the unwinding of premiums and discounts on financial instruments at amortised cost.

in '000 GEL

<b>Interest and similar income</b>	<b>2019</b>	<b>2018</b>
Loans and advances to customers	85,282	81,868
Cash and cash equivalents and due from banks	3,680	3,209
Investment in debt securities	1,920	1,262
<b>Total interest income</b>	<b>90,882</b>	<b>86,339</b>
<b>Interest and similar expenses</b>		
Customer accounts	(17,018)	(11,895)
Other borrowed funds	(19,427)	(19,220)
Subordinated debt	(5,427)	(1,954)
Due to banks	(735)	(1,663)
Lease liabilities	(103)	-
<b>Total interest expenses</b>	<b>(42,710)</b>	<b>(34,732)</b>
<b>Net interest income</b>	<b>48,172</b>	<b>51,607</b>

**26. FEE AND COMMISSION INCOME AND EXPENSES**

**Consolidated and Separate**

in '000 GEL

<b>Fee and commission income</b>	<b>2019</b>	<b>2018</b>
Payment transfers and cash transactions	4,074	3,842
Debit/credit card issuance fee	3,327	2,622
Account maintenance fee	3,708	3,581
Letters of credit and guarantees	1,551	1,359
Internet bank fee	24	67
SMS service fee	6	13
Other fee and commission income	103	102
<b>Total fee and commission income</b>	<b>12,793</b>	<b>11,586</b>
<b>Fee and commission expenses</b>		
Debit/credit card issuance fee	(5,989)	(4,697)
Account maintenance fee	(1,248)	(965)
Payment transfers and transactions	(112)	(112)
Service fee	(119)	(120)
Letters of credit and guarantees	(367)	(163)
<b>Total fee and commission expenses</b>	<b>(7,835)</b>	<b>(6,057)</b>
<b>Net fee and commission income</b>	<b>4,958</b>	<b>5,529</b>

The item “other fee and commission income” consists of transactions carried out on behalf of third parties, e.g. Western Union.

**PROCREDIT BANK GROUP**  
**Notes to the Financial Statements - 31 December 2019**

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**27. OTHER ADMINISTRATIVE EXPENSES**

**Consolidated and Separate**

Other administrative expenses include the following items:

in '000 GEL	2019	2018
Depreciation and amortization	5,658	4,764
Communication and IT expenses	4,706	4,910
Personnel recruitment, training and other staff-related expenses	2,916	2,753
Consulting services	2,544	2,493
Marketing, advertising and entertainment	1,831	1,387
Repair and maintenance	436	559
Transport	879	920
Security service	293	445
Insurances	318	319
Utilities and electricity	790	746
Consulting and legal services	775	22
Audit and other financial services	512	777
Office rent	135	910
Taxes other than on income	1,657	1,660
Other	1,127	326
<b>Total</b>	<b>24,577</b>	<b>22,991</b>

Administrative expenses above includes GEL 512 thousand (2018: GEL 311 thousand) fees incurred for audit and other professional services provided by Auditor/Audit Firm as defined in the Law of Georgia on Accounting, Reporting and Auditing.

Of the total personnel and administrative expenses, expenses of GEL 1,741 thousand were incurred on staff training and related activities during 2019 (2018: GEL 1,789 thousand).

In 2019 the monthly average number of persons employed by the Group and Bank was 341 people (2018: 331).

Breakdown of monthly average number of employees by categories is as follows:

	2019	2018
Senior Management	3	4
Middle Management	22	21
Other staff	242	241
Service contractors	74	65
<b>Total</b>	<b>341</b>	<b>331</b>

## **28. OTHER OPERATING INCOME AND EXPENSE**

### **Consolidated and Separate**

#### **(a) Other operating income**

in '000 GEL	<b>2019</b>	<b>2018</b>
Income from disposal of property, and equipment	1,769	925
Rental income from investment properties	1,239	952
Income from sale of repossessed properties	819	1,092
Other operating income	1,402	644
<b>Total</b>	<b>5,229</b>	<b>3,613</b>

#### **(b) Other operating expenses**

in '000 GEL	<b>2019</b>	<b>2018</b>
Expense related to write/sale off of repossessed property	1,268	334
Expenses related for deposit insurance fund	333	390
Expenses from disposal of property and equipment	227	809
Other operating expense	1,433	1,488
<b>Total</b>	<b>3,261</b>	<b>3,021</b>

## **29. FINANCIAL RISK AND CAPITAL MANAGEMENT**

### **Consolidated and Separate unless otherwise indicated.**

#### **Management of the Overall Group and Bank Risk Profile – Capital Management**

##### **Objectives**

Overall, the Group and Bank is not allowed to take on more risk than it is capable of bearing. The capital management of the Group and Bank has the following objectives:

- Ensuring that the Group and Bank is equipped with a sufficient volume and quality of capital at all times to cope with (potential) losses arising from different risks even under extreme circumstances.
- Ensuring full compliance by the Bank with external capital requirements set by the regulator of the Georgian banking sector.
- Meeting the internally defined minimum capital adequacy requirements.
- Enabling the Group and Bank to implement its plans for growth while following its business strategy.

##### **Processes and procedures**

The capital management of the Group and Bank is governed by the Policy on Capital Management and the Policy on ICAAP (Internal Capital Adequacy Process). To ensure that the above stated objectives are met, the Group and Bank uses four indicators. Aside from regulatory and Basel III/Capital Requirements Regulation (CRR) ratios, the Tier1 leverage ratio and ICAAP are monitored on a monthly basis by the General Risk Unit and the Parent's General Risk Management Committee.

##### **Compliance with external and internal capital requirements**

External minimum capital requirements are imposed and monitored by the local banking supervision authorities of Georgia. Capital adequacy is calculated and reported to the members of the Group and Bank General Risk Management Committee on a monthly basis. These reports include rolling forecasts to ensure not only current but also future compliance (quarterly).

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As at 31 December 2019 the Group and Bank was in compliance with the regulatory capital adequacy requirements imposed by the NBG according to the guidelines of the Basel Committee (Basel II /III). The following table shows the capital adequacy ratios as calculated in accordance with those requirements:

<b>As at 31 December 2019 (Pillar I + Pillar II)</b>	<b>2019</b>	<b>2018</b>
Tier 1 Capital /RWA (required to be above 11.57%)	15.20%	13.37%
Tier 1 + Tier 2 Capital /RWA (required to be above 15.85%)	19.82%	17.79%

NBG introduced Pillar II buffers which were to be maintained from December, 2017. As of 31 December 2019 the minimum requirements including set buffers for Tier 1 equals to 11.57% and for Regulatory capital 15.88% of the total risk weighted assets. Unhedged credit risk is excluded from total risk weighted assets for Pillar I and added as a buffer.

Additionally, capital adequacy is monitored by using a uniform capital adequacy calculation across the Parent in compliance with the Basel III requirements as set forth under the European Capital Requirements Directive and Capital Requirements Regulation (CRR). The following table shows the Basel III / CRR capital adequacy ratios of the Group and Bank:

**Consolidated and Separate:**

<b>As at 31 December</b>	<b>2019*</b>	<b>2018*</b>
Tier 1 Capital / RWA	18.57%	16.25%
Tier 1 + Tier 2 Capital / RWA	22.64%	20.75%

in '000 GEL

<b>As at 31 December</b>	<b>2019*</b>	<b>2018*</b>
Ordinary share capital	100,352	88,915
Share premium	51,324	36,388
Prior period retained earnings	60,636	64,560
Profit for first nine months	19,040	21,640
Less other adjustments	(23)	(30)
Less dividends budgeted for the next year	(26,373)	(30,323)
Less intangible assets	(544)	(1,287)
<b>Tier I capital</b>	<b>204,412</b>	<b>179,863</b>
<b>Adjusted Tier I capital</b>	<b>204,412</b>	<b>179,863</b>
Subordinated loans	44,737	49,854
<b>Tier II capital</b>	<b>44,737</b>	<b>49,854</b>
<b>Total regulatory capital</b>	<b>249,149</b>	<b>229,717</b>

in '000 GEL

<b>As at 31 December</b>	<b>2019*</b>	<b>2018*</b>
RWA on balance	954,145	953,238
RWA off balance	24,424	19,578
RWA from open currency position	1	492
RWA from operational risk	121,776	133,678
<b>Total RWA</b>	<b>1,100,346</b>	<b>1,106,986</b>

\* These amounts are unaudited.

The Group and Bank uses a combination of straight equity and subordinated debt, mainly issued by the Parent for capital management purposes.

With respect to leveraging, a lower limit for the ratio of Tier 1 capital to recognized and unrecognized exposures (Tier 1 leverage ratio) was introduced in 2011 according to which the leverage ratio of the Group and Bank should not fall below 5%. As at 31 December 2019 and 2018 the Group and Bank's leverage ratio was above 10%.

**PROCREDIT BANK GROUP**  
**Notes to the Financial Statements - 31 December 2019**

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**ICAAP**

In addition to regulatory capital ratios, the Group and Bank assesses its capital adequacy by using the concept of ICAAP to reflect the specific risk profile of the Group and Bank, i.e. comparing potential losses arising from its operations with its risk bearing capacity.

The risk bearing capacity of the Group and Bank is defined as equity (net of intangibles) plus subordinated debt with the maturity of over one year, which amounted to GEL 259 million as at 31 December 2019 (2018: GEL 227 million). The Resources Available to Cover Risk (RAAtCR) was set at 60% of the risk-taking potential, i.e. GEL 136 million, unaudited for 2019 (2018: GEL 136 million, unaudited). For calculating potential losses in the different risk categories the following concepts are used:

- Credit risk (clients): Based on a regularly updated migration analysis on the loan portfolio, the historical loss rates are calculated and applied to the current loan portfolio as well as the off-balance portfolio to calculate potential loan losses;
- Counterparty risk: The calculation of potential losses due to counterparty risk is based on the probability of default arising from the respective international rating of the counterparty or its respective country of operation;
- Market risks: Whereas historical currency fluctuations are statistically analysed and the highest variances (99% confidence level) are applied to current currency positions, interest rate risk is calculated by determining the 12-months interest earnings at a standard interest rate shock for EUR/USD (two percentage points, Basel interest rate shock) and higher (historical) shock levels for local currency;
- Operational risk: The Basel II Standard approach is used to calculate the respective value.

The volume of economic capital to cover credit risk stayed stable as at 31 December 2019 and 2018. The underlying portfolio quality showed improvement throughout 2018. Counterparty, interest rate and currency risk limit utilisation remained low. All risks combined, as quantified by the methods established in the Group and Bank Standards for Bank ICAAP, are below 60% of the Group and Bank's total risk taking potential as defined. Other risks have been assessed as not sufficiently relevant for the Group and Bank or as relevant, but not quantifiable.

The table below shows the distribution of the RAAtCR among the different risk categories as determined by the Parent's Risk Management Committee and the level of utilisation for the Group and Bank as at the end of December 2019. The economic capital required to cover operational risk is calculated according to the Basel II standard approach.

<b>Risk Factor</b>	<b>Risk Detail</b>	<b>Limit (in %)*</b>	<b>Limit (in '000 GEL)*</b>	<b>Actual (in '000 GEL)*</b>	<b>Limit Used (in % of risk bearing capacity)*</b>
Credit Risk (Clients)	Credit Risk (Clients)	33.0%	85,373	48,199	18.6%
Counterparty Risk	Commercial Banks	5.0%	12,935	2,689	1.0%
Market Risk	Interest Rate Risk	10.0%	25,871	14,462	5.6%
Market Risk	Currency Risk	2.0%	5,174	294	0.1%
Operational Risk	Operational Risk	10.0%	25,871	9,742	3.8%
<b>Resources Available to Cover Risk</b>		<b>60.0%</b>	<b>155,224</b>	<b>75,386</b>	<b>29.1%</b>

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As at the end of December 2018 the distribution of RAtCR was as follows:

<b>Risk Factor</b>	<b>Risk Detail</b>	<b>Limit (in %)*</b>	<b>Limit (in '000 GEL)*</b>	<b>Actual (in '000 GEL)*</b>	<b>Limit Used (in % of risk bearing capacity)*</b>
Credit Risk (Clients)	Credit Risk (Clients)	33.0%	74,844	37,757	16.6%
Counterparty Risk	Commercial Banks	5.0%	11,340	1,997	0.9%
Market Risk	Interest Rate Risk	10.0%	22,680	7,944	3.5%
Market Risk	Currency Risk	2.0%	4,536	225	0.1%
Operational Risk	Operational Risk	10.0%	22,680	10,694	4.7%
<b>Resources Available to Cover Risk</b>		<b>60.0%</b>	<b>136,080</b>	<b>58,617</b>	<b>25.8%</b>

\* These amounts are unaudited.

**Management of individual risks**

In 2019, the Group and Bank further developed the policies and tools in managing of individual risks that serve the further enhancement of the risk management of the Group and Bank. In particular, strengthened processes were introduced for the management of:

- (a) Credit risk
- (b) Liquidity risk.
- (c) Market risk.
- (d) Operational risk
- (e) Anti-money laundering activities

The Group and Bank places emphasis on a general understanding of the factors driving risk and an ongoing analysis and group-wide discussion of possible developments/scenarios and their potential adverse impacts. The objectives of risk management include ensuring that all material risks are recognised in a timely manner, understood completely and managed appropriately. This includes, for example, ensuring that no products or services are offered unless they are thoroughly understood by all parties and can be properly managed.

Deviations from limits used for individual risks within which the Group and Bank positions its own risk strategies are only allowed upon approval of the Parent's General Risk Management Committee, but under consideration of being in compliance with stricter limits (e.g. in cases where such limits are stipulated by local regulations).

**(a) Credit risk**

Credit risk is defined as the danger that the party to a credit transaction will not be able, or will only partially be able, to meet its contractually agreed obligations towards the Group and Bank. As house bank for small and medium businesses, ProCredit banks are lending institutions in which loans to customers dominate statement of financial position. Consequently, customer credit risk is the most important risk that the Group and Bank faces.

The following table shows the maximum exposure to credit risk:

Credit risk is defined as the risk of losses due to a potential non-fulfilment of the contractual payment obligations associated with a customer credit exposure.

## **PROCREDIT BANK GROUP**

### **Notes to the Financial Statements - 31 December 2019**

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The management of credit risk from customer credit exposures is based on a thorough implementation of the following lending principles:

- analysis of the debt capacity of borrowers.
- documentation of the credit risk assessments, assuring that the analysis performed can be understood by knowledgeable third parties.
- avoidance of over indebtedting the Group and Bank's borrowers.
- building a personal and long term relationship with the client and maintaining regular contact.
- regular monitoring of borrower's capacity.
- monitoring of loan repayment, fulfilment of covenants.
- practising effective arrears management.
- exercising strict collateral collection in the event of default.
- investing in well-trained and highly motivated staff implementing carefully designed and well-documented processes.
- application of the "four-eyes principle".

The differentiation between individually significant and insignificant credit exposures leads to distinct processes in lending for the different types of credit exposures. The processes are distinguished mainly in terms of segregation of duties; the information collected from the clients, ranging from audited financial statements to self-declarations; the key criteria for credit exposure decisions based on the financial situation of the borrower. All credit decisions are taken by a credit committee consisting representatives of front and back office staff members.

The granularity of the credit exposure portfolio is an effective credit risk mitigating factor. The core business of the Group and Bank, lending to small and medium enterprises, necessitated a high degree of standardisation in lending processes and ultimately led to a high degree of diversification of these exposures in terms of geographic distribution and economic sectors.

Nevertheless, lending to medium-sized enterprises, i.e. larger credit exposures exceeding the threshold of EUR 500,000 constitutes a supplementary area of the Group and Bank's business in terms of its overall strategic focus. Many of these clients are dynamically growing enterprises that have been clients of the Group and Bank for many years.

Nonetheless, the higher complexity of these businesses requires an appropriate analysis of the business, the project that is to be financed and any connected entities. A strict division of front and back office functions is applied and requirements for both documentation and collateral are typically more stringent.

Overall, the loan portfolio of the Group and Bank includes 355 borrower group credit exposures of more than USD 250,000 (2018: 364 borrower group credit exposures).

The quality of the loan portfolio is monitored on an ongoing basis.

The central element of IFRS 9 Impairment Model approach for the Group and Bank is the expected credit loss model for the recognition and measurement of impairment.

The model requires the recognition of expected credit losses in a timely manner to ensure that the amount of expected credit losses recognised at each reporting date reflects the changes in the credit risk of the financial instruments.

As such, the model is forward-looking and it replaces the incurred loss model for recognition of credit losses, by recognising credit losses not necessarily triggered by a potential loss event.

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Specifically, the model addresses the IFRS 9 requirements on measurement of expected credit losses based on reasonable and supportable information that is available without undue cost or effort, including historical, current and forecasted information.

Credit risk in the context of the calculation of loan loss provisions is quantified by the expected loss due to client default risk. In general, the expected loss (*EL*) is determined by the exposure at default (*EAD*), the probability of a default (*PD*), and the loss rate (*LGD*):

$$ECL = EAD \times PD \times LGD.$$

#### **Exposure at default:**

- Only a part of the off-balance amount might be used in the case of a default. This is quantified by the credit conversion factors (CCF).
- All or a part of the total exposure might be repaid prematurely within the considered time period. This situation is quantified by the methods for full and partial prepayments.

#### **Probability of default:**

- The PDs are specified for the relevant time horizon (one year or lifetime). In particular, there is an adaption for maturities below one year.
- PDs are defined for all risk-relevant sub-portfolios (like business, private, or restructured clients), and depend on several client characteristics (like the risk classification for business clients).
- PDs are specified as point-in-time (PiT) forecasts, that is, they take into account the macroeconomic outlook of the upcoming period, and time trend.
- The uncertainty inherent in the macroeconomic outlook of the upcoming period is addressed by considering several macroeconomic scenarios, using them to derive alternative PiT PD forecasts, and applying a weighted average of them as the final parameter for the LLP calculation.

#### **Loss given default:**

- LGDs are specified by client exposure size classes. The estimates are averages of cured and non-cured and of collateralized and non-collateralized loss defaulted exposures.<sup>1</sup>
- As PDs, LGDs are specified as weighted averages of PiT forecasts based on different scenarios of the macroeconomic outlook.

#### **Loans and advances to customers**

Loans and advances to customers are recorded when the Group and Bank advances money to purchase or originate a loan due from a customer. Based on the business model and the cash flow characteristics, the Group and Bank classifies loans and advances to customers into AC category.

Impairment allowances are determined based on the forward-looking ECL models. Note 29 provides information about inputs, assumptions and estimation techniques used in measuring ECL, including an explanation of how the Group and Bank incorporates forward-looking information in the ECL models.

#### Increase of loss allowances

For the recognition of loss allowances, a three-stage model is used based on expected credit losses.

- Stage 1: All financial assets are generally classified as “Stage 1” at initial recognition except for purchased or originated credit impaired (POCI) assets which are treated and reported separately within Stage 3. The Group and Bank establishes loss allowances in an amount equivalent to the 12 month expected credit losses, insofar as there has not been a significant increase in credit risk since initial recognition. For exposures with a remaining maturity of less than 12 months, the used probability of default (PD) reflects the remaining maturity.



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- Stage 2: If the credit risk increases significantly, then “Stage 2” classification is assigned, and loss allowances are established in an amount equivalent to the lifetime expected credit losses.
- Stage 3: Defaulted financial assets are assigned to “Stage 3” and loss allowances are likewise established in an amount equivalent to the lifetime expected credit losses considering a 100% probability of default (lifetime ECL credit impaired). For significant exposures, risk provisioning is determined on the basis of recoverable cash flows. For insignificant exposures, loss allowances are determined on the basis of portfolio-based parameters. Stage 3 also includes financial assets which are already impaired at initial recognition (“POCI”). These are measured initially at fair value and without loss allowances. Regardless of future changes in the credit risk, POCI assets remain in Stage 3 until their disposal.

This model outlines three stages based on changes in the exposure’s credit risk since the date of initial recognition.

**Stage 1** includes exposures that have not had a significant increase in credit risk since initial recognition or that have low credit risk at the reporting date, including those that transfer back from Stage II due to decrease in credit risk. For these exposures, one-year expected credit losses are recognised in the profit or loss and a loss allowance is established. One-year expected losses refer to the expected credit losses that result from default events possible within 12 months after the reporting date.

Stage 1 comprises financial assets for which credit risk has not significantly increased since initial recognition as well as those showing low credit risk as of the reporting date or for which no triggers for Stage 2 or 3 allocation apply. Assets are allocated in Stage 1 upon initial recognition except for purchased or originated credit impaired (POCI) assets which are treated and reported separately within Stage 3. For assets in Stage 1, the expected credit losses arising from possible default events within the 12 months following the reporting date (12 month ECL) are recognised as expenses. For exposures with a remaining maturity of less than 12 months, the used probability of default (PD) reflects the remaining maturity.

Credit exposures are not considered to have low credit risk simply because of the value of collateral if the loan would not be considered low credit risk without that collateral. Loan contracts are also not considered to have low credit risk simply because they have a lower risk of default than other credit products or relative to the credit risk of the jurisdiction within which an entity operates.

All exposures in this stage consist of the portfolio that does not show any signs of increased credit risk

**Stage 2** includes exposures that have had a significant increase in credit risk since initial recognition (unless they have low credit risk at the reporting date) and there is no objective evidence of impairment. For these assets, lifetime expected losses are recognised. Lifetime expected losses are the expected credit losses that result from all possible default events over the expected life - maturity of a loan.

Stage 2 comprises financial assets for which credit risk has significantly increased since initial recognition, but for which there is no objective indication of impairment. This assessment takes account for appropriate and plausible information. Loss allowances are established in an amount equivalent to the expected credit losses over the entire remaining maturity, i.e. lifetime expected losses (lifetime ECL not credit impaired).

The significant increase in credit risk is established based on both quantitative and qualitative information

Based on the comparison of the remaining lifetime PD of an exposure at each reporting date against its remaining lifetime PD at the date of origination. The loss parameters are based on the internal risk classification system for the rated exposures. A SICR occurs if the difference in PDs exceeds a pre-defined threshold (the threshold is specified as a separate parameter, predetermined threshold for each risk class is set as 2.5) and the respective asset will be transferred from Stage 1 to Stage 2. Inversely, a transfer from Stage 2 to 1 is possible when the associated credit risk is reduced significantly.

When at least one of the following events is detected:

- customer is in arrears more than 30 days (including PAR 30 during month) but less than 90 days
- significant worsening of the financial situation of the customer resulting in a downgrade of the risk classification to 6 or 7
- standard or watch restructuring event(s)

After being transferred into Stage 2, the lifetime expected credit loss must be determined.

**Stage 3** includes exposures that have objective evidence of impairment at the reporting date. For these assets, lifetime expected losses are recognised and interest revenue is calculated on the net carrying amount (gross carrying amount adjusted for the loss allowance).

Stage 3 includes all exposures that are credit impaired as of the reporting date. The respective calculation of loss allowances is performed based on the lifetime expected credit losses considering a 100% probability of default (lifetime ECL credit impaired).

An exposure is considered as credit impaired and transferred to Stage 3 when the following or similar characteristics apply at the reporting date:

- client is in arrears more than 90 days
- qualitative and quantitative criteria based on which the bank considers the clients' unlikeliness to pay in full without realising collateral
- client is assigned to Risk Classification 8
- impaired restructuring event(s)
- bankruptcy procedure is initiated
- the bank has started legal proceedings against the client
- credit fraud event
- other signs of impairment indicating that full repayment from the client cannot be expected.

After being transferred into Stage 3, the lifetime expected credit loss must be determined.

### **Individually insignificant credit exposures**

For individually insignificant credit exposures showing signs of impairment, an individualised impairment test is typically not performed, as the operational costs do not justify an extensive impairment test for each of these clients. Instead, the assessment of expected losses is based on the methodology as defined in the Description of the credit risk model for LLPs. Only in exceptional cases may the bank perform an impairment test for individually insignificant credit exposures through an assessment for specific individual impairment.

Individually significant credit exposures are monitored by the respective Credit Committee and Business Client Adviser or Credit Analyst. For such credit exposures, the committee assesses whether objective evidence of impairment exists, i.e.:

- An impaired restructuring event
- The bank has initiated court procedures.
- Bankruptcy proceedings have been initiated.
- Past due days in arrears of 90 days.
- A credit fraud event.
- A downgrade of risk classification to 8 for all clients with small and medium credit exposures.
- Originated Credit Impairment exposures (POCI) at initial recognition.
- Other signs of impairment.

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For individually significant exposures a discounted cash flow approach is applied in order to calculate the respective ECL. Expectations regarding both the timing and the amount of future cash flows are conservative and adequately reflects the uncertainties of the future. In the assessment and measurement of ECL the Group and Bank is using at least two different scenarios based on forward-looking information including macroeconomic factors. This concerns any net expected future payments from the customer and its guarantor (s), as well as expected net recoveries on collateral. The expected direct costs of collateral recoveries is based on actually incurred costs in previous, comparable cases as well as on external standards such as established costs for presenting cases to the court, execution costs as percentages of the collateral value etc. The expected cash inflows from the customer or its guarantor(s) are based on the assessment of the payment capacity of the respective customer or guarantor(s). Additionally, in using multiple scenarios, the client's payment capacity should be affected by one or several relevant macroeconomic indicators.

In cases where a relevant financial analysis showing the payment capacity of the customer or guarantor(s) is not available, only cash flows from collateral are assumed. The amount that can be recovered on collateral and the expected time until recovery is estimated based on the previous relevant experience of the Bank with collateral enforcement on comparable collateral items and forward looking information formed on projected macroeconomic data and the forecasted collateral price. At least two different scenarios are used for focused cash flows received from collateral sales.

If the Bank's internal data is not reliable or comparable enough, the Bank uses sufficient and reliable information from external sources that supports the assumptions used for the timing and value of expected future cash flows from collateral.

**Risk classification process**

The risk classification system for small and medium clients comprises an important part of the process for determining an increase in credit risk and, consequently, the classification of the loan portfolio. Prior to initial disbursement, each credit exposure is assigned one of the risk classes – 1 to 8 (1 being the best and 8 the worst). Assigning a risk class implies an extensive analysis of multiple qualitative and quantitative criteria at client level, which are assessed in regular basis to identify the increase in credit risk through the classes.

ProCredit grants new loan exposures to performing clients. Additional exposures for clients with risk classification 6, 7 or 8 are not allowed.

	<b>Underperforming loan portfolio</b>	<b>Default loan portfolio</b>
<b>At 31 December 2019</b>	<b>3.3%</b>	<b>2.8%</b>
<b>At 31 December 2018</b>	<b>2.3%</b>	<b>2.7%</b>

According to the policies of the Bank, usually only short-term credit exposures may be issued without being well collateralised. Credit exposures with a higher risk profile are always covered with solid collateral, typically real estate.

The Group and Bank's policy on the treatment of repossessed property requires that all goods obtained due to customers' defaults be sold to third parties in order to avoid any conflict of interest arising from the below-market valuation of collateral. Also, repossessed property is sold at the highest possible price via public auction, and any remaining balance after the payment of principal, interest and penalty is credited to the customer's account. Most repossessed property consists of land and buildings. A smaller part is composed of inventory, equipment and vehicles.

The structure of the loan portfolio is regularly reviewed by the Credit Risk Department, in order to identify potential events which could have an impact on large portion of the loan portfolio (common risk factors) and, if necessary, limit the exposure towards certain sectors of the economy.

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The Group's and Bank's loan portfolio (gross) grouped according to the common risk factors is as follows:

in '000 GEL At 31 December 2019	Agriculture, Wholesale forestry and and Trade	Agriculture, fishing	Production	Transportation and storage	Other economic activities	Housing	Investment loans	Others	Total
< 50,000 USD	24,050	3,020	11,220	2,769	26,493	33,385	3,203	129	104,269
50,000 to 250,000 USD	136,278	16,944	60,433	12,047	132,138	67,980	351	-	426,171
>250,000 USD	181,180	18,629	81,338	7,186	272,475	2,432	-	-	563,240
<b>Total</b>	<b>341,508</b>	<b>38,593</b>	<b>152,991</b>	<b>22,002</b>	<b>431,106</b>	<b>103,797</b>	<b>3,554</b>	<b>129</b>	<b>1,093,680</b>

in '000 GEL At 31 December 2018	Agriculture, Wholesale forestry and and Trade	Agriculture, fishing	Production	Transportation and storage	Other economic activities	Housing	Investment loans	Others	Total
< 50,000 USD	31,614	2,655	11,801	3,562	29,158	36,573	3,405	225	118,993
50,000 to 250,000 USD	145,150	14,105	61,871	14,961	145,519	71,029	340	-	452,975
>250,000 USD	169,598	29,737	69,200	2,849	203,609	2,851	-	-	477,844
<b>Total</b>	<b>346,362</b>	<b>46,497</b>	<b>142,872</b>	<b>21,372</b>	<b>378,286</b>	<b>110,453</b>	<b>3,745</b>	<b>225</b>	<b>1,049,812</b>

The Group and Bank follows a guideline that limits concentration risk in its loan portfolio by ensuring that large credit exposures (those exceeding 10% of regulatory capital) must be approved by the Parent's Credit Risk Committee and Supervisory Board. No single large credit exposure may exceed 25% of the Group and Bank's regulatory capital.

Larger credit exposures are analysed and monitored, both by the responsible employees through regular monitoring activities enabling early detection of risks, and through the regular reviews carried out by the Credit Committee. Information about related parties of the borrowers is typically collected prior to lending.

Expected credit loss model requires the recognition of expected credit losses in a timely manner to ensure that the amount of expected credit losses recognised at each reporting date reflects the changes in the credit risk of the financial instruments.

As such, the model is forward-looking and it replaces the incurred loss model for recognition of credit losses, by recognising credit losses not necessarily triggered by a potential loss event.

Specifically, the model addresses the IFRS 9 requirements on measurement of expected credit losses based on reasonable and supportable information that is available without undue cost or effort, including historical, current and forecasted information. This model outlines three stages based on changes in the exposure's credit risk since the date of initial recognition.

**Credit risk from interbank placements and issuer risk**

*Conceptual risk management framework*

The objective of counterparty and issuer risk management is to prevent the Group and Bank from incurring losses caused by the unwillingness or inability of a financial counterparty (e.g. a commercial bank) or issuer to fulfil its obligations towards the Group and Bank. This type of risk is further divided into:

- principal risk: the risk of losing the amount invested due to the counterparty's failure to repay the principal in full on time;
- replacement risk: the risk of loss of an amount equal to the incurred cost of replacing an outstanding deal with an equivalent one on the market;
- settlement risk: the risk of loss due to the failure of a counterparty to honour its obligation to deliver assets as contractually agreed;
- issuer risk: the probability of loss resulting from the default and insolvency of the issuer of a security;
- market price risk: the risk of loss due to the drop of the market value of securities as interest rates increase.

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Counterparty and issuer risks evolve especially from the Group and Bank's need to invest its liquidity reserve, to conclude foreign exchange transactions, or to buy protection on specific risk positions. Excess liquidity is placed in the interbank market with short maturities, typically up to three months. Foreign exchange transactions are also concluded with short maturities, typically up to two days. Derivative contracts, which are used to protect the Group and Bank against foreign currency risk, may have maturity of up to one year. Furthermore, as a result of the Group and Bank's efforts to finance its lending activities with retail deposits, there is also an exposure towards the NBG. This is because the NBG requires banks operating in its territory to hold a mandatory reserve on a NBG account, the size of which depends on the amount of deposits taken from customers or other funds used to fund the Group and Bank's operations.

The counterparty and issuer risks are managed according to the Counterparty Risk Management Policy (incl. Issuer Risk), which describes the counterparty/issuer selection and the limit setting process, as well as by the Treasury Policy, which specifies the set of permissible transactions and rules for their processing. As a matter of principle, only large international banks of systemic importance and, for local currency business, local banks with a good reputation and financial standing are eligible counterparties. As a general rule, the Group and Bank applies limits of up to 10% of its regulatory capital for exposures to banking groups in non-OECD countries and up to 25% for those in OECD countries with maximum remaining maturity of 3 months. Higher limits and longer maturities are subject to approval by the Parent's General Risk Management Committee.

The Asset Liability Committee (ALCO) ensures that every counterparty is subject to a thorough analysis, typically conducted by the General Risk Unit in collaboration with the Compliance and Anti-Money Laundering (AML) Unit. If the counterparty is approved, a limit for the maximum exposure is set.

According to the Counterparty Risk Management Policy the Group and Bank is not supposed to conduct any speculative trading activities. However, for liquidity management purposes, the Group and Bank is allowed to buy and hold securities (treasury bills and certificates of deposits). The inherent issuer risk is managed by the provisions of the Treasury Policy. Among other requirements, the policy stipulates that the securities in GEL should preferably be issued by the Government of Georgia or the NBG, or in case of foreign currency by international and/or multinational institutions with very high credit ratings (i.e. an international rating of AA- or better).

The following table provides an overview of the types of counterparties and issuers with whom the Group and Bank concludes transactions.

in '000 GEL	2019	In %	2018	In %
<b>Banking groups</b>	<b>83,489</b>	<b>29%</b>	<b>32,142</b>	<b>13%</b>
OECD banks	43,370	15%	15,795	6%
Non-OECD banks	40,119	14%	16,347	7%
<b>NBG</b>	<b>197,312</b>	<b>69%</b>	<b>216,948</b>	<b>75%</b>
Mandatory reserve	175,926	62%	170,806	67%
Other exposures	21,386	7%	46,142	8%
<b>Government of Georgia</b>	<b>4,924</b>	<b>2%</b>	<b>4,943</b>	<b>12%</b>
Treasury bills	4,924	2%	4,943	12%
<b>Total counterparty and issuer exposure</b>	<b>285,725</b>	<b>100%</b>	<b>254,033</b>	<b>100%</b>

The exposure to the NBG is primarily related to the mandatory reserve requirement which makes up 62% (2018: 67%) of the Group's and Bank's counterparty and issuer exposure. The distribution of the NBG and government exposures across currencies can be seen in the following table:

in '000 GEL				
<b>31 December 2019</b>	<b>GEL</b>	<b>EUR</b>	<b>USD</b>	<b>Total</b>
<b>NBG</b>	<b>21,274</b>	<b>44,380</b>	<b>131,658</b>	<b>197,312</b>
Mandatory reserve	-	44,331	131,595	175,926
Balances at NBG excluding mandatory reserves	4,281	49	63	4,393
Certificates of deposits of NBG	16,993	-	-	16,993
<b>Government of Georgia</b>	<b>4,924</b>	<b>-</b>	<b>-</b>	<b>4,924</b>
	<b>26,198</b>	<b>44,380</b>	<b>131,658</b>	<b>202,236</b>

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in '000 GEL

**31 December 2018**

	<b>GEL</b>	<b>EUR</b>	<b>USD</b>	<b>Total</b>
<b>NBG</b>	<b>45,317</b>	<b>35,122</b>	<b>136,509</b>	<b>216,948</b>
Mandatory reserve	-	34,304	136,502	170,806
Balances at NBG excluding mandatory reserves	20,493	818	7	21,318
Certificates of deposits of NBG	24,824	-	-	24,824
<b>Government of Georgia</b>	<b>4,943</b>	<b>-</b>	<b>-</b>	<b>4,943</b>
	<b>50,260</b>	<b>35,122</b>	<b>136,509</b>	<b>221,891</b>

**(b) Liquidity risk**

“Liquidity risk’ is the risk that the Group and Bank will encounter difficulty in meeting obligations associated with its financial liabilities that are settled by delivering cash or another financial asset. Liquidity risk arises from mismatches in the timing and amounts of cash flows, which is inherent to the Group’s and Bank’s operations and investments.

The liquidity risk management (LRM) system is tailored to the specific characteristics of the Group and Bank. Portfolio of loans given comprises of large number of short and medium-term exposures to small and medium sized businesses. The majority of the loans are disbursed as annuity term loans and have low default rates. This leads to highly diversified, reliable cash inflows. The usage of financial markets instruments is low. All of these factors limit possible liquidity risk concentrations and warrant a relatively simple and straightforward LRM system.

Liquidity risk in the narrowest sense (risk of insolvency) is the danger that the Group and Bank will no longer be able to meet its current and future payment obligations in full, or in a timely manner. Liquidity risk in a broader sense (funding risk) is the danger that additional funding can no longer be obtained, or can only be obtained at increased market interest rates.

The ALCO determines the liquidity strategy of the Group and Bank and sets the liquidity risk limits. The Treasury and Cash Management Unit manage the Group and Bank’s liquidity on a daily basis and is responsible for the execution of the ALCO’s decisions. Compliance with strategies, policies and limits are constantly monitored by the General Risk Unit.

In addition to the requirements set by the local regulatory authorities, the standards that the Group and Bank applies in this area are guided by the Liquidity Risk Management Policy and the Treasury Policy. Both policies were first implemented by the Group and Bank in 2009 and are updated on an annual basis. These policies are also in line with the Principles for Sound Liquidity Risk Management defined by the Basel Committee on Banking Supervision EU regulation 575/2013 [Capital Requirement Regulation -CRR] and EU directive 2013/36/EU [Capital Requirement Directive - CRD IV]. Limit breaches and exceptions to these policies are subject to decisions of the Parent’s ALCO and Parent’s General Risk Management Committee.

The Treasury and Cash Management Unit manages liquidity on a daily basis using a cash flow analysis tool. This tool is designed to provide a realistic picture of the future liquidity situation. It includes assumptions about deposit and loan developments and helps to forecast liquidity risk indicators.

The key tools for measuring liquidity risks includes a forward looking liquidity gap analysis, which shows the contractual maturity structure of assets and liabilities and estimates future funding needs based on certain assumptions.

Starting with the estimation of future liquidity in a normal financial environment, the assumptions are increasingly tightened in order to analyse the Group and Bank’s liquidity situation in adverse scenarios (stress tests). Based on the gap analyses, a set of key liquidity risk indicators and early warning indicators are calculated on daily and monthly basis and are closely monitored.

The main indicator of short-term liquidity is the sufficient liquidity indicator (SLI), which compares the amounts of assets available and liabilities assumed to be due within the next 30 days. The indicator must be above 1, which implies that the Group and Bank has sufficient funds to repay the liabilities simulated to be due within

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the next 30 days. This is complemented by the indicators, which was implemented in 2018 – “survival period”, which is the time-period during which the bank can meet all its payments due without needing to generate additional (i.e. still not contracted) funds, i.e. the period within which the bank does not have negative liquidity gaps in any of the time-buckets. The defined minimum survival period limits is at least 90 days on total currency level, as well as on total hard currency level and local currency level.

The Group and Bank also analyses its liquidity situation from a more structural perspective, taking into account the liquidity gaps of the later time buckets and additional sources of potential liquidity. The respective key indicator is defined as the Liquidity Position. This analysis also takes into account credit lines which can be drawn by the Group and Bank with some time delay, and other assets which take some time to liquidate.

In addition to prescribing the close monitoring of these early warning indicators, the Liquidity Risk Management Policy also defines reporting triggers related to interbank market indicator, negative short-term liquidity gap, deposit concentration and Liquidity Coverage Ratio (set forth under Basel III). If one of the reporting triggers is passed the ALCO and the Parent’s ALCO or General Risk Management Committee must be involved in decisions on appropriate measures.

In order to safeguard the liquidity of the Group and Bank even in stress situations, the potential liquidity needs in different scenarios are determined. The result is analysed and on this basis the Group and Bank’s liquidity reserve target is determined by the ALCO. The results of these stress tests are also used to determine liquidity standby lines provided by the Parent to the Group and Bank if necessary.

The Group and Bank also aims to diversify its funding sources. Depositor concentrations are monitored in order to avoid dependencies on a few large depositors.

The Group and Bank also minimises its dependency on the interbank market. The Group and Bank’s policies stipulate that the total amount of interbank liabilities may not exceed 40% of its available lines and overnight funding may not exceed 4% of total liabilities. Higher limits need to be approved by the Parent’s ALCO.

The following tables show the remaining contractual maturities of the undiscounted financial assets and financial liabilities. The remaining contractual maturity is defined as the period between the reporting date and the contractually agreed due date of the asset or liability, or the due date of a partial payment under the contract for an asset or liability.

in '000 GEL At 31 December 2019	Up to 1 month	1 – 3 months	3 – 12 months	1 -5 years	More than 5 years	Total gross amount inflow (outflow)	Carrying amount
<b>Non-derivative Financial Assets</b>							
Cash and balances with the NBG (including mandatory reserve)	196,263	7,043	33,056	23,070	3,477	262,909	262,909
Due from banks	83,489	-	-	-	-	83,489	83,489
Loans and advances to customers	32,686	74,340	315,232	622,205	251,396	1,295,859	1,070,120
Investments in debt securities	17,000	-	5,007	-	-	22,007	21,917
Other financial assets	4,518	-	-	-	-	4,518	4,518
<b>Total Financial Assets</b>	<b>333,956</b>	<b>81,383</b>	<b>353,295</b>	<b>645,275</b>	<b>254,873</b>	<b>1,668,782</b>	<b>1,442,953</b>
<b>Non-derivative Financial Liabilities</b>							
Due to banks	1,218	69,189	-	-	-	70,407	70,407
Customer accounts	492,590	31,745	149,003	103,992	15,666	792,996	767,297
Other borrowed funds	4,550	6,732	41,552	347,697	57,504	458,035	406,707
Other financial liabilities	977	168	-	-	-	1,145	1,145
Lease liability	48	-	236	1,221	1,585	3,090	2,938
Subordinated debt	-	-	3,849	13,060	49,509	66,418	45,314
<b>Derivative liabilities</b>							
- Inflow	-	142,646	-	-	-	142,646	
- Outflow	-	(143,205)	-	-	-	(143,205)	1,258
<b>Total Financial Liabilities</b>	<b>499,383</b>	<b>107,275</b>	<b>194,640</b>	<b>465,970</b>	<b>124,264</b>	<b>1,391,532</b>	<b>1,295,066</b>
<b>Liquidity Gap</b>	<b>(165,427)</b>	<b>(25,892)</b>	<b>158,655</b>	<b>179,305</b>	<b>130,609</b>		
<b>Cumulative Liquidity Gap, excluding credit related commitments and guarantees</b>	<b>(165,427)</b>	<b>(191,319)</b>	<b>(32,664)</b>	<b>146,641</b>	<b>277,250</b>		
<b>Credit related commitments and guarantees</b>	<b>(97,422)</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>(97,422)</b>	

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in '000 GEL	Up to	1 – 3	3 – 12	1 -5	More	Total gross	Carrying
At 31 December 2018	1 month	months	months	years	than	amount inflow	Amount
					5 years	(outflow)	
<b>Non-derivative assets Financial Assets</b>							
Cash and balances with the NBG (including mandatory reserve)	279,212	7,119	30,723	18,206	3,388	338,648	338,648
Due from banks	32,164	-	-	-	-	32,164	32,143
Loans and advances to customers	38,642	72,075	293,429	638,859	186,521	1,229,526	1,023,256
Investments in debt securities	8,697	18,893	2,608	-	-	30,198	29,767
Other financial assets	4,120	-	-	-	-	4,120	4,120
<b>Derivative assets</b>							
- Inflow	-	-	56,668	-	-	56,668	
- Outflow	-	-	(55,240)	-	-	(55,240)	(224)
<b>Total Financial Assets</b>	<b>362,835</b>	<b>98,087</b>	<b>328,188</b>	<b>657,065</b>	<b>189,909</b>	<b>1,636,084</b>	<b>1,427,934</b>
<b>Non-derivative Financial Liabilities</b>							
Due to banks	18,991	13,810	39,397	-	-	72,198	71,608
Customer accounts	462,310	29,371	126,766	75,118	13,977	707,542	696,377
Other borrowed funds	35,320	36,877	60,187	295,227	37,375	464,986	457,234
Other financial liabilities	1,130	-	-	-	-	1,130	1,130
Subordinated debt	-	661	45,563	12,289	49,757	108,270	82,978
<b>Total Financial Liabilities</b>	<b>517,751</b>	<b>80,719</b>	<b>271,913</b>	<b>382,634</b>	<b>101,109</b>	<b>1,354,126</b>	<b>1,309,327</b>
<b>Liquidity Gap</b>	<b>(154,916)</b>	<b>17,368</b>	<b>56,275</b>	<b>274,431</b>	<b>88,800</b>		
<b>Cumulative Liquidity Gap, excluding credit related commitments and guarantees</b>	<b>(154,916)</b>	<b>(137,548)</b>	<b>(81,273)</b>	<b>193,158</b>	<b>281,958</b>		
<b>Credit related commitments and guarantees</b>	<b>(65,328)</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>(65,328)</b>	

The Group/Bank's capability to discharge its liabilities relies on its ability to realize an equivalent amount of assets within the same period of time.

As at 31 December 2019, total current accounts within 'Customer accounts' amounted to GEL 224,775 thousand (2018: GEL 221,694 thousand). Within amounts of the customer accounts for the period of the preceding two years on a monthly basis, current accounts end-of-month balances have not fallen below GEL 117,312 thousand (2018: GEL 141,208 thousand). Significant part of total current accounts represents current accounts from legal entities which historically are of long-term nature.

The Parent's financial risk management team together with the Group/Bank' risk management conducts historical analysis, annually to determine cash flow behavior of customer accounts. Based on the result of this analysis, the outflow rates are applied on customer accounts. The Group/Bank performs regular estimation and stress test analysis of liquidity position for all financial assets and liabilities including customer accounts. Based on expected liquidity analysis Bank maintains robust liquidity position for next 12 months from the date these Financial Statements are authorized for issues. The longer-term liquidity and funding needs are covered in the 5-year business plan.

As at 31 December 2019, the Group and Bank was in compliance with the sufficient liquidity indicator limit set at 1 according to the Liquidity Risk Management Policy as well, as with "survival period" limit set at 90 days.

As mentioned above, the Group and Bank also performs stress test calculations in order to safeguard its liquidity. The result is analysed and the Group and Bank's liquidity reserve target is determined by ALCO. The results of the stress tests are also used to determine liquidity stand-by lines provided by the Parent to the Group and Bank if necessary.

The Group and Bank aims to rely primarily on customer deposits for its funding. This source is supplemented by funding received from international financial institutions (IFIs), such as the CEB, OeEB, EIB and EBRD which provide earmarked funds under targeted financing programmes (e.g. for lending to SMEs). In order to further diversify its sources of funds, the Group and Bank also maintains relationships with other banks, especially for short-term liquidity lines. In addition, the Parent and also ProCredit Bank Germany provide short- and long-term funding.



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In order to maintain a high level of diversification among its customer deposits, the Group and Bank has implemented a deposit concentration indicator, which is the share of deposits of 5 largest non-financial customer depositors or of all non-financial customer depositors having more than 1% share in the total non-financial customer deposit portfolio which can be withdrawn in the next 30 days in the total non-financial customer deposits. Customers excluding financial institutional clients include all private individuals and legal entities, excluding financial institutional clients. Financial institutional clients are the ones which are assigned to the client category “Institutional” and sub-category “Financial and insurance activities”.

The table below shows the approximate distribution of funding sources as at 31 December 2019 and 2018. It shows that, as mentioned above, customer deposits are by far the largest source of funds. Other main sources of funding are liabilities to the companies under Parent’s control and IFIs.

<b>In %</b>	<b>31 December 2019</b>	<b>31 December 2018</b>
Liabilities to banks	-	1.4%
Customer deposits	59.3%	53.2%
Liabilities to the companies under Parent’s control	20.5%	24.4%
Liabilities to IFIs	19.9%	20.9%
Other liabilities	0.3%	0.1%

Overall, the Group and Bank considers its funding sources to be sufficiently diversified, especially given that the bulk of the funds are provided by a large number of customer deposits.

#### **I. Funding risk**

The business plan, which is reviewed annually, serves as the basis for determining medium-term funding needs in regard to both equity and debt financing for the Group and Bank. In order to ensure sufficient liquidity at all times, the Parent holds a liquidity reserve, which can be tapped in case of emergency.

The Group and Bank still considers funding risk to be low due to strong reliance on customer deposits as well as the fact that the Group and Bank continues to access funding from various international sources.

#### **(c) Market risk**

Market price risk for the Group and Bank is defined as currency risk (i) and interest rate risk (ii).

##### **i. Currency risk**

The assets and liabilities of the Group and Bank are denominated in more than one currency. If the assets and liabilities in one currency do not match, the Group and Bank has an open currency position (OCP) and is exposed to potentially unfavourable changes in exchange rates.

Due to the still developing financial market, a history of high inflation and exchange rate fluctuations a considerable part of private savings in Georgia is held in USD or EUR. Also, loans in USD and EUR which are available at (nominally) lower interest rates and have longer maturities (as compared to GEL loans) still play an important role in the financing of many of the country’s businesses. As a result, foreign currencies play a major role in the Group and Bank’s operations.

Currency risk management is guided by the Foreign Currency Risk Management Policy. This policy was first implemented by the Group and Bank in 2009 and is updated on an annual basis. Its adherence to this policy is constantly monitored by the Parent’s financial risk team at the group level, and amendments as well as exceptions to this policy are decided by the Parent’s ALCO or General Risk Management Committee.

The Treasury and Cash Management Unit is responsible for continuously monitoring the developments of exchange rates and foreign currency markets. The Treasury and Cash Management Unit also manages the currency positions of the Group and Bank on a daily basis. As a general principle, all currency positions should be kept as low as possible at end-of-day; long or short positions for speculative purposes are not permitted.

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According to the Treasury Policy, derivatives may only be used for hedging purposes to close positions of the Group and Bank as well as for liquidity purposes. Permissible foreign exchange derivatives are currency forwards (including non-deliverable forwards) and currency swaps. The Group and Bank's foreign currency exposures are monitored and controlled on a daily basis by the Treasury back office and General Risk Unit.

Developments in the foreign exchange markets and the currency positions are regularly reported to the ALCO, which is authorised to take strategic decisions with regard to Treasury activities. In cases where exceptions to the Group and Bank's policy may be necessary or violations to the limits may have occurred, the General Risk Unit reports to the Parent's ALCO or General Risk Management Committee and proposes appropriate measures.

The Group and Bank aims to keep currency positions as low as possible and ensures that an open currency position remains within the limits at all times. For the purpose of currency risk management the Group and Bank has established two levels of control: early warning indicators and limits. In cases where the positions cannot be brought back below 5% of the regulatory capital for a single currency, or 7.5% for the aggregate of all currencies, the bank's ALCO and the Parent's ALCO have to be informed and appropriate measures taken. This mechanism helps to ensure that the Group and Bank's total Open currency position (OCP) does not exceed 10% of regulatory capital. Exemptions from the limit or strategic positions are subject to approval by the Parent's ALCO or General Risk Management Committee.

The Group's OCPs were within the aforementioned limits as at 31 December 2019.

The following significant exchange rates applied during the year:

in GEL	Average rate 2019	Average rate 2018	Reporting date spot rate 31 December 2019	Reporting date spot rate 31 December 2018
USD 1	2.8168	2.5312	2.8646	2.6803
EUR 1	3.1535	2.9899	3.2181	3.0689

The following tables show the distribution of financial monetary assets and liabilities across its material operating currencies:

in '000 GEL			Other		
As at 31 December 2019	EUR	USD	currencies	GEL	Total
<b>Assets</b>					
Cash and balances with the NBG (including Mandatory reserve deposits with NBG)	66,175	171,044	1,074	24,616	262,909
Due from banks	632	43,845	-	39,012	83,489
Investments in debt securities	-	-	-	21,917	21,917
Loans and advances to customers	403,164	395,345	-	271,611	1,070,120
Other financial assets	1,202	1,979	-	1,337	4,518
<b>Total financial assets</b>	<b>471,173</b>	<b>612,213</b>	<b>1,074</b>	<b>358,493</b>	<b>1,442,953</b>
<b>Liabilities</b>					
Due to banks	69,834	573	-	-	70,407
Customer accounts	132,595	454,336	475	179,891	767,297
Other borrowed funds	109,718	266,078	-	30,911	406,707
Other financial liabilities	360	88	-	697	1,145
Lease liability	194	2,717	-	27	2,938
Subordinated debt	16,096	29,218	-	-	45,314
<b>Total financial liabilities</b>	<b>328,797</b>	<b>753,010</b>	<b>475</b>	<b>211,526</b>	<b>1,293,808</b>
<b>Net position</b>	<b>142,376</b>	<b>(140,797)</b>	<b>599</b>	<b>146,967</b>	<b>149,145</b>
<b>The effect of derivatives</b>	<b>(143,205)</b>	<b>142,546</b>	<b>100</b>	<b>-</b>	<b>(559)</b>
<b>Net position after derivatives</b>	<b>(829)</b>	<b>1,749</b>	<b>699</b>	<b>146,967</b>	<b>148,586</b>

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in '000 GEL					
<b>As at 31 December 2018</b>	<b>EUR</b>	<b>USD</b>	<b>Other currencies</b>	<b>Local currency</b>	<b>Total</b>
<b>Assets</b>					
Cash and balances with the NBG (including mandatory reserve)	73,231	221,671	640	43,106	338,648
Due from banks	1,028	16,149	-	14,966	32,143
Investments in debt securities	-	-	-	29,767	29,767
Loans and advances to customers	180,399	608,542	-	234,315	1,023,256
Other financial assets	1,245	1,199	-	1,676	4,120
<b>Total financial assets</b>	<b>255,903</b>	<b>847,561</b>	<b>640</b>	<b>323,830</b>	<b>1,427,934</b>
<b>Liabilities</b>					
Due to banks	56,610	14,998	-	-	71,608
Customer accounts	116,542	407,602	284	171,949	696,377
Other borrowed funds	11,858	414,488	-	30,888	457,234
Other financial liabilities	546	13	-	571	1,130
Subordinated debt	15,347	67,631	-	-	82,978
<b>Total financial liabilities</b>	<b>200,903</b>	<b>904,732</b>	<b>284</b>	<b>203,408</b>	<b>1,309,327</b>
<b>Net position</b>	<b>55,000</b>	<b>(57,171)</b>	<b>356</b>	<b>120,422</b>	<b>118,607</b>
<b>The effect of derivatives</b>	<b>(55,240)</b>	<b>56,668</b>	<b>-</b>	<b>-</b>	<b>1,428</b>
<b>Net position after derivatives</b>	<b>(240)</b>	<b>(503)</b>	<b>356</b>	<b>120,422</b>	<b>120,035</b>

In order to identify maximum expected losses associated with currency fluctuations (USD and EUR), seven years of historical currency movements are statistically analyzed. Historical rate of fluctuation is used to stress the net foreign currency position subject to 99% and 95% confidence levels. 1-year holding period are applied to current currency positions:

in '000 GEL		
<b>As at 31 December 2019</b>	<b>95% confidence</b>	<b>99% confidence</b>
Maximum loss (VaR)	(125)	(113)
Average loss in case confidence interval is exceeded	(61)	(57)

in '000 GEL		
<b>As at 31 December 2018</b>	<b>95% confidence</b>	<b>99% confidence</b>
Maximum loss (VaR)	(151)	(171)
Average loss in case confidence interval is exceeded	(126)	(138)

**ii. Interest rate risk**

Interest rate risk specifies the risk that movements in market interest rates will adversely affect the bank's economic value and its interest earnings and eventually capital. Interest rate risk arises from structural differences between the maturities of assets and those of liabilities. The average maturity of loans typically exceeds that of customer deposits, thus exposing the Group to interest rate risk as described above. In order to keep the interest rate risk at acceptable level, the most of the Group's short-term loans are offered at fixed interest rates while loans with longer maturities are disbursed with floating interest rates. Given that financial instruments to mitigate interest rate risks (hedges) are only available for hard currencies such as EUR and USD, this requires the Group to closely monitor interest rate risk.

The Group's and Bank's approach to measuring and managing interest rate risk is guided by the Interest Rate Risk Management Policy.

There are two indicators, which the bank uses for managing interest rate risk: economic value impact and interest earnings indicator.

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*Economic value risk*

The economic value of the bank is the net present value of all future expected cash flows, i.e. the present value of expected cash inflows from assets minus the present value of expected cash outflows from liabilities. The present value of expected cash flows that depend on interest rates from the bank's off-balance sheet items is also considered. Economic value risk is the risk that the net present value of expected cash flows from already contracted interest rate sensitive assets and liabilities will decrease.

The economic value risk is measured by the economic value impact which represents the change in present value of the bank's future cash flows which would result in the case of an interest rate shock. The economic value risk has a longer term perspective and therefore identifies the risk arising from long term re-pricing. The size of the economic value impact depends on the repricing structure and characteristics of interest sensitive assets and liabilities, as well as on the assumed interest rate change

*Interest earnings risk*

Interest earnings risk considers how changes in interest rate could affect the bank's profitability given its current re-pricing structure. The earnings risk has a near term perspective (up to one year) and therefore identifies the risk arising from shorter term re-pricing mismatches. It is analyzed via a profit and loss (P/L) analysis of interest earnings.

For EUR or USD, a parallel shift of the interest rate curve by +/- 200 bps is assumed. For the local currency, the definition of a shock is derived from historic interest rate volatilities over the last seven deviations from the Interest Rate Risk Policy and violations of interest rate limits are subject to approval by the Parent's General Risk Management Committee.

The Group's interest rate risk position is monitored by the General Risk Management Committee. The indicators are also reported to the Parent's General Risk Management Committee.

Beyond monitoring and limiting interest rate risk in the sense of re-pricing risk, the Group also aims to align the maturities of its assets and liabilities which generate interest earnings and interest expenses.

The table below presents the aggregated amounts of the Group's and the Bank's financial assets and liabilities at carrying amounts, categorised by the earlier of contractual interest re-pricing or maturity dates.

in '000 GEL	Up to	1 - 3	3 - 6	6 -12	1 -5	More than	Non-	
<b>As at 31 December 2019</b>	<b>1 month</b>	<b>months</b>	<b>months</b>	<b>months</b>	<b>years</b>	<b>5 years</b>	<b>interest</b>	<b>Total</b>
<b>Assets</b>								
Cash and balances with the NBG (including Mandatory reserve deposits with NBG)	215,657	-	-	-	-	-	47,252	262,909
Due from banks	81,969	-	-	-	-	-	1,520	83,489
Investments in debt securities	16,993	-	4,924	-	-	-	-	21,917
Loans and advances to customers	109,759	111,162	206,908	170,267	352,336	114,767	4,921	1,070,120
Other financial assets	-	-	-	-	-	-	4,518	4,518
<b>Total financial assets</b>	<b>424,378</b>	<b>111,162</b>	<b>211,832</b>	<b>170,267</b>	<b>352,336</b>	<b>114,767</b>	<b>58,211</b>	<b>1,442,95</b>
<b>Liabilities</b>								
Due to banks	-	69,235	-	-	-	-	1,172	70,407
Customer accounts	268,030	27,360	42,168	116,817	71,968	12,266	228,688	767,297
Other borrowed funds	74,493	91,081	8,760	43,744	155,137	29,229	4,263	406,707
Other financial liabilities	-	-	-	-	-	-	1,145	1,145
Lease liability	-	-	-	-	-	-	2,938	2,938
Subordinated debt	-	-	-	-	-	44,736	578	45,314
<b>Total liabilities</b>	<b>342,523</b>	<b>187,676</b>	<b>50,928</b>	<b>160,561</b>	<b>227,105</b>	<b>86,231</b>	<b>238,784</b>	<b>1,293,80</b>
<b>Net interest sensitivity gap</b>	<b>81,855</b>	<b>-76,514</b>	<b>160,904</b>	<b>9,706</b>	<b>125,231</b>	<b>28,536</b>		

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in '000 GEL	Up to	1 - 3	3 - 6	6 -12	1 -5	More than	Non-	
As at 31 December 2018	1 month	months	months	months	years	5 years	interest bearing	Total
<b>Assets</b>								
Cash and balances with the NBG (including mandatory reserve)	235,539	-	-	-	-	-	103,109	338,648
Due from banks	25,783	-	-	-	-	-	6,360	32,143
Investment securities available-for-sale	8,682	18,523	-	2,380	-	-	182	29,767
Loans and advances to customers	84,705	88,928	149,722	167,202	372,267	151,028	9,404	1,023,256
Other financial assets	-	-	-	-	-	-	4,120	4,120
<b>Total financial assets</b>	<b>354,709</b>	<b>107,451</b>	<b>149,722</b>	<b>169,582</b>	<b>372,267</b>	<b>151,028</b>	<b>123,175</b>	<b>1,427,934</b>
<b>Liabilities</b>								
Due to banks	13,402	13,810	9,207	29,155	-	-	6,034	71,608
Customer accounts	241,444	25,152	32,924	106,977	49,627	12,434	227,819	696,377
Other borrowed funds	53,606	105,058	53,210	12,322	194,468	33,620	4,950	457,234
Other financial liabilities	-	-	-	-	-	-	1,130	1,130
Subordinated debt	-	40,205	-	-	-	42,148	625	82,978
<b>Total liabilities</b>	<b>308,452</b>	<b>184,225</b>	<b>95,341</b>	<b>148,454</b>	<b>244,095</b>	<b>88,202</b>	<b>240,558</b>	<b>1,309,327</b>
<b>Net interest sensitivity gap</b>	<b>46,257</b>	<b>(76,774)</b>	<b>54,381</b>	<b>21,128</b>	<b>128,172</b>	<b>62,826</b>		

In quantitative terms, the risks associated with interest rate fluctuations are currently limited by stipulating that the interest rate risk exposure (economic value impact in present value) of the Group and the Bank following an interest rate shock of +/- 200 bps on EUR/USD and historical worst case for local currency, may not exceed 15% of regulatory capital for all currencies. As at 31 December 2019, the Group and the Bank were in compliance with these requirements. Cumulative interest earnings impact for 12 months shows the following figures as at 31 December 2019:

	<b>Impact on profit or loss (equals impact on equity)</b>			
	Probable adverse case scenario		Stress scenario	
	2%	-2%	5%	-5%
USD	(3,859)	3,859	(9,647)	9,647
EUR	(70)	70	(176)	176
GEL	(2,607)	2,607	(6,517)	6,517
	<b>(6,536)</b>	<b>6,536</b>	<b>(16,340)</b>	<b>16,340</b>

As at 31 December 2018, the impact of cumulative interest earnings was as follows:

	<b>Impact on profit or loss (equals impact on equity)</b>			
	Probable adverse case scenario		Stress scenario	
	2%	-2%	5%	-5%
USD	137	(137)	341	(341)
EUR	1,550	(1,550)	3,875	(3,875)
GEL	3,154	(3,154)	5,272	(5,272)
	<b>4,841</b>	<b>(4,841)</b>	<b>9,488</b>	<b>(9,488)</b>

The scenarios for interest rate sensitivity calculations are taken from Basel regulations.

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The Group and Bank monitors interest rates for its financial instruments by each major currency. The table below summarises average interest rates based on reports reviewed by key management personnel:

**At 31 December 2019**

in % p.a.	EUR	USD	GEL
<b>Financial assets</b>			
Due from banks	(0.2)	0.59	5.03
Loans and advances to customers	5.35	7.24	11.10
<b>Financial liabilities</b>			
Due to other banks	0.63	-	2.50
Customer accounts	0.57	2.60	2.72
Other borrowed funds	2.71	3.38	8.24
Subordinated debt	5.94	8.41	-

**At 31 December 2018**

in % p.a.	EUR	USD	GEL
<b>Financial assets</b>			
Due from banks	-	-	7.10
Loans and advances to customers	6.21	7.46	11.02
<b>Financial liabilities</b>			
Due to other banks	4.94	5.43	-
Customer accounts	0.56	2.41	2.70
Other borrowed funds	3.71	3.74	8.25
Subordinated debt	5.94	7.19	-

**iii. Country risk**

Country risk is defined as the risk that the Group and the Bank may not be able to enforce rights over certain assets in a foreign country (expropriation risk) or that a counterparty in a foreign country is unable to perform an obligation because specific political, economic or social risks prevailing in that country have an adverse effect on the credit exposures (transfer and convertibility risk). Given the nature of the Group's and the Bank's business and the environment in which it operates, the Group/Bank defines country risk more broadly to refer to the possible adverse impact that significant country-specific external macroeconomic, socio-political or regulatory factors can have on the Group's/Bank's earnings, capital or liquidity. In particular, it includes the risk of direct or indirect government intervention in the business operations of the Group/Bank in the form of nationalisation or seizure of assets, or significant market or regulatory intervention.

The Group's/Bank's business strategy is to focus on meeting the demand for credit exhibited by small and medium businesses in the local market. Therefore, it does not normally enter into cross-border transactions or incur country risks. However, as stated above, for the purpose of financial risk management the Group/Bank may need to enter into cross-border transactions, e.g. for the purpose of investing excess liquidity in bond exposures to highly rated international or multinational institutions.

Broader country risk issues are addressed by, and inherent in the Group's/Bank's policies and methodologies for the management of credit, market, liquidity, counterparty/issuer and operational risk. As cross-border exposures are controlled by the Group's/Bank's and the Parent's risk management functions, the Group/Bank is exposed to country risk only to a limited degree.

**(d) Operational risk**

The operational risk is defined as the risk of loss resulting from inadequate or failed internal processes, people or systems or from external events. This definition includes fraud risk, IT and information security risks, legal risk, reputational risk and outsourcing risk. Policies on operational risk management have been implemented since 2009; they have been approved by the Management of the bank and are updated annually. The principles

set forth in the policies are in compliance with the requirements for the standardized approach for operational risk pursuant to CRR, the operational risk management regulations of the National Bank of Georgia, the cybersecurity framework of the National Bank of Georgia and international best practices.

The aim of operational risk management is to detect risks at an early stage and to avoid recurrence of loss events. The main tools utilized are the group-wide Risk Event Database (RED), the annual risk assessments of operational and fraud risks, established Key Risk Indicators (KRI) and the analysis of all new services and processes in a structured procedure, the New Risk Approval (NRA) process.

The Risk Event Database was developed to ensure that all operational risk events identified in the ProCredit group are documented, analyzed and communicated effectively. All ProCredit banks document their risk events using the provided framework, which ensures that adequate attention is paid to the implementation of necessary corrective or preventive measures for reducing or avoiding operational and fraud risk.

In contrast to the ex-post analysis of risk events as recorded in the Risk Event Database, annual risk assessments are systematically performed in order to identify and evaluate key risks and assess the adequacy of the control environment. These two tools complement each other and provide an overall picture of the operational risk profile for ProCredit Bank.

Risk indicators are also used to identify elevated fraud risk in specific areas of banking operations or specific outlets that could be used by potential fraudsters. These indicators are analyzed regularly and where needed preventive measures are agreed on.

To complete the management of operational risk, all new services need to be analyzed to identify and manage potential risks before implementation (NRA process).

In order to limit IT risks, the ProCredit group has defined standards for IT infrastructure, business continuity and information security. At bank level, ProCredit Bank incorporates the requirements from the National Bank of Georgia into the IT/information security risk management framework. Regular controls of information security and business continuity are part of existing processes and procedures. The bank carries out a classification of its information assets and conducts an annual risk assessment on its critical information assets. The business continuity framework implemented in the bank ensures that these risks are understood by all members of staff that critical processes are identified and that resources are allocated to restore operations, in line with the prioritization of processes.

**(e) Anti-money laundering activities**

ProCredit Bank attaches great importance to providing transparent and socially responsible banking services. The Group's/Bank's code of conduct and the exclusion list, together form a binding frame of reference for all of our staff members by documenting ProCredit's refusal to enter into business relationships with individuals or companies whose activities are incompatible with the ProCredit group's and the Bank's ethical values.

ProCredit Bank adheres to the uniform policy framework of the Group/Bank Anti-Money Laundering Policy (Group AML Policy) and accompanying group standards and guidelines, all of which are in compliance with German and EU regulatory requirements as well as the guidelines issued by the Basel Committee on Banking Supervision (BCBS) and the Financial Action Task Force (FATF). In addition to applying international standards and best practice in the area of AML, ProCredit Bank complies with national rules and regulations.

The Group/Bank AML framework includes the following central elements:

- The Group/Bank AML team at ProCredit Holding acts as the central unit for the prevention of money laundering, terrorism financing and fraud throughout the ProCredit group. Besides providing the group policy framework and performing AML training measures, Group AML conducts regular controls in ProCredit banks to monitor the implementation of the Group AML Policy.

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- The Bank appoints an AML Officer who regularly reports to the Management Board (or the Supervisory Board, if required) of the Bank and to the Group Anti-Money Laundering Officer at ProCredit Holding.
- Constant AML trainings for all Bank employees are conducted, both when staff enter the Bank and on an ongoing basis within the framework of the Bank's training plan, in accordance with the Group AML Policy.
- In accordance with the Group Customer Due Diligence (CDD) Standard, ProCredit Bank applies strict Know Your Customer (KYC) rules in its customer due diligence procedures.
- The bank maintains a risk classification system for its customers and applies due diligence and monitoring procedures accordingly.
- All customers and transactions of the bank are screened against relevant international sanctions and embargos as well as national and internal lists of politically exposed persons (PEP).
- The risk of money laundering, terrorism financing, fraud and other financial crime is assessed on an annual basis for the whole ProCredit group, allowing identified risks to be addressed and mitigated through specific measures.
- The bank co-operates with criminal investigation authorities in the country. All activities raising suspicion of money laundering, terrorism financing or financial crime are reported to the responsible Financial Intelligence Units (FIU) as well as to the Group Anti-Money Laundering Officer. On group level, the Group AML Officer co-operates with criminal investigation and law enforcement agencies in Germany and abroad.

ProCredit Bank has established the compliance function, which bears responsibility for adhering to national banking regulations and reports regularly and ad-hoc basis to the Management of the Bank and to the Group Compliance officer.

The Bank is in full compliance with all regulatory requirements concerning the prevention of money laundering and terrorism financing. Moreover, the Bank has implemented the group wide guidelines on the prevention of money laundering and terrorism financing, which in many respects are stricter than the legal requirements prevailing in the country.

### **30. FAIR VALUE OF FINANCIAL INSTRUMENTS**

A number of accounting policies and disclosures require the determination of fair values for financial assets and liabilities. Fair values have been determined for measurement and disclosure purposes. The Group measures fair values using the following fair value hierarchy that reflects the significance of the inputs used in making the measurements:

- Level 1: quoted market price (unadjusted) in an active market for an identical instrument.
- Level 2: inputs other than quoted prices included within Level 1 that are observable either directly (i.e. as prices) or indirectly (i.e., derived from prices). This category includes instruments valued using: quoted market prices in active markets for similar instruments; quoted prices for similar instruments in markets that are considered less than active; or other valuation techniques where all significant inputs are directly or indirectly observable from market data.
- Level 3: inputs that are unobservable. This category includes all instruments where the valuation technique includes inputs not based on observable data and the unobservable inputs have a significant effect on the instrument's valuation. This category includes instruments that are valued based on quoted prices for similar instruments where significant unobservable adjustments or assumptions are required to reflect differences between the instruments.



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The Group and Bank estimates the fair value of all financial assets and liabilities as at 31 December 2019 and 2018. Results are provided in the following table:

in '000 GEL	Level	2019		2018	
		Carrying value	Fair value	Carrying value	Fair value
<b>Financial assets</b>					
Cash and cash equivalents	Level 2	86,983	86,983	167,842	167,842
Mandatory reserve deposits with NBG	Level 2	175,926	175,926	170,806	170,806
Due from other banks	Level 2	83,489	83,489	32,143	32,143
Loans and advances to customers	Level 3	1,070,120	1,053,398	1,023,256	1,000,294
Other financial assets	Level 3	4,518	4,518	4,120	4,120
<b>Total financial assets</b>		<b>1,421,036</b>	<b>1,404,314</b>	<b>1,398,167</b>	<b>1,375,205</b>

in '000 GEL	Level	2019		2018	
		Carrying value	Fair value	Carrying value	Fair value
<b>Financial liabilities</b>					
Due to other banks	Level 2	70,407	70,407	71,608	71,608
Customer accounts					
Current accounts	Level 2	224,775	224,775	221,694	221,695
Savings accounts	Level 2	249,314	249,290	230,271	230,271
Term accounts	Level 3	289,152	294,580	238,302	241,892
Other liabilities to customers	Level 2	4,056	4,056	6,110	6,110
Other borrowed funds	Level 3	406,707	404,146	457,234	443,636
Other financial liabilities	Level 3	1,145	1,145	1,130	1,130
Subordinated debt	Level 3	45,314	45,314	82,978	78,594
<b>Total financial liabilities</b>		<b>1,290,870</b>	<b>1,293,713</b>	<b>1,309,327</b>	<b>1,294,936</b>

The estimates of fair value are intended to approximate 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. However, given the uncertainties and the use of subjective judgment, the fair value should not be interpreted as being realisable in an immediate sale of the assets or transfer of liabilities.

The Group has determined fair values using valuation techniques. The objective of valuation techniques is to arrive at a fair value determination that reflects the price that would be received to sell the asset or paid to transfer the liability in an orderly transaction between market participants at the measurement date. The valuation technique used is the discounted cash flow model.

The fair value of floating rate instruments that are not quoted in an active market was estimated to be equal to their carrying amount. The fair value of unquoted fixed interest rate instruments was estimated based on estimated future cash flows expected to be received discounted at current interest rates for new instruments with similar credit risk and remaining maturity. In case observable market rates are not available to determine the fair value of financial liabilities measured at amortized cost, the Parent's Treasury rates are used as an input for a discounted cash flow model. The Parent's Treasury rates are determined considering the cost of capital depending on currencies and maturities plus a risk margin that depends on an internal risk rating for each institution. These internal rates are regularly compared to those applied for third party transactions.

Where available, the fair value of loans and advances is based on observable market transactions. Where observable market transactions are not available, fair value is estimated using the Group's own fair value model, such as the discounted cash flow technique. Input using the valuation technique includes expected lifetime credit losses, interest rates and prepayment rates. The fair value of deposits from banks and customers is estimated using discounted cash flow techniques, applying the rates that are offered for deposits of similar maturities and terms. The fair value of deposits payable on demand is the amount payable at the reporting date.

### 31. CONTINGENT LIABILITIES AND COMMITMENTS

The Group/Bank has outstanding commitments to extend credit. These commitments take the form of approved loans limits and overdraft facilities. The Group/Bank provides financial guarantees and letters of credit to guarantee the performance of customers to third parties. These agreements have fixed limits and generally extend for a period of up to five years.

The Group/Bank applies the same credit risk management policies and procedures when granting credit commitments, financial guarantees and letters of credit as it does for granting loans and advances to customers.

in '000 GEL

<b>As at 31 December</b>	<b>2019</b>	<b>2018</b>
Financial guarantees and stand-by letters of credit	12,850	10,149
Performance guarantees	35,613	28,948
Commitments to extend credit:		
- Original term to maturity of one year or less	28,603	11,710
- Original term to maturity of more than one year	20,356	14,521
<b>Total</b>	<b>97,422</b>	<b>65,328</b>

As at 31 December 2019 the Group/Bank allocates commitments to extend credit, financial guarantees and stand-by letters of credit in Stage 1 and 2 for the purposes of identifying expected credit loss under IFRS 9 (1 January 2018: Stage 1 and 2). The Group/Bank calculates ECL of performance guarantees according to IAS 37. Management estimates that ECL is immaterial at reporting dates. The table discloses the nominal principal amounts of contingent liabilities, commitments and guarantees, i.e. the amounts at risk, should contracts be fully drawn upon and clients default. The management believes that a significant portion of guarantees and commitments will expire without being drawn upon; therefore the total of the contractual amounts is not representative of future liquidity requirements.

#### **Tax legislation**

The taxation system in Georgia is relatively new and is characterised by frequent changes in legislation, official pronouncements and court decisions, which are sometimes unclear, contradictory and subject to varying interpretation. In the event of a breach of tax legislation, no liabilities for additional taxes, fines or penalties may be imposed by the tax authorities after three years have passed since the end of the year in which the breach occurred.

These circumstances may create tax risks in Georgia that are more significant than in other countries. Management believes that it has provided adequately for tax liabilities based on its interpretations of applicable Georgian tax legislation, official pronouncements and court decisions. However, the interpretations of the relevant authorities could differ and the effect on these financial statements, if the authorities were successful in enforcing their interpretations, could be significant.

#### **Litigation**

In the ordinary course of business, the Group/Bank is subject to legal actions and complaints. Management believes that the ultimate liability, if any, arising from such actions or complaints will not have a material adverse effect on the financial condition or the results of future operations of the Group/Bank.

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**32. RELATED PARTY TRANSACTIONS**

The Group and Bank's immediate parent company is ProCredit Holding AG & Co. KGaA, which produces publicly available financial statements.

Parties are generally considered to be related if the parties are under common control, or one party has the ability to control the other party or can 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. The key management personnel include the executive directors of the Group and Bank and their close family members.

The Group and Bank had the following balances outstanding as at 31 December 2019 and 2018 with related parties:

in '000 GEL As at 31 December	Contractual interest rate, p.a.	2019	2018
<b>Assets</b>			
<b>Due from banks</b>			
- Entities under common control	(0.75%) to 1.55 %	36,013	40,213
<b>Loans and advance to customers</b>			
- Key management	12 %	6	31
<b>Due to banks</b>			
- Entities under common control	up to 0.99%	70,434	53,190
<b>Customer accounts</b>			
- Key management	0.0%-4.5%	186	329
<b>Other borrowed funds</b>			
- Parent	2.84%-4.0%	108,435	186,464
- entities under common control	2.6%-4.3%	40,672	37,524
<b>Subordinated debt</b>			
- Parent	5.9%-7.9%	45,314	42,685

Included in the profit or loss for the year ended 31 December 2019 and 2018 are the following amounts which arose due to transactions with related parties:

in '000 GEL	2019	2018
<b>Interest expense</b>		
- Parent	10,919	10,567
- entities under common control	1,943	3,259
- key management	5	11
<b>Fees and commission expenses</b>		
- entities under common control	2,073	1,854
<b>Other operating income</b>		
- Parent	-	8
<b>Personnel expenses</b>		
- Key management	874	1,068
<b>Other administrative expenses</b>		
- Parent	2,544	2,493
- entities under common control	3,851	3,932

The transactions leading to the above balances were made in the ordinary course of business and on substantially the same terms as for comparable transactions with entities or persons of a similar standing or, where applicable, with other employees. The transactions did not involve more than the normal risk of payment defaults nor did they comprise other unfavorable features.

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The Bank had the following balances outstanding as at 31 December 2019 and 2018 with it subsidiary:

in '000 GEL		
<b>As at 31 December</b>	<b>2019</b>	<b>2018</b>
<b>Assets</b>		
<b>Investment in Subsidiaries</b>		
- Subsidiary	6,100	6,100
<b>Liability</b>		
<b>Customer accounts</b>		
Subsidiary	4,089	3,317

**33. EVENTS AFTER THE END OF THE REPORTING PERIOD**

**Subsequent events – the COVID-19 outbreak**

*(i). General overview*

On 11 March 2020, the World Health Organisation (WHO) declared the COVID-19 coronavirus pandemic. The first case in Georgia was officially reported on 26 February 2020. As measures against spreading of the virus, Government of Georgia imposed various restrictions over activities within the country. The restrictions imposed at various times include ban on all cross-border travel, restriction over all travel within the country during specific hours, closing of all public transport, stopping all commercial activity except those which can be done distantly from home as well as except specific business (groceries, pharmacies, commercial banks, gas stations, post offices etc.). The restrictions imposed by Government of Georgia do not apply to any of the Bank’s operations. The Bank continues work in under the business continuity plan with personnel assigned to either of the two offices and working remotely from home as much as possible.

*(ii). Changes in regulatory requirements*

As response to the existing crisis, the National Bank of Georgia (“NBG”) took several actions aiming at alleviating the negative financial and economic challenges created by the global COVID-19 pandemic in Georgia. The following NBG actions may potentially have effect on the Bank’s operations:

- in order to stabilize sudden increase in foreign exchange rates (GEL/USD peak rate of 3.4842 was recorded on 27 March 2020), NBG sold USD 100 million on local market during March 2020;
- coordinated Georgian banks’ initiative to provide voluntary grace period of three months to most of commercial banks’ retail and small business borrowers within the country. In parallel to slightly amplified drawdowns of deposits for household cash needs, this initiative has further stressed the GEL liquidity in the financial sector. To address it, NBG started to offer FX swaps to commercial banks and microfinance organizations, up to USD 200 million for each sector;
- softened regulatory requirements for commercial banks, including softening certain requirements for capital adequacy and liquidity ratios. This will allow banks to use existing buffers to support customers in the current financially stressed circumstances, to continue normal business activities to the extent possible. Liquidity coverage ratio (LCR) requirements (for local and foreign currency, as well as total requirement) may as well be revisited and reduced, if necessary;
- imposed general provisions for possible credit losses for each bank individually;
- is not going to impose any monetary sanctions in case of breach of economic normative and limits driven by external factors (e.g. reserves, exchange rate depreciation).

*(iii). Effect of COVID 19 on the Bank*

As part of the Government initiative to provide moratorium on the repayment of loans to customers (principal and interest) to the Bank followed individual approach on a customer's need base. The Bank granted moratorium on the repayments of principal and interest to its customers that were effected based on their request. Around 39% of loans to customers' portfolio has been granted moratorium for the repayment of interest and principal from 3 to 6 months as of the date of this Financial Statements are authorized for issue. The Bank has considered effect of moratorium in its liquidity analysis. In addition, the Bank revised expected credit loss model for updated macroeconomic environment thus resulting in increase of expected credit losses in March 2020.

Management of the Bank also performed stress tests for several possible scenarios to estimate possible downside effects of the pandemic on the Bank's operations on the liquidity. Bank stressed cash flow on customer accounts assuming outflow in the range from 10% to 20% for the next 12 months. In addition the Bank also stressed repayment (inflows) on loans to customers by reducing repayment for the next three months to nil and 50% thereafter for 9 months. The Bank has assessed its liquidity and capital adequacy position for the 12 months from the date these Financial Statements are authorized for issues. Even in the worst case scenario of stress tests the Bank maintains sufficient liquidity and capital adequacy to support continued operations for the foreseeable future.

**Other**

In January 2020 the Group and Bank obtained a loan from EBRD with amount of EUR 15 000 000.