JSC Terabank

Consolidated Financial Statements for 2017

Contents

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Independent Auditors' Report

To the Shareholders of JSC Terabank

Opinion

We have audited the consolidated financial statements of JSC Terabank (the "Bank") and its subsidiary (the "Group"), which comprise the consolidated statement of financial position as at 31 December 2017, the consolidated 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 financial statements present fairly, in all material respects, the consolidated financial position of the Group as at 31 December 2017, and its consolidated financial performance and its consolidated 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 Financial Statements* section of our report. We are independent of the Group in accordance with the International Ethics Standards Board for Accountants' *Code of Ethics for Professional Accountants* (IESBA Code) together with the ethical requirements that are relevant to our audit of the consolidated financial statements in Georgia, and we have fulfilled our other ethical responsibilities in accordance with these requirements and the IESBA Code. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Statement of Management Report

Management is responsible for the Management Report. The Management Report is expected to be made available to us after the date of this auditors' report.

Our opinion on the consolidated financial statements does not cover the Management Report and we will not express any form of assurance conclusion thereon.

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

When we read the Management Report, we conclude whether the other information:

— is consistent with the consolidated 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 Financial Statements

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

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

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

Auditors' Responsibilities for the Audit of the Consolidated Financial Statements

Our objectives are to obtain reasonable assurance about whether the consolidated financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an 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 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 financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Group's internal control.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management.
- Conclude on the appropriateness of management's use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Group's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditors' report to the related disclosures in the consolidated financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditors' report. However, future events or conditions may cause the Group to cease to continue as a going concern.
- Evaluate the overall presentation, structure and content of the consolidated financial statements, including the disclosures, and whether the consolidated financial statements represent the underlying transactions and events in a manner that achieves fair presentation.
- Obtain sufficient appropriate audit evidence regarding the financial information of the entities or business activities within the Group to express an opinion on the consolidated financial statements. We are responsible for the direction, supervision and performance of the group audit. We remain solely responsible for our audit opinion.

We communicate with 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:

Andrew Coxshall

P.P.

KPMG Georgia LLC
Tbilisi, Georgia
3 May 2018

GEL'000	Notes	2017	2016
Assets			
Cash and cash equivalents	4	88,803	91,555
Mandatory reserve deposit with the National Bank of Georgia		76,551	72,573
Loans to customers	6	559,942	434,943
Investment securities	5	53,333	29,465
Premises and equipment	7	18,742	18,154
Other intangible assets		2,788	4,109
Repossessed property	6	13,865	22,084
Other assets		4,353	3,383
Goodwill	8	20,374	20,374
Total assets		**838,751**	**696,640**
Liabilities			
Loans from financial institutions	10	65,214	10,696
Deposits and balances from banks	13	16,952	416
Current accounts and deposits from customers	14	579,626	520,602
Deferred tax liabilities	9	276	315
Other liabilities	15	14,557	12,408
Subordinated loans	11	31,706	33,705
Total liabilities		**708,331**	**578,142**
Equity	16		
Share capital		121,372	121,372
Retained Earnings/(Accumulated losses)		9,048	(2,874)
Total equity		**130,420**	**118,498**
Total liabilities and equity		**838,751**	**696,640**

These consolidated financial statements were approved by the Management Board on 3 May 2018 and were signed on its behalf by:

Thea Lortkipanidze
General Director

Sophie Jugeli
Chief Financial Officer

The consolidated statement of financial position is to be read in conjunction with the notes to, and forming part of, the consolidated financial statements set out on pages 9 to 44.

GEL'000	Notes	2017	2016
Interest income	17	63,080	63,093
Interest expense	17	(29,479)	(36,029)
Net interest income		**33,601**	**27,064**
Loan impairment losses	6	(4,461)	(10,014)
Net fee and commission income	18	3,371	2,744
Net gain from trading in foreign currencies		6,935	3,483
Net (loss)/gain from foreign exchange translation		(931)	5,206
Other income		2,420	917
Operating income		**40,935**	**29,400**
Personnel expenses		(12,763)	(10,149)
Depreciation and amortization		(4,641)	(4,162)
Other provisions		(1,930)	(426)
Other operating expenses	19	(9,718)	(9,409)
Profit before income tax		**11,883**	**5,254**
Income tax benefit	9	39	282
Profit and total comprehensive income for the year		**11,922**	**5,536**

The consolidated statement of profit or loss and other comprehensive income is to be read in conjunction with the notes to, and forming part of, the consolidated financial statements set out on pages 9 to 44.

GEL'000	Share capital	Retained earnings/ (Accumulated losses)	Total equity
Balance at 1 January 2016	111,000	(8,410)	102,590
Profit and total comprehensive income for the year	-	5,536	5,536
Transactions with owners, recorded directly in equity			
Issue of share capital (note 16)	10,372	-	10,372
Balance at 31 December 2016	**121,372**	**(2,874)**	**118,498**
Balance at 1 January 2017	121,372	(2,874)	118,498
Profit and total comprehensive income for the year	-	11,922	11,922
Balance at 31 December 2017	**121,372**	**9,048**	**130,420**

The consolidated statement of changes in equity is to be read in conjunction with the notes to, and forming part of, the consolidated financial statements set out on pages 9 to 44.

GEL'000	Notes	2017	2016
Cash flows from operating activities			
Interest received		61,466	62,047
Interest paid		(29,986)	(38,487)
Fees and commissions received		7,928	6,348
Fees and commissions paid		(4,051)	(3,512)
Realised gains less losses from dealing in foreign currencies and operations with foreign currency derivatives		6,935	3,483
Other operating income received		2,420	937
Personnel expenses paid		(10,674)	(10,551)
Other operating expenses paid		(8,982)	(9,406)
Cash flows from operating activities before changes in operating assets and liabilities		**25,056**	**10,859**
Changes in:			
Mandatory reserve deposits with the National Bank of Georgia		(4,228)	(21,536)
Loans to customers		(130,379)	13,199
Other assets and repossessed property		5,389	(917)
Deposits and balances from banks		16,834	(36,805)
Current accounts and deposits from customers		60,276	49,140
Other liabilities		(2,494)	2,917
Net cash (used in)/ from operating activities		**(29,546)**	**16,857**
Cash flows used in investing activities			
Acquisition of investment securities		(30,076)	(13,564)
Proceeds from redemption of investment securities		5,752	18,100
Acquisition of premises and equipment		(2,950)	(4,134)
Acquisition of intangible assets		(956)	(1,183)
Net cash used in investing activities		**(28,230)**	**(781)**
Cash flows from financing activities			
Receipts of loans from financial institutions		59,467	-
Repayment of the loans from the financial institution		(6,358)	(11,726)
Repayment of the subordinated loans		(1,271)	(693)
Proceeds from issue of share capital		-	5,433
Net cash from/(used in) financing activities		**51,838**	**(6,986)**
Effect of exchange rates changes on cash and cash equivalents		3,186	576
Net (decrease)/increase in cash and cash equivalents		**(2,752)**	**9,666**
Cash and cash equivalents, beginning	4	**91,555**	**81,889**
Cash and cash equivalents, ending	4	**88,803**	**91,555**

The consolidated statement of cash flows is to be read in conjunction with the notes to, and forming part of, the consolidated financial statements set out on pages 9 to 44.

1. Reporting entity

(a) Georgian business environment

The Group's operations are located in Georgia. Consequently, the Group is 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 financial statements reflect management's assessment of the impact of the Georgian business environment on the operations and the financial position of the Group. The future business environment may differ from management's assessment.

(b) Organisation and operations

These consolidated financial statements comprise the financial statements of JSC Terabank (the Bank) and its subsidiary (the Group). The Bank was established in Georgia as a joint stock company on 30 December 2007 under the legal name of JSC Kor Bank. On 23 May 2016 the Bank changed its legal name to JSC Terabank. The company's registration number is 204546045.

The Bank's principal activities are deposit taking, customer account maintenance, credit operations, issuing guarantees, cash and settlement operations, and securities and foreign exchange transactions. The Bank's activities are regulated by the National Bank of Georgia (NBG). The Bank has a general banking license issued by NBG on 25 January 2008.

The Bank's registered legal address is 3, K. Tsamebuli Avenue, Tbilisi 0103, Georgia. The Bank operates through 26 branches, service centres and service desks, which are located in all major cities of Georgia.

The Bank has one subsidiary, Standard Insurance LLC, which does not have operations in 2017 and 2016.

As at 31 December 2017 and 2016, the Bank's shareholding structure is as follows:

Owners	**Ownership interest, %**
Sheikh Nahayan Mabarak Al-Nahayan	45%
Sheikh Hamdan Bin Zayed Alnehayan	20%
Sheikh Mohamed Butti Alhamed	15%
Sheikh Mansoor Binzayed Binsultan Al-Nahayan	15%
Investment Trading Group LLC	5%
	100%

Related party transactions are described in detail in note 24.

2. Basis of preparation

(a) Statement of compliance

The accompanying consolidated financial statements are prepared in accordance with International Financial Reporting Standards (IFRS).

(b) Basis of measurement

The consolidated financial statements are prepared on the historical cost basis except that financial instruments at fair value through profit or loss are stated at fair value.

(c) Functional and presentation currency

The functional currency of the Group is the Georgian Lari (GEL) as, being the national currency of Georgia, it reflects the economic substance of the majority of underlying events and circumstances relevant to them.

The GEL is also the presentation currency for the purposes of these consolidated financial statements.

(d) Use of estimates and judgments

The preparation of consolidated financial statements in conformity with IFRS requires management to make judgments, estimates and assumptions that affect the application of accounting policies and the reported amounts of assets, liabilities, income and expenses. Actual results could 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.

Information about significant areas of estimation uncertainty and critical judgments in applying accounting policies is described in the following notes:

— loan impairment estimates – note 6;
— Goodwill impairment test – note 8;
— Estimates of fair values of financial assets and liabilities – note 22.

(e) Changes in accounting policies and presentation

The Group has adopted the following amendments to standards with a date of initial application of 1 January 2017:

- *Disclosure Initiative (Amendments to IAS 7).* IAS 7 *Statement of Cash Flows* has been amended as part of the IASB's broader disclosure initiative to improve presentation and disclosure in financial statements. The amendment requires disclosures that enable users of financial statements to evaluate changes in liabilities arising from financing activities, including both changes arising from cash flow and non-cash changes. One way to meet this new disclosure requirement is to provide a reconciliation between the opening and closing balances for liabilities arising from financing activities. However, the objective could also be achieved in other ways.
- *Recognition of Deferred Tax Asset for Unrealised Losses (Amendments to IAS 12).* The amendments to IAS 12 *Income Taxes* clarify that the existence of a deductible temporary difference depends solely on a comparison of the carrying amount of an asset and its tax base at the end of the reporting period, and is not affected by possible future changes in the carrying amount or expected manner of recovery of the asset. Therefore, assuming that the tax base remains at the original cost of the debt instrument, there is a temporary difference. The amendments show that the entity can recognise a deferred tax asset if the future bottom line of its tax return is expected to be a loss if certain conditions are met.
- *Annual Improvements to IFRSs 2014–2016 Cycle – various standards (Amendments to IFRS 12).* Amendments to IFRS 12 Disclosure of Interests in Other Entities clarify that the disclosure requirements for interests in other entities also apply to interests that are classified as held for sale or distribution.

3. Significant accounting policies

The accounting policies set out below are applied consistently to all periods presented in these consolidated financial statements, and are applied consistently by the Bank and its subsidiary.

Basis of consolidation

Subsidiaries

Subsidiaries are investees controlled by the Group. The Group 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.

Transactions eliminated on consolidation

Intra-group balances and transactions, and any unrealised gains arising from intra-group transactions, are eliminated in preparing the consolidated financial statements.

Foreign currency translation

Transactions in foreign currencies are translated to GEL at exchange rates at the dates of the transactions.

Monetary assets and liabilities denominated in foreign currencies at the reporting date are retranslated to GEL at the exchange rate at that 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 assets and liabilities denominated in foreign currencies that are measured at fair value are retranslated to the functional currency at the exchange rate at the date that the fair value is determined. Non-monetary items that are measured in terms of historical cost in a foreign currency are translated using the exchange rate at the date of the transaction.

Foreign currency differences arising on retranslation are recognised in profit or loss.

Financial instruments

Financial instruments at fair value through profit or loss are financial assets or liabilities that are:

- acquired or incurred principally for the purpose of selling or repurchasing in the near term
- part of a portfolio of identified financial instruments that are managed together and for which there is evidence of a recent actual pattern of short-term profit-taking
- derivative financial instruments (except for a derivative that is a financial guarantee contract or a designated and effective hedging instruments) or,
- upon initial recognition, designated as at fair value through profit or loss.

The Group may designate financial assets and liabilities at fair value through profit or loss where either:

- the assets or liabilities are managed, evaluated and reported internally on a fair value basis
- the designation eliminates or significantly reduces an accounting mismatch which would otherwise arise or,
- the asset or liability contains an embedded derivative that significantly modifies the cash flows that would otherwise be required under the contract.

All trading derivatives in a net receivable position (positive fair value), as well as options purchased, are reported as assets. All trading derivatives in a net payable position (negative fair value), as well as options written, are reported as liabilities.

Management determines the appropriate classification of financial instruments in this category at the time of the initial recognition. Derivative financial instruments and financial instruments designated as at fair value through profit or loss upon initial recognition are not reclassified out of at fair value through profit or loss category.

Financial assets that would have met the definition of loans and receivables may be reclassified out of the fair value through profit or loss or available-for-sale category if the Group has an intention and ability to hold them for the foreseeable future or until maturity. Other financial instruments may be reclassified out of at fair value through profit or loss category only in rare circumstances. Rare circumstances arise from a single event that is unusual and highly unlikely to recur in the near term.

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market, other than those that the Group:

- intends to sell immediately or in the near term
- upon initial recognition designates as at fair value through profit or loss
- upon initial recognition designates as available-for-sale or,
- may not recover substantially all of its initial investment, other than because of credit deterioration

Held-to-maturity investments are non-derivative financial assets with fixed or determinable payments and fixed maturity that the Group has the positive intention and ability to hold to maturity, other than those that:

- the Group upon initial recognition designates as at fair value through profit or loss

- the Group designates as available-for-sale or,
- meet the definition of loans and receivables.

Available-for-sale financial assets are those non-derivative financial assets that are designated as available-for-sale or are not classified as loans and receivables, held-to-maturity investments or financial instruments at fair value through profit or loss.

The Group classifies all financial assets as loans and receivables, except for the investment securities, which are classified as held-to-maturity investments.

Recognition of financial instruments

Financial assets and liabilities are recognised in the consolidated statement of financial position when the Group becomes a party to the contractual provisions of the instrument. All regular way purchases of financial assets are accounted for at the settlement date.

Measurement of financial instruments

A financial asset or liability is initially measured at its fair value plus, in the case of a financial asset or liability not at fair value through profit or loss, transaction costs that are directly attributable to the acquisition or issue of the financial asset or liability.

Subsequent to initial recognition, financial assets, including derivatives that are assets, are measured at their fair values, without any deduction for transaction costs that may be incurred on their sale or other disposal, except for:

- loans and receivables which are measured at amortized cost using the effective interest method
- held-to-maturity investments that are measured at amortized cost using the effective interest method
- investments in equity instruments that do not have a quoted market price in an active market and whose fair value cannot be reliably measured which are measured at cost

All financial liabilities, other than those designated at fair value through profit or loss and financial liabilities that arise when a transfer of a financial asset carried at fair value does not qualify for derecognition, are measured at amortised cost. All financial liabilities are classified as other financial liabilities, except for swaps, which are designated at fair value through profit or loss.

Amortized cost

The amortised cost of a financial asset or liability is the amount at which the financial asset or liability is measured at initial recognition, minus principal repayments, plus or minus the cumulative amortisation using the effective interest method of any difference between the initial amount recognised and the maturity amount, minus any reduction for impairment. Premiums and discounts, including initial transaction costs, are included in the carrying amount of the related instrument and amortised based on the effective interest rate of the instrument

Cash and cash equivalents and mandatory reserve with the NBG

Cash and cash equivalents consist of cash on hand, amounts due from the NBG, excluding mandatory reserves, amounts due from credit institutions and other highly liquid financial assets with original maturities of less than three months, which are subject to insignificant risk of changes in their fair value, and are used by the Group in the management of short-term commitments. Cash and cash equivalents are carried at amortised cost in the consolidated statement of financial position.

The mandatory reserve deposit is a non-interest bearing deposit calculated in accordance with regulations issued by the NBG and whose withdrawability is restricted. The mandatory reserve deposit with the NBG is not considered to be a cash equivalent, due to restrictions on its withdrawability.

Fair value measurement principles

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 in the principal, or in its absence, the most advantageous market to which the Group has access at that date. The fair value of a liability reflects its non-performance risk.

When available, the Group measures the fair value of an instrument using quoted prices in an active market for that instrument. A market is regarded as active if transactions for the asset or liability take place with sufficient frequency and volume to provide pricing information on an ongoing basis.

When there is no quoted price in an active market, the Group uses valuation techniques that maximise the use of relevant observable inputs and minimise the use of unobservable inputs. The chosen valuation technique incorporates all the factors that market participants would take into account in these circumstances.

The best evidence of the fair value of a financial instrument at initial recognition is normally the transaction price, i.e., the fair value of the consideration given or received. If the Group determines that the fair value at initial recognition differs from the transaction price and the fair value is evidenced neither by a quoted price in an active market for an identical asset or liability nor based on a valuation technique that uses only data from observable markets, the financial instrument is initially measured at fair value, adjusted to defer the difference between the fair value at initial recognition and the transaction price. Subsequently, that difference is recognised in profit or loss on an appropriate basis over the life of the instrument, but no later than when the valuation is supported wholly by observable market data or the transaction is closed out.

Gains and losses on subsequent measurement of fair value

A gain or loss arising from a change in the fair value of a financial asset or liability is recognised as follows:

- a gain or loss on a financial instrument classified as at fair value through profit or loss is recognised in profit or loss
- a gain or loss on an available-for-sale financial asset is recognised as other comprehensive income in equity (except for impairment losses and foreign exchange gains and losses on debt financial instruments available-for-sale) until the asset is derecognised, at which time the cumulative gain or loss previously recognised in equity is recognised in profit or loss. Interest in relation to an available-for-sale financial asset is recognised in profit or loss using the effective interest method.

For financial assets and liabilities carried at amortized cost, a gain or loss is recognised in profit or loss when the financial asset or liability is derecognised or impaired, and through the amortisation process.

Derecognition of financial instruments

The Group derecognises a financial asset when the contractual rights to the cash flows from the financial asset expire, or when it transfers the financial asset in a transaction in which substantially all the risks and rewards of ownership of the financial asset are transferred or in which the Group neither transfers nor retains substantially all the risks and rewards of ownership and it does not retain control of the financial asset. Any interest in transferred financial assets that qualify for derecognition that is created or retained by the Group is recognised as a separate asset or liability in the consolidated statement of financial position. The Group derecognises a financial liability when its contractual obligations are discharged or cancelled or expire.

The Group enters into transactions whereby it transfers assets recognised on its consolidated statement of financial position, but retains either all risks and rewards of the transferred assets or a portion of them. If all or substantially all risks and rewards are retained, then the transferred assets are not derecognised.

In transactions where the Group neither retains nor transfers substantially all the risks and rewards of ownership of a financial asset, it derecognises the asset if control over the asset is lost.

In transfers where control over the asset is retained, the Group continues to recognise the asset to the extent of its continuing involvement, determined by the extent to which it is exposed to changes in the value of the transferred assets.

The Group writes off assets deemed to be uncollectible.

Offsetting of financial instruments

Financial assets and liabilities are offset and the net amount presented in the statement of financial position when, and only when, the Group currently has a legally enforceable right to set off the recognised amounts and intends either to settle on a net basis or to realise the asset and settle the liability simultaneously. The Group currently has a legally enforceable right to set off if that right is not contingent on a future event and enforceable both in the normal course of business and in the event of default, insolvency or bankruptcy of the Group and all counterparties.

Impairment of financial assets

The Group assesses at each reporting date whether there is any objective evidence that a financial asset or a group of financial assets is impaired. A financial asset or a group of financial assets is deemed to be impaired if, and only if, there is objective evidence of impairment as a result of one or more events that has occurred after the initial recognition of the asset (an incurred 'loss event') and that loss event (or events) has an impact on the estimated future cash flows of the financial asset or the group of financial assets that can be reliably estimated. Evidence of impairment may include indications that the borrower or a group of borrowers is experiencing significant financial difficulty, default or delinquency in interest or principal payments, the probability that they will enter bankruptcy or other financial reorganisation and where observable data indicate that there is a measurable decrease in the estimated future cash flows, such as changes in arrears or economic conditions that correlate with defaults.

The Group first assesses individually whether objective evidence of impairment exists individually for financial assets that are individually significant, or collectively for financial assets that are not individually significant. If the Group determines that no objective evidence of impairment exists for an individually assessed financial asset, whether significant or not, it includes the asset in a group of financial assets with similar credit risks characteristics and collectively assesses them for impairment. Assets that are individually assessed for impairment and for which an impairment loss is, or continues to be, recognized are not included in a collective assessment of impairment.

If there is an objective evidence that an impairment loss has been incurred, the amount of the loss is measured as the difference between the assets' carrying amount and the present value of estimated future cash flows (excluding future expected credit losses that have not yet been incurred). The carrying amount of the asset is reduced through the use of an allowance account and the amount of the loss is recognised in profit or loss. Interest income continues to be accrued on the reduced carrying amount based on the original effective interest rate of the Financial assets together with the associated allowance are written off when there is no realistic prospect of future recovery and all collateral has been realised or has been transferred to the Group. If, in a subsequent year, the amount of the estimated impairment loss increases or decreases because of an event occurring after the impairment was recognised, the previously recognised impairment loss is increased or reduced by adjusting the allowance account. If a future write-off is later recovered, the recovery is credited to the consolidated statement of profit and loss and other comprehensive income. The present value of the estimated future cash flows is discounted at the financial asset's original effective interest rate. If a loan has a variable interest rate, the discount rate for measuring any impairment loss is the current effective interest rate. The calculation of the present value of the estimated future cash flows of a collateralised financial asset reflects the cash flows that may result from foreclosure less costs for obtaining and selling the collateral, whether or not foreclosure is probable.

For the purpose of a collective evaluation of impairment, financial assets are grouped on the basis of the Group's internal credit grading system that considers credit risk characteristics such as asset type, industry, geographical location, collateral type, past-due status and other relevant factors.

Future cash flows on a group of financial assets that are collectively evaluated for impairment are estimated on the basis of historical loss experience for assets with credit risk characteristics similar to those in the group. Historical loss experience is adjusted on the basis of current observable data to reflect the effects of current conditions that did not affect the years on which the historical loss experience is based and to remove the effects of conditions in the historical period that do not exist currently. Estimates of changes in future cash flows reflect, and are directionally consistent with, changes in related observable data from year to year (such as changes in unemployment rates, property prices, commodity prices, payment status, or other factors that are indicative of incurred losses in the group or their magnitude). The methodology and assumptions used for estimating future cash flows are reviewed regularly to reduce any differences between loss estimates and actual loss experience.

Repossessed property

Repossessed property represents financial and non-financial assets acquired by the Group in settlement of overdue loans. The assets are initially recognised at net book value of respective loan when acquired and included in premises and equipment, other financial assets or inventories depending on their nature and the Group's intention in respect of recovery of these assets and are subsequently remeasured and accounted for in accordance with the accounting policies for these categories of assets.

Provision

A provision is recognised in the consolidated statement of financial position when the Group has a legal or constructive obligation as a result of a past event, and it is probable that an outflow of economic benefits will be required to settle the obligation. If the effect is material, provisions are determined by discounting the expected future cash flows at a pre-tax rate that reflects current market assessments of the time value of money and, where appropriate, the risks specific to the liability

Inventories

Inventories are measured at the lower of cost and net realisable value. The cost of inventories is based on the first in first out principle, and includes expenditure incurred in acquiring the inventories, production or conversion costs and other costs incurred in bringing them to their existing location and condition.

Net realisable value is the estimated selling price in the ordinary course of business, less the estimated costs of completion and selling expenses.

Credit related commitments

The Group enters into credit related commitments, including letters of credit and financial guarantees. Financial guarantees represent irrevocable assurances to make payments in the event that a customer cannot meet its obligations to third parties and carry the same credit risk as loans. Financial guarantees and commitments to provide a loan are initially recognised at their fair value, which is normally evidenced by the amount of fees received. This amount is amortised on a straight line basis over the life of the commitment, except for commitments to originate loans if it is probable that the Group will enter into a specific lending arrangement and does not expect to sell the resulting loan shortly after origination; such loan commitment fees are deferred and included in the carrying value of the loan on initial recognition. At the end of each reporting period, the commitments are measured at the higher of (i) the remaining unamortised balance of the amount at initial recognition and (ii) the best estimate of expenditure required to settle the commitment at the end of each reporting period.

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

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 will become effective from 1 January 2019.

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.

Tax reimbursement is available for the current tax paid on the undistributed earnings in the years 2008-2017, if those earnings are distributed in 2019 or further years.

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 recognised in respect of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes. Deferred tax is not recognised for the following temporary differences:

- initial recognition of goodwill not deductible for tax purposes,
- the initial recognition of assets or liabilities in a transaction that is not a business combination and that affects neither accounting nor taxable profit or loss
- temporary differences related to investments in subsidiaries, associates and joint arrangements to the extent that where the Group is able to control the timing of the reversal of the temporary differences and it is probable that they will not reverse in the foreseeable future.

Deferred tax assets are recognised for unused tax losses, unused tax credits and deductible temporary differences to the extent that it is probable that future taxable profits will be available against which they can be used. Future taxable profits are determined based on the reversal of relevant taxable temporary differences. If the amount of taxable temporary differences is insufficient to recognise a deferred tax asset in full, then future taxable profits, adjusted for reversals of existing temporary differences, are considered, based on the business plans for individual subsidiaries in the Group. 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; such reductions are reversed when the probability of future taxable profits improves.

Unrecognised deferred tax assets are reassessed at each reporting date and recognised to the extent that it has become probable that future taxable profits will be available against which they can be used.

In determining the amount of current and deferred tax the Group takes into account the impact of uncertain tax positions and whether additional taxes, penalties and late-payment interest may be due. The Group believes that its accruals for tax liabilities are adequate for all open tax years based on its assessment of many factors, including interpretations of tax law and prior experience. This assessment relies on estimates and assumptions and may involve a series of judgments about future events. New information may become available that causes the Group to change its judgment regarding the adequacy of existing tax liabilities; such changes to tax liabilities will impact the tax expense in the period that such a determination is made.

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 2019, 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 2019 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 2019 and hence, no deferred income tax assets and liabilities will arise, there on.

Premises and equipment

Premises and equipment are carried at cost less accumulated depreciation and any accumulated impairment. Costs of minor repairs and maintenance are expensed when incurred. Costs of replacing major parts or components of premises and equipment items are capitalised and the replaced part is retired.

At the end of each reporting period management assesses whether there is any indication of impairment of premises and equipment. If any such indication exists, management estimates the recoverable amount, which is determined as the higher of an asset's fair value less costs to sell and its value in use. The carrying amount is reduced to the recoverable amount and the impairment loss is recognised in profit or loss for the year. An impairment loss recognised for an asset in prior years is reversed if there has been a change in the estimates used to determine the asset's value in use or fair value less costs to sell.

Gains and losses on disposals determined by comparing proceeds with carrying amount are recognised in profit or loss.

Land is not depreciated. Depreciation on other items of premises and equipment is calculated using the straight-line method to allocate their cost to their residual values over their estimated useful lives:

Premises	25 years
Office and computer equipment	5-15 years
Vehicles	5 years
Furniture, fixtures and other fixed assets	5 years
Leasehold improvements	5-10 years

The residual value of an asset is the estimated amount that the Group would currently obtain from disposal of the asset less the estimated costs of disposal, if the asset were already of the age and in the condition expected at the end of its useful life. The assets' residual values and useful lives are reviewed, and adjusted if appropriate, at the end of each reporting period.

Goodwill

Goodwill represents the excess of the cost of an acquisition over the fair value of the acquirer's share of the identifiable assets, liabilities and contingent liabilities of the acquired subsidiary or associate at the date of exchange. Goodwill on acquisitions of subsidiaries is presented separately in the consolidated statement of financial position. Goodwill is carried at cost less accumulated impairment losses, if any.

The Group tests goodwill for impairment at least annually and whenever there are indications that goodwill may be impaired. Goodwill is allocated to the cash-generating units, or groups of cash-generating units, that are expected to benefit from the synergies of the business combination. Such units or group of units represent the lowest level at which the Group monitors goodwill and are not larger than an operating segment. Gains or losses on disposal of an operation within a cash generating unit to which goodwill has been allocated include the carrying amount of goodwill associated with the operation disposed of, generally measured on the basis of the relative values of the operation disposed of and the portion of the cash-generating unit which is retained.

Impairment is determined by assessing the recoverable amount of the cash-generating unit to which the goodwill relates. Where the recoverable amount of the cash-generating unit is less than the carrying amount, an impairment loss is recognised. Impairment losses relating to goodwill cannot be reversed in future periods.

Intangible assets other than goodwill

Acquired intangible assets are stated at cost less accumulated amortisation and impairment losses. Acquired computer software licenses are capitalised on the basis of the costs incurred to acquire and bring to use the specific software. Amortisation is charged to profit or loss on a straight-line basis over the estimated useful lives of intangible assets. The estimated useful lives range from 3 to 10 years.

Share capital

Share capital

Ordinary shares are classified as equity. Incremental costs directly attributable to the issue of ordinary shares and share options are recognised as a deduction from equity, net of any tax effects.

Dividends

The ability of the Group to declare and pay dividends is subject to the rules and regulations of Georgia. Dividends in relation to ordinary shares are reflected as an appropriation of retained earnings in the period when they are declared.

Recognition of income and expense

Interest income and expense are recognised in profit or loss using the effective interest method.

Loan origination fees, loan servicing fees and other fees that are considered to be integral to the overall profitability of a loan, together with the related transaction costs, are deferred and amortised to interest income over the estimated life of the financial instrument using the effective interest method.

Other fees, commissions and other income and expense items are recognised in profit or loss when the corresponding service is provided.

Payments made under operating leases are recognised in profit or loss on a straight-line basis over the term of the lease. Lease incentives received are recognised as an integral part of the total lease expense, over the term of the lease.

New standards and interpretations not yet adopted

The following new standards, *amendments to standards,* and interpretations are not yet effective as at 31 December 2017, and are not applied in preparing these consolidated financial statements. The Group plans to adopt these pronouncements when they become effective.

The following standards are expected to have a material impact on the Group's financial statements in the period of initial application.

(i) IFRS 9 Financial instruments

In July 2014, the IASB issued the final version of IFRS 9 Financial Instruments. IFRS 9 is effective for annual periods beginning on or after 1 January 2018, with early adoption permitted. It replaces IAS 39 Financial Instruments: Recognition and Measurement.

In October 2017, the IASB issued Prepayment Features with Negative Compensation (Amendments to IFRS 9). The amendments are effective for annual periods beginning on or after 1 January 2019, with early adoption permitted.

The Group will apply IFRS 9 as issued in July 2014 initially on 1 January 2018 and will early adopt the amendments to IFRS 9 on the same date. Based on assessments undertaken to date, the total estimated adjustment (net of tax) of the adoption of IFRS 9 on the opening balance of the Group's equity at 1 January 2018 is approximately GEL 1,441 thousands, representing:

- a reduction of approximately GEL 1,578 thousand related to impairment,;
- an increase of approximately GEL 137 thousand related to deferred tax impacts.
- The above assessment is preliminary because not all transition work has been finalised. The actual impact of adopting IFRS 9 on 1 January 2018 may change because:
- IFRS 9 will require the Group to revise its accounting processes and internal controls and these changes are not yet complete;
- the Group is refining and finalising its models for Expected Credit Loss (ECL) calculations; and
- the new accounting policies, assumptions, judgements and estimation techniques employed are subject to change until the Group finalises its first financial statements that include the date of initial application.

i. Classification – Financial assets

IFRS 9 contains a new classification and measurement approach for financial assets that reflects the business model in which assets are managed and their cash flow characteristics.

IFRS 9 includes three principal classification categories for financial assets: measured at amortised cost, fair value through other comprehensive income (FVOCI) and fair value through profit or loss (FVTPL). It eliminates the existing IAS 39 categories of held to maturity, loans and receivables and available for sale.

A financial asset is measured at amortised cost if it meets both of the following conditions and is not designated as at FVTPL:

- it is held within a business model whose objective is to hold assets to collect contractual cash flows; and
- its contractual terms give rise on specified dates to cash flows that are solely payments of principal and interest (SPPI) on the principal amount outstanding.
- A financial asset is measured at FVOCI only if it meets both of the following conditions and is not designated as at FVTPL:
- it is held within a business model whose objective is achieved by both collecting contractual cash flows and selling financial assets; and
- its contractual terms give rise on specified dates to cash flows that are solely payments of principal and interest on the principal amount outstanding.

On initial recognition of an equity investment that is not held for trading, the Group may irrevocably elect to present subsequent changes in fair value in OCI. This election is made on an investment-by-investment basis.

All financial assets not classified as measured at amortised cost or FVOCI as described above are measured at FVTPL. In addition, on initial recognition the Group may irrevocably designate a financial asset that otherwise meets the requirements to be measured at amortised cost or at FVOCI as at FVTPL if doing so eliminates or significantly reduces an accounting mismatch that would otherwise arise.

A financial asset is classified into one of these categories on initial recognition. See (vii) for the transition requirements relating to classification of financial assets.

Under IFRS 9, derivatives embedded in contracts where the host is a financial asset in the scope of IFRS 9 are not separated. Instead, the hybrid financial instrument as a whole is assessed for classification.

Business model assessment

The Group will make an assessment of the objective of the business model in which a financial asset is held at a portfolio level because this best reflects the way the business is managed and information is provided to management. The information that will be considered includes:

- the stated policies and objectives for the portfolio and the operation of those policies in practice, including whether management's strategy focuses on earning contractual interest revenue, maintaining a particular interest rate profile, matching the duration of the financial assets to the duration of the liabilities that are funding those assets or realising cash flows through the sale of assets;
- how the performance of the portfolio is evaluated and reported to the Group's management;
- the risks that affect the performance of the business model (and the financial assets held within that business model) and how those risks are managed;
- how managers of the business are compensated – e.g. whether compensation is based on the fair value of the assets managed or the contractual cash flows collected; and
- the frequency, volume and timing of sales in prior periods, the reasons for such sales and expectations about future sales activity. However, information about sales activity is not considered in isolation, but as part of an overall assessment of how the Group's stated objective for managing the financial assets is achieved and how cash flows are realised.

Financial assets that are held for trading and those that are managed and whose performance is evaluated on a fair value basis will be measured at FVTPL because they are neither held to collect contractual cash flows nor held both to collect contractual cash flows and to sell financial assets.

Assessment whether contractual cash flows are solely payments of principal and interest

For the purposes of this assessment, 'principal' is defined as the fair value of the financial asset on initial recognition. 'Interest' is defined as consideration for the time value of money, for the credit risk associated with the principal amount outstanding during a particular period of time and for other basic lending risks and costs (e.g. liquidity risk and administrative costs), as well as a profit margin.

In assessing whether the contractual cash flows are solely payments of principal and interest, the Group will consider the contractual terms of the instrument. This will include assessing whether the financial asset contains a contractual term that could change the timing or amount of contractual cash flows such that it would not meet this condition. In making the assessment, the Group will consider:

- Contingent events that would change the amount and timing of cash flows;
- Leverage features;
- Prepayment and extension terms;
- Terms that limit the Group's claim to cash flows from specified assets – e.g. non-recourse asset arrangements;
- Features that modify consideration for the time value of money – e.g. periodic reset of interest rates.

A significant part of the Group's loans contain prepayment features.

A prepayment feature is consistent with the SPPI criterion if the prepayment amount substantially represents unpaid amounts of principal and interest on the principal amount outstanding, which may include reasonable compensation for early termination of the contract.

In addition, a prepayment feature is treated as consistent with this criterion if a financial asset is acquired or originated at a premium or discount to its contractual par amount, the prepayment amount substantially represents the contractual par amount plus accrued (but unpaid) contractual interest (which may also include reasonable compensation for early termination), and the fair value of the prepayment feature is insignificant on initial recognition.

Impact assessment

The standard will affect the classification and measurement of financial assets held as at 1 January 2018 as follows.

- Loans and advances to banks and to customers that are classified as loans and receivables and measured at amortised cost under IAS 39 will in general also be measured at amortised cost under IFRS 9.
- Held-to-maturity investment securities measured at amortised cost under IAS 39 will in general also be measured at amortised cost under IFRS 9.

ii. Impairment – Financial assets, loan commitments and financial guarantee contracts

IFRS 9 replaces the 'incurred loss' model in IAS 39 with a forward-looking 'expected credit loss' (ECL) model. This will require considerable judgement over how changes in economic factors affect ECLs, which will be determined on a probability-weighted basis.

The new impairment model applies to the following financial instruments that are not measured at FVTPL:

- financial assets that are debt instruments;
- lease receivables; and
- loan commitments and financial guarantee contracts issued (previously, impairment was measured under IAS 37 *Provisions, Contingent Liabilities and Contingent Assets*).

IFRS 9 requires a loss allowance to be recognised at an amount equal to either 12-month ECLs or lifetime ECLs. Lifetime ECLs are the ECLs that result from all possible default events over the expected life of a financial instrument, whereas 12-month ECLs are the portion of ECLs that result from default events that are possible within the 12 months after the reporting date.

The Group will recognise loss allowances at an amount equal to lifetime ECLs, except in the following cases, for which the amount recognised will be 12-month ECLs:

Financial instruments for which credit risk has not increased significantly since initial recognition.

The impairment requirements of IFRS 9 are complex and require management judgements, estimates and assumptions, particularly in the following areas, which are discussed in detail below:

- assessing whether the credit risk of an instrument has increased significantly since initial recognition; and
- incorporating forward-looking information into the measurement of ECLs.

Measurement of ECLs

ECLs are a probability-weighted estimate of credit losses and will be measured as follows:

- *financial assets that are not credit-impaired at the reporting date:* the present value of all cash shortfalls – i.e. the difference between the cash flows due to the entity in accordance with the contract and the cash flows that the Group expects to receive;
- *financial assets that are credit-impaired at the reporting date:* the difference between the gross carrying amount and the present value of estimated future cash flows;
- *undrawn loan commitments:* the present value of the difference between the contractual cash flows that are due to the Group if the commitment is drawn down and the cash flows that the Group expects to receive; and
- *financial guarantee contracts:* the present value of the expected payments to reimburse the holder less any amounts that the Group expects to recover.

Definition of default

Under IFRS 9, the Group will consider a financial asset to be in default when any of the following have occurred:

- Loans are past due more than 90 days;
- Bankruptcy proceedings and/or legal proceedings that may affect the company's ability to service its obligations
- Death of borrower, liquidation of the borrower's company (if legal entity);
- Any other events that may affect the borrower's ability to repay the loan.

Inputs into the assessment of whether a financial instrument is in default and their significance may vary over time to reflect changes in circumstances.

Significant increase in credit risk

Under IFRS 9, when determining whether the credit risk (i.e. risk of default) on a financial instrument has increased significantly since initial recognition, the Group will consider reasonable and supportable information that is relevant and available without undue cost or effort, including both quantitative and qualitative information and analysis based on the Group’s historical experience, expert credit assessment and forward-looking information.

The Group will recognize that a significant increase in credit risk has occurred for an exposure if:

- The exposure is overdue for more than 30 days for collectively assessed loans and 15 days for individually significant clients.
- Its financial standing deteriorated and the exposure has been restructured;
- Other weaknesses that the bank deems to have negative effect on borrower’s performance. (e.g. watch list clients)
- The Group will monitor the effectiveness of the criteria used to identify significant increases in credit risk by regular reviews to confirm that:
- The criteria are capable of identifying significant increases in credit risk before an exposure is in default;
- The criteria do not align with the point in time when an asset becomes 30 days past due;
- The average time between the identification of a significant increase in credit risk and default appears reasonable;
- Exposures are not generally transferred directly from 12-month ECL measurement to credit-impaired; and there is no unwarranted volatility in loss allowance from transfers between 12-month ECL and lifetime ECL measurements

Generating the term structure of Probability of Default (“PD”)

The Group will collect performance and default information about its credit risk exposures analysed by type of product and borrower. For some portfolios, information purchased from external credit reference agencies may also be used for individually assessed clients.

The Group will employ statistical models to analyse the data collected and generate estimates of the remaining lifetime PD of exposures and how these are expected to change as a result of the passage of time.

This analysis will include the identification and calibration of relationships between changes in default rates and changes in key macro-economic factors, as well as in-depth analysis of the impact of certain other factors (e.g. forbearance experience) on the risk of default. For most exposures, key macro-economic indicator is likely to be GDP growth.

The Group's approach to incorporating forward-looking information into this assessment is discussed below.

Modified financial assets

The contractual terms of a loan may be modified for a number of reasons, including changing market conditions, customer retention and other factors not related to a current or potential credit deterioration of the customer. An existing loan whose terms have been modified may be derecognised and the renegotiated loan recognised as a new loan at fair value.

The Group renegotiates loans to customers in financial difficulties (referred to as 'forbearance activities') to maximise collection opportunities and minimise the risk of default. Under the Group's forbearance policy, loan forbearance is granted on a selective basis if the debtor is currently in default on its debt or if there is a high risk of default, there is evidence that the debtor made all reasonable efforts to pay under the original contractual terms and the debtor is expected to be able to meet the revised terms.

The revised terms usually include extending the maturity, changing the timing of interest payments and amending the terms of loan covenants. Both retail and corporate loans are subject to the forbearance policy. The Group Credit Committee regularly reviews reports on forbearance activities. Restructuring is a qualitative indicator of significant increase in credit risk, as well as default and credit impairment. So the Group considers such client as modified and loss allowance is measured at an amount equal to lifetime ECLs.

Inputs into measurement of ECLs

The key inputs into the measurement of ECLs are likely to be the term structures of the following variables:

- PD;
- loss given default (LGD); and
- exposure at default (EAD).
- effective interest rate (EIR).

These parameters will be derived from internally developed statistical models and other historical data. They will be adjusted to reflect forward-looking information as described below.

PD estimates are estimates at a certain date, which is calculated based on historical overdue behavior and assessed using transition matrixes tailored to the various categories of counterparties and exposures. These statistical models is based on internally compiled data comprising both quantitative and qualitative factors. Where it is available, market data may also be used to derive the PD for large corporate counterparties. If a counterparty or exposure migrates between risk categories, then this will lead to a change in the estimate of the associated PD. PDs will be estimated considering the contractual maturities of exposures.

LGD is the magnitude of the likely loss if there is a default. The Group will estimate LGD parameters based on the history of recovery rates of claims against defaulted counterparties. They will be calculated on a discounted cash flow basis using the effective interest rate as the discounting factor.

EAD represents the expected exposure in the event of a default. The Group will derive the EAD from the current exposure to the counterparty and potential changes to the current amount allowed under the contract. The EAD of a financial asset will be the gross carrying amount at default. For lending commitments and financial guarantees, the EAD will consider the amount drawn.

As described above, and subject to using a maximum of a 12-month PD for financial assets for which credit risk has not significantly increased, the Group will measure ECLs considering the risk of default over the maximum contractual period (including any borrower's extension options) over which it is exposed to credit risk, even if, for risk management purposes, the Group considers a longer period. The maximum contractual period extends to the date at which the Group has the right to require repayment of an advance or terminate a loan commitment or guarantee.

Where modelling of a parameter is carried out on a collective basis, the financial instruments will be grouped on the basis of shared risk characteristics that include:

- instrument type;
- collateral type;
- remaining term to maturity;

The groupings will be subject to regular review to ensure that exposures within a particular group remain appropriately homogeneous.

Forward-looking information

Under IFRS 9, the Group will incorporate forward-looking information into its measurement of ECLs. The Group uses expert judgment of the Groups asset-liability committee (ALCO) in assessment of forward-looking information. This assessment is based also on external information. External information may include economic data and forecasts published by governmental bodies and monetary authorities in the countries where the Group operates, such as the National Bank of Georgia.

The Group will also periodically carry out stress-testing of more extreme shocks to calibrate its determination of these other representative scenarios.

The Group has identified and documented key drivers of credit risk and credit losses for each portfolio of financial instruments and, using an analysis of historical data, has estimated relationships between macro-economic variable and credit risk and credit losses. This key driver is GDP forecasts. Predicted relationships between the key indicator and default and loss rates on various portfolios of financial assets have been developed based on analysing historical data over the past 4 years.

Impact assessment

The most significant impact on the Group's financial statements from the implementation of IFRS 9 is expected to result from the new impairment requirements. Impairment losses will increase and become more volatile for financial instruments in the scope of the IFRS 9 impairment model.

The Group has estimated that, on the adoption of IFRS 9 at 1 January 2018, the impact of the increase in loss allowances (before tax) will be approximately GEL 1,578 thousand. Loss allowances on unsecured products with longer expected lives such as overdrafts and credit cards will be most affected by the new impairment requirements.

iii. Classification – Financial liabilities

IFRS 9 largely retains the existing requirements in IAS 39 for the classification of financial liabilities.

iv. Derecognition and contract modification

IFRS 9 incorporates the requirements of IAS 39 for the derecognition of financial assets and financial liabilities without substantive amendments.

However, it contains specific guidance for the accounting when the modification of a financial instrument not measured at FVTPL does not result in derecognition. Under IFRS 9, the Group will recalculate the gross carrying amount of the financial asset (or the amortised cost of the financial liability) by discounting the modified contractual cash flows at the original effective interest rate and recognise any resulting adjustment as a modification gain or loss in profit or loss. Under IAS 39, the Group does not recognise any gain or loss in profit or loss on modifications of financial liabilities and non-distressed financial assets that do not lead to their derecognition.

The Group expects an immaterial impact from adopting these new requirements.

v. Disclosures

IFRS 9 will require extensive new disclosures, in particular about hedge accounting, credit risk and ECLs.

vi. Impact on capital planning

Currently the Group assesses that the adoption of IFRS 9 will not have impact on statutory capital of the Group; however, further developments in the regulatory environment in respect of this aspect may take place in the near future.

vii. Transition

Changes in accounting policies resulting from the adoption of IFRS 9 will generally be applied retrospectively, except as described below.

— The Group will take advantage of the exemption allowing it not to restate comparative information for prior periods with respect to classification and measurement (including impairment) changes. Differences in the carrying amounts of financial assets and financial liabilities resulting from the adoption of IFRS 9 will generally be recognised in retained earnings and reserves as at 1 January 2018.
— The following assessments have to be made on the basis of the facts and circumstances that exist at the date of initial application.
— The determination of the business model within which a financial asset is held.
— The designation of certain investments in equity instruments not held for trading as at FVOCI.
— If a debt investment security has low credit risk at 1 January 2018, then the Group will determine that the credit risk on the asset has not increased significantly since initial recognition.

(ii) IFRS 15 Revenue from Contracts with Customers

IFRS 15 *Revenue from Contracts with Customers* establishes a comprehensive framework for determining whether, how much and when revenue is recognised. It replaces existing revenue recognition guidance, including IAS 18 *Revenue*, IAS 11 *Construction Contracts* and IFRIC 13 *Customer Loyalty Programmes*. The core principle of the new standard is that an entity recognises revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. The new standard results in enhanced disclosures about revenue, provides guidance for transactions that were not previously addressed comprehensively and improves guidance for multiple-element arrangements. IFRS 15 is effective for annual reporting periods beginning on or after 1 January 2018, with early adoption permitted. The Group has not adopted this standard early. IFRS 15 is not expected to have a significant impact on the Group's consolidated financial statements

(iii) IFRS 16 Leases

IFRS 16 replaces existing leases guidance including IAS 17 Leases, IFRIC 4 Determining whether an Arrangement contains a Lease, SIC-15 Operating Leases—Incentives and SIC-27 Evaluating the Substance of Transactions Involving the Legal Form of a Lease.

The standard is effective for annual periods beginning on or after 1 January 2019. Early adoption is permitted for entities that apply IFRS 15 at or before the date of initial application of IFRS 16.

IFRS 16 introduces a single, on-balance sheet lease accounting model for lessees. A lessee recognises a right-of-use asset representing its right to use the underlying asset and a lease liability representing its obligation to make lease payments. There are recognition exemptions for short-term leases and leases of low value items. Lessor accounting remains similar to the current standard – i.e. lessors continue to classify leases as finance or operating leases.

The Group has completed an initial assessment of the potential impact on its consolidated financial statements but has not yet completed its detailed assessment. The actual impact of applying IFRS 16 on the consolidated financial statements in the period of initial application will depend on future economic conditions, including the Group's borrowing rate at 1 January 2019, the composition of the Group's lease portfolio at that date, the Group's latest assessment of whether it will exercise any lease renewal options and the extent to which the Group chooses to use practical expedients and recognition exemptions.

In addition, the nature of expenses related to those leases will now change as IFRS 16 replaces the straight-line operating lease expense with a depreciation charge for right-of-use assets and interest expense on lease liabilities. The Group is assessing the potential impact on its consolidated financial statements. The following amended standards and interpretations are not expected to have a significant impact on the Group's consolidated financial statements.

- *Annual Improvements to IFRSs 2014-2016 Cycle – Amendments to IFRS 1 and IAS 28.*
- *Classification and Measurement of Share-based Payment Transactions (Amendments to IFRS 2).*
- *Transfers of Investment Property (Amendments to IAS 40).*
- *Sale or Contribution of Assets between an Investor and its Associate or Joint Venture (Amendments to IFRS 10 and IAS 28).*
- *IFRIC 22 Foreign Currency Transactions and Advance Consideration.*
- *IFRIC 23 Uncertainty over Income Tax Treatments.*

4. Cash and cash equivalents

GEL'000	2017	2016
Cash on hand	**42,289**	**36,834**
Nostro accounts with the NBG	**15,573**	**13,809**
Current accounts with other credit institutions		
- rated A- to A+	20,156	3,530
- rated BBB to BBB+	205	33,703
- rated from BB- to BB+	10,399	3,619
- not rated	181	60
Total current accounts with other credit institutions	**30,941**	**40,912**
Total cash and cash equivalents	**88,803**	**91,555**

No cash and cash equivalents are impaired or past due.

As at 31 December 2017 the Group has no banks (2016: 1 bank), whose balance exceeds 10% of equity. The gross value of the balance in 2016 was GEL 33,514 thousand.

5. Investment securities

Investment securities of GEL 53,333 thousand (2016: GEL 29,465 thousand) represent debt securities of the Government of Georgia. All investment securities are denominated in GEL and their contractual interest rates and maturities are as follows:

	31 December 2017		**31 December 2016**	
	Nominal interest rate, %	**Maturity**	**Nominal interest rate, %**	**Maturity**
Debt securities of the Ministry of Finance	7 – 14	2018 - 2022	7 – 14	2017 - 2020

No investment securities are impaired or past due.

6. Loans to customers

GEL'000	2017	2016
Business loans	235,007	184,893
Consumer loans	194,510	147,710
Gold pawn loans	105,564	95,956
Mortgage loans	59,467	38,268
Gross loans to customers	**594,548**	**466,827**
Less: allowance for impairment	(34,606)	(31,884)
Net loans to customers	**559,942**	**434,943**

(a) Industry and geographical analysis of the loan portfolio

Loans to customers were issued primarily to customers located within Georgia who operate in the following economic sectors:

GEL'000	2017	2016
Individuals	253,977	185,978
Gold pawn lending sector	105,564	95,956
Trading and service	105,118	85,121
Construction sector	62,370	40,863
Financial institutions	11,086	18,289
Healthcare	14,041	15,793
Energy	22,829	15,248
Agriculture and food processing	17,842	7,027
Other	1,721	2,552
Gross loans to customers	**594,548**	**466,827**

(b) Significant credit exposures

As at 31 December 2017 and 2016 none of the Group's borrower's balance exceeds 10% of equity.

As at 31 December 2017, the Group had a concentration of loans represented by GEL 84,163 thousand due from the ten largest third party borrowers (2016: GEL 79,400 thousand). An allowance of GEL 5,248 thousand (2016: GEL 4,073 thousand) was recognised against these loans. For details of credit quality, please see note 21.

(c) Movement in allowance for impairment of loans to customers

GEL'000	Business loans	Consumer loans	Mortgage loans	Gold pawn loans	Total
At 1 January 2017	5,780	7,797	1,702	16,605	31,884
Charge for the year	44	2,398	237	1,782	4,461
Recoveries	23	863	119	2	1,007
Amounts written off	(205)	(2,398)	(97)	(46)	(2,746)
At 31 December 2017	**5,642**	**8,660**	**1,961**	**18,343**	**34,606**
Individual impairment	1,246	473	140	18,317	20,176
Collective impairment	4,396	8,187	1,821	26	14,430
	5,642	**8,660**	**1,961**	**18,343**	**34,606**
Gross amount of loans, individually determined to be impaired, before deducting any individually assessed impairment allowance	**7,621**	**815**	**364**	**36,406**	**45,206**

GEL'000	Business loans	Consumer loans	Mortgage loans	Gold pawn loans	Total
At 1 January 2016	6,400	6,153	1,897	11,656	26,106
Charge for the year	(174)	5,253	(14)	4,949	10,014
Recoveries	107	766	37	-	910
Amounts written off	(553)	(4,375)	(218)	-	(5,146)
At 31 December 2016	**5,780**	**7,797**	**1,702**	**16,605**	**31,884**
Individual impairment	1,256	417	223	16,605	18,501
Collective impairment	4,524	7,380	1,479	-	13,383
	5,780	**7,797**	**1,702**	**16,605**	**31,884**
Gross amount of loans, individually determined to be impaired, before deducting any individually assessed impairment allowance	**7,477**	**417**	**479**	**36,196**	**44,569**

(d) Key assumptions and judgments for estimating loan impairment

The Group estimates loan impairment for loans to customers based on an analysis of the future cash flows for loans with individual signs of impairment and based on its past loss experience for portfolios of loans for which no individual signs of impairment has been identified.

As at 31 December 2017, GEL 549,342 thousand of the gross loan portfolio (2016: GEL 422,258 thousand) was assessed on a collective basis and GEL 14,430 thousand (2016: GEL 13,383 thousand) of loan loss allowance was created against it, which represents 2.63% (2016: 3.17%) of loss rate on the loan portfolio assessed collectively. In determining the impairment allowance for loans to customers, management uses estimates based on historical loss experience of the past 3 years for assets with credit risk characteristics and objective evidence of impairment similar to those in the group of loans.

As at 31 December 2017, GEL 45,206 thousand (2016: GEL 44,569 thousand) of the gross loan portfolio was determined to be individually impaired and an allowance of GEL 20,176 thousand (2016: GEL 18,501 thousand) was created. The Group makes individual assessment of the loan loss allowance as the difference between the carrying amount of the loan and the present value of estimated future cash flows for loans to customers for which the Group assessed that a loss event exists. The future cash flows are determined as the value of the collateral pledged and expected future repayments, discounted for the delay of approximately 2 years in obtaining proceeds from the foreclosure of collateral. The management monitors market value of the collateral on a regular basis and seeks for the independent expert opinion, where applicable. Determination of a loss event primarily depends on the borrowers’ debt service.

The loan loss allowance on gold pawn loans is mainly attributable to the loans that were provided as a result of the fraudulent activity by the Group employees in 2015 and previous years. Particularly, for some gold pawn loans the overstated amount of collateral received was recorded, therefore loan collateralization was inadequate. The Group hired an independent external appraiser to examine and revalue potentially suspicious collateral. The revaluation of collateral by the independent external appraiser revealed instances of loan disbursements in breach of the Group’s policies and credit limits. As a result, an individual impairment loss was recognized in respect of the gold pawn loans.

(e) Analysis of collateral and other credit enhancements

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 generally requests borrowers to provide it.

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

The main types of collateral obtained are as follows:

- for gold pawn lending- gold and other precious metals and jewelry (“Precious Metals”);
- for commercial lending- real estate properties, movable property, and inventory;
- for retail lending- real estate, vehicles and other movable properties.

Management ensures, that the major part of the business loans, gold pawn loans and mortgage loans are fully covered by the market value of the collateral.

GEL’000	**Net exposures**					
At 31 December 2017	**Real estate**	**Cash collateral**	**Other**	**No collateral**	**Precious Metals**	**Total**
Business loans	191,294	18,879	18,827	365	-	229,365
Consumer loans	138,301	3,367	931	43,220	-	185,819
Mortgage loans	57,421	38	75	3	-	57,537
Gold pawn loans	1,558	3,558	-	1,248	80,857	87,221
Total	**388,574**	**25,842**	**19,833**	**44,836**	**80,857**	**559,942**

GEL'000	Net exposures					
At 31 December 2016	**Real estate**	**Cash collateral**	**Other**	**No collateral**	**Precious Metals**	**Total**
Business loans	142,600	18,167	15,776	1,560	1,010	179,113
Consumer loans	86,202	2,198	1,028	50,485	-	139,913
Mortgage loans	36,187	-	-	379	-	36,566
Gold pawn loans	491	-	-	3,169	75,691	79,351
Total	**265,480**	**20,365**	**16,804**	**55,593**	**76,701**	**434,943**

The tables above excludes overcollateralisation. For loans secured by multiple types of collateral, collateral that is most relevant for impairment assessment is disclosed. The majority of the loans with no collateral represents payroll loans, which include loans secured with personal guarantees.

(f) Repossessed property

Repossessed property mainly represents real estate assets acquired by the Group in settlement of overdue loans. These assets are treated as inventories, are recognized at net book value of the respective loan when acquired and subsequently measured at the lower of cost and net realizable value. The Group's policy is to sell the repossessed property as soon as it is practicable.

7. Premises and equipment

GEL'000	Land	Premises	Office and computer equipment	Vehicles	Furniture, fixtures and other fixed assets	Leasehold improvements	Total
Cost							
As at 1 January 2016	449	13,813	5,979	676	6,174	2,837	29,928
Additions	-	1,353	1,136	5	1,453	187	4,134
Disposals	-	-	(236)	-	(175)	(5)	(416)
Transfers	-	(63)	-	-	27	36	-
As at 31 December 2016	**449**	**15,103**	**6,879**	**681**	**7,479**	**3,055**	**33,646**
As at 1 January 2017	449	15,103	6,879	681	7,479	3,055	33,646
Additions	-	1,450	284	16	1,124	98	2,972
Disposals	-	-	-	-	(64)	(983)	(1,047)
Transfers	-	(1,100)	-	-	-	1,100	-
As at 31 December 2017	**449**	**15,453**	**7,163**	**697**	**8,539**	**3,270**	**35,571**
Accumulated depreciation							
As at 1 January 2016	-	2,589	3,268	522	5,159	2,294	13,832
Depreciation charge	-	590	739	78	418	252	2,077
Disposals	-	-	(236)	-	(175)	(6)	(417)
As at 31 December 2016	**-**	**3,179**	**3,771**	**600**	**5,402**	**2,540**	**15,492**
As at 1 January 2017	-	3,179	3,771	600	5,402	2,540	15,492
Depreciation charge	-	645	816	57	630	213	2,361
Disposals	-	-	-	-	(62)	(962)	(1,024)
As at 31 December 2017	**-**	**3,824**	**4,587**	**657**	**5,970**	**1,791**	**16,829**
Net book value							
1 January 2016	**449**	**11,224**	**2,711**	**154**	**1,015**	**543**	**16,096**
31 December 2016	**449**	**11,924**	**3,108**	**81**	**2,077**	**515**	**18,154**
31 December 2017	**449**	**11,629**	**2,576**	**40**	**2,569**	**1,479**	**18,742**

8. Goodwill

Goodwill of GEL 20,374 thousand fully relates to the acquisition of JSC Standard Bank in 2008 by JSC Kor. JSC Kor was established as a commercial bank with a view of acquiring JSC Standard Bank and had no operations of its own prior to business combination.

The Group is considered as a one cash-generating unit (the CGU) for the impairment test purposes. The recoverable amount of the CGU is based on the value in use, estimated using discounted cash flows.

The key assumptions used in the estimation of the recoverable amount are set out below. The values assigned to the key assumptions represented management's assessment of future trends in the banking industry, projected growth rate of the country's economy and were based on historical data from both external and internal sources.

In percent	**2017**	**2016**
Discount rate	10.2%	10.6%
Terminal value growth rate	5.5%	5.0%
Budgeted growth rate of free cash flows (average of next five years)	5.5%	5.0%

The discount rate reflects the required rate of return for the cash flows on the invested capital of similar companies denominated in USD.

The estimated recoverable amount of the CGU exceeded its carrying amount. Management believes that no reasonably possible change in any of the key assumptions would cause the carrying amount of the CGU to exceed its recoverable amount.

9. Taxation

GEL '000	**2017**	**2016**
Current tax expense		
Current year	-	-
Movement in temporary differences due to origination and reversal of temporary differences	39	282
Total income tax benefit	**39**	**282**

In 2017, the applicable tax rate for current and deferred tax is 15% (2016: 15%).

Reconciliation of effective tax rate:

GEL'000	**2017**	**%**	**2016**	**%**
Profit before income tax	**11,883**		**5,254**	
Income tax at the applicable tax rate	(1,782)	(15)	(788)	(15)
Change in unrecognized deferred tax asset	654	6	(847)	(16)
Change in unrecognised deferred tax liabilities due to change in the legislation (note 3)	658	6	1,423	27
Net non-taxable income	509	4	494	9
	39	**1**	**282**	**5**

Movement in temporary differences during the year

GEL'000	**1 January 2017**	**Recognised in profit or loss**	**31 December 2017**
Loans to customers	(1,437)	496	(941)
Goodwill and other intangible assets	66	359	425
Tax loss carry-forwards	1,380	(436)	944
Other	(324)	(380)	(704)
	(315)	**39**	**(276)**

GEL'000	1 January 2016	Recognised in profit or loss	31 December 2016
Loans to customers	877	(2,314)	(1,437)
Goodwill and other intangible assets	(1,789)	1,855	66
Tax loss carry-forwards	115	1,265	1,380
Other	200	(524)	(324)
	(597)	**282**	**(315)**

Tax loss carry-forwards

Deferred tax assets have not been recognised in respect of the following items:

GEL'000	31 December 2017	31 December 2016
Tax loss carry-forwards	**193**	**847**

The Group's tax loss carry-forwards by expiration date comprise:

GEL'000	31 December 2017	31 December 2016
2019	-	115
2021	1,137	2,112
	1,137	**2,227**

In accordance with the Georgian tax legislation, tax losses may be carried forward for up to 5 years. However due the changes in the Georgian tax legislation (Note 3), tax losses will expire from 1 January 2019. Deferred tax asset of GEL 944 thousand is recognised only to the extent that it is probable that future taxable profits will be available against which unused tax losses can be utilised.

According to the Georgian government's latest announcements, the Banking sector's transition to the new taxation legislation system (Note 3) will be effective from 1 January 2023, instead of 1 January 2019. Despite the fact that the Georgian tax code has not yet been amended, the Management believes that the government's public announcement will be reflected in the tax code.

10. Loans from financial institutions

			31 December 2017		31 December 2016	
'000 GEL	Currency	Year of maturity	Face value	Carrying amount	Face value	Carrying amount
Black Sea Trade and Development Bank (BSTDB)	USD	2018	9,934	9,934	10,696	10,696
Nederlandse Financierings-Maatschappij Voor Ontwikkelingslanden N.V. ("FMO")	GEL	2023	31,260	31,260	-	-
Loans from NBG	GEL	2018	24,020	24,020	-	-
Total			**65,214**	**65,214**	**10,696**	**10,696**

Due to liquidity management purposes the bank received short term loans from NBG with original maturities of less than 3 months comprising GEL 24,020 thousand.

The Group has complied with all the financial covenants stipulated by lending agreements as at 31 December 2017 and 31 December 2016.

11. Subordinated loans

			31 December 2017		31 December 2016	
'000 GEL	Currency	Year of maturity	Face value	Carrying amount	Face value	Carrying amount
Standard Capital Georgia Ltd	USD	2025	6,268	6,268	7,183	7,183
Standard Capital Georgia Ltd	USD	2026	4,696	4,696	5,341	5,341
Dhabi Contracting*	USD	2023	20,742	20,742	21,181	21,181
Total subordinated loans			**31,706**	**31,706**	**33,705**	**33,705**

In case of bankruptcy, the repayment of the subordinated loans will be made after repayment in full of all other liabilities of the Group.

***** In 2016 the subordinated loan of USD 2,000 thousand (GEL 4,938 thousand) was settled against the issue of the share capital of the Bank (note 16).

12. Reconciliation of movements of liabilities to cash flows arising from financing activities

The table below sets out an analysis of the movements in liabilities that are reported as financing in the statement of cash flows for the period presented.

GEL'000	Loans from financial institutions	Subordinated loans	Total
Balance at 1 January 2017	10,696	33,705	44,401
Cash flow from financing activities	**53,109**	**(1,271)**	**51,838**
Receipts of loans	59,467	-	59,467
Repayment of the loans	(6,358)	(1,271)	(7,629)
Foreign exchange adjustments	592	(740)	(148)
Other non-cash movements	817	12	829
Balance at 31 December 2017	**65,214**	**31,706**	**96,920**

Due to the amendments being issued one year before the effective date, the Group need not provide comparative information as it applied the amendment for the first time.

13. Deposits and balances from banks

GEL'000	2017	2016
Time deposits from banks	16,785	-
Short-term placements of other banks	167	416
Total deposits and balances from banks	**16,952**	**416**

14. Current accounts and deposits from customers

GEL'000	2017	2016
Current accounts	139,371	241,063
Time deposits	440,255	279,539
Total current account and deposits from customers	**579,626**	**520,602**
Held as a security against guarantees and letters of credit issued	**18,367**	**14,197**

As at 31 December 2017, the Group has 7 customers (2016: 12 customers), whose balances exceed 10% of equity. These balances as at 31 December 2017 are GEL 161,225 thousand (2016: GEL 226,227 thousand).

GEL'000	2017	2016
Private enterprises	317,861	301,533
Individuals	204,355	145,472
State and budgetary organizations	57,410	73,597
Total current account and deposits from customers	**579,626**	**520,602**

An analysis of amounts due to customers by economic sector is as follows:

GEL'000	2017	2016
Individuals	204,355	145,472
State and budgetary organizations	57,410	73,597
Trade and service	104,511	51,791
Energy	27,870	43,461
Transport and communication	23,392	42,323
Construction	46,372	39,826
Non-banking credit organizations	19,137	19,220
Insurance	9,229	15,943
Mining	2,771	3,269
Other	84,579	85,700
Total current account and deposits from customers	**579,626**	**520,602**

15. Other liabilities

GEL'000	2017	2016
Swap agreements	-	6,917
Settlement on plastic card and money transfer operations	8,010	2,687
Accrued Employee Benefit Costs	2,764	675
Financial liabilities from services received	598	654
Other	561	456
Total other financial liabilities	**11,933**	**11,389**
Provisions for guarantees and credit related commitments	548	360
Other provisions	1,755	250
Other	321	409
Total other liabilities	**14,557**	**12,408**

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

	2017		2016	
GEL'000	Notional amount	Fair value liabilities/(assets)	Notional amount	Fair value liabilities
Foreign exchange contracts				
Swaps – domestic	32,878	(111)	34,439	6,917

16. Equity

Number of shares	Ordinary shares	
	2017	2016
In issue at 1 January	1,213,720	1,110,000
Issued in cash, fully paid	-	54,329
Set off with the subordinated loan (note 11)	-	49,391
In issue at 31 December, fully paid	**1,213,720**	**1,213,720**
Authorised shares - par value	**100**	**100**

All ordinary shares rank equally with regard to the Bank's residual assets.

Ordinary shares

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 meetings of the Bank. No dividends were declared or paid in 2017 and 2016.

17. Net interest income

GEL'000	2017	2016
Loans to customers	58,344	58,751
Investment securities	3,824	3,172
Cash and cash equivalents and mandatory reserve with the NBG	912	1,170
Total interest income	**63,080**	**63,093**
Current accounts and deposits from customers	23,342	31,003
Loans from financial institutions	3,962	2,355
Subordinated loans	2,175	2,671
Total interest expense	**29,479**	**36,029**
Net interest income	**33,601**	**27,064**

18. Fee and commission income and expenses

GEL'000	2017	2016
Plastic card transactions	3,084	2,578
Settlement transactions	1,638	1,338
Guarantees and letters of credit issued	1,166	800
Cash transactions	570	995
Other	963	589
Total fee and commission income	**7,421**	**6,300**
Plastic card transactions	2,777	2,415
Cash transactions	544	377
Settlement transactions	400	442
Other	329	322
Total fee and commission expenses	**4,050**	**3,556**
Net fee and commission income	**3,371**	**2,744**

19. Other operating expenses

GEL'000	2017	2016
Operating lease expenses	2,424	2,073
Advertising and marketing services	1,511	1,381
Professional services	1,300	1,169
Repair and maintenance	735	692
Taxes other than on income	535	596
Communications	409	370
Insurance	401	255
Transportation and cash collection	386	373
Security expense	374	369
Representative expenses	298	546
Office supply	280	329
Business trip expenses	108	122
Plastic card expenses	66	161
Other	891	973
Total other operating expenses	**9,718**	**9,409**

For 2017, professional fees paid to financial auditors comprised GEL 96 thousand (2016:GEL 108 thousand).

20. Credit related commitments

The Group has outstanding credit related commitments to extend loans. These credit related commitments take the form of approved loans and credit card limits and overdraft facilities. The Group 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 three years.

The Group 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 to customers.

The contractual amounts of credit related commitments are set out in the following table by category. The amounts reflected in the table for credit related commitments assume that amounts are fully advanced. The amounts reflected in the table for guarantees and letters of credit represent the maximum accounting loss that would be recognised at the reporting date if the counterparties failed completely to perform as contracted.

GEL'000	2017	2016
Credit related commitments		
Guarantees	55,708	33,352
Letters of credit	1,122	386
Total credit related commitments	**56,830**	**33,738**
Less: cash held as security against guarantees and letters of credit	(18,367)	(14,197)
Net exposure to guarantees and letters of credit	**38,463**	**19,541**
Undrawn loan commitments	**5,574**	**5,102**

21. Risk management

Management of risk is fundamental to the business of banking and forms an essential element of the Group's operations. The major risks faced by the Group are those related to market risk, credit risk, liquidity risk, and operational, legal and reputational risks.

The risk management policies aim to identify, analyse and manage the risks faced by the Group, to set appropriate risk limits and controls, and to continuously monitor risk levels and adherence to limits. Risk management policies and procedures are reviewed regularly to reflect changes in market conditions, products and services offered and emerging best practice. The Group has developed a system of reporting on significant risks and capital.

As at 31 December 2017, the Group's internal documentation establishing the procedures and methodologies for identification, managing and stress-testing the Group's significant risks, was approved by the authorized management bodies of the Group in accordance with regulations and recommendations issued by the NBG.

The Board of Directors has overall responsibility for the oversight of the risk management framework, overseeing the management of key risks and reviewing its risk management policies and procedures as well as approving significantly large exposures.

The management is responsible for monitoring and implementing risk mitigation measures, and ensuring that the Group operates within established risk parameters. The Head of the Risk Department is responsible for the overall risk management and compliance functions, ensuring the implementation of common principles and methods for identifying, measuring, managing and reporting both financial and non-financial risks. He reports directly to the Chief Executive Officer and indirectly to the Board of Directors.

The Supervisory Board has responsibility for controlling the Group's compliance with risk limits and capital adequacy ratios as established by the Group's internal documentation. With the view of controlling effectiveness of the Group's risk management procedures and their consistent application the Supervisory Board and management bodies of the Group periodically receive reports prepared by the internal audit function and the Risk Department, discuss the contents of these reports and consider proposed corrective actions.

Credit, market and liquidity risks, both at the portfolio and transactional levels, are managed and controlled through a system of Credit Committees and an Asset and Liability Management Committee (ALCO). In order to facilitate efficient and effective decision-making, the Group established a hierarchy of credit committees, depending on the type and amount of the exposure.

Both external and internal risk factors are identified and managed throughout the organisation. Particular attention is given to identifying the full range of risk factors and determining the level of assurance over current risk mitigation procedures. Apart from the standard credit and market risk analysis, the Risk Department monitors financial and non-financial risks by holding regular meetings with operational units in order to obtain expert judgments in their respective areas of expertise.

Credit risk

The Group takes on exposure to credit risk, which is the risk that one party to a financial instrument will cause a financial loss for the other party by failing to discharge an obligation. Exposure to credit risk arises primary as a result of the Group's lending and other transactions with counterparties giving rise to financial assets.

The Group structures the levels of credit risk it undertakes by placing limits on the amount of risk accepted in relation to one borrower, or groups of borrowers. The Group further established 3 levels of credit committees which are responsible for approving credit limits for individual borrowers. Review and approval limits for each credit committee differs per loan type. Only retail loans with the maximum amount of GEL 20 thousand are issued on branch level. Loan applications originated by the relevant client relationship managers are passed on to the relevant credit committee for approval of credit limit.

In order to monitor credit risk exposures, regular reports are produced by the portfolio analysis manager and reviewed by the credit risk department. Monitoring includes review of the customer's financial performance.

The financial assets of the Group exposed to credit risk can be analysed as follows:

	Neither past due nor impaired					
2017	**High grade**	**Standard**	**Sub-standard**	**Past due but not impaired**	**Individually impaired**	**Total**
Cash and cash equivalents	46,514	-	-	-	-	46,514
Mandatory reserve deposit with the NBG	76,551	-	-	-	-	76,551
Loans to customers						
Consumer loans	3,369	132,327	43,594	14,405	815	194,510
Business loans	5,660	163,371	51,280	7,075	7,621	235,007
Mortgage loans	39	56,960	419	1,685	364	59,467
Gold pawn loans	62,350	1,342	5,430	36	36,406	105,564
	71,418	**354,000**	**100,723**	**23,201**	**45,206**	**594,548**
Investment securities	53,333	-	-	-	-	53,333
Other financial assets	2,201	-	-	227	-	2,428
Total	**250,017**	**354,000**	**100,723**	**23,428**	**45,206**	**773,374**

	Neither past due nor impaired					
2016	**High grade**	**Standard**	**Sub-standard**	**Past due but not impaired**	**Individually impaired**	**Total**
Cash and cash equivalents	54,721	-	-	-	-	54,721
Mandatory reserve deposit with the NBG	72,573	-	-	-	-	72,573
Loans to customers						
Consumer loans	2,202	82,166	49,964	12,961	417	147,710
Business loans	19,191	127,444	22,198	8,585	7,475	184,893
Mortgage loans	-	35,145	465	2,180	478	38,268
Gold pawn loans	36,570	135	22,696	356	36,199	95,956
	57,963	**244,890**	**95,323**	**24,082**	**44,569**	**466,827**
Investment securities	29,465	-	-	-	-	29,465
Other financial assets	1,232	-	-	233	-	1,465
Total	**215,954**	**244,890**	**95,323**	**24,315**	**44,569**	**625,051**

An analysis of past due loans is provided below. The majority of the past due loans are not considered to be impaired because of high quality and adequacy of collateral.

Neither past due nor impaired financial assets of the Group are classified as follows:

- High grade: A financial asset with no overdue days secured by deposit or precious metals. The Group treats the mandatory reserve deposit amount with the NBG, together with Ministry of Finance treasury bills and bonds and deposit certificates of the NBG as high grade financial assets.
- Standard grade: A financial asset with no overdue days secured by real estate.
- Substandard grade: A financial asset with no overdue days secured by other collateral or not fully collateralized.

Aging analysis of past due but not impaired loans per class of financial assets:

GEL'000 31 December 2017	**Less than 30 days**	**31 to 60 days**	**61 to 90 days**	**More than 90 days**	**Total**
Loans to customers					
Consumer loans	6,283	1,235	1,002	5,885	14,405
Business loans	3,636	1,305	641	1,493	7,075
Mortgage loans	598	119	22	946	1,685
Gold pawn loans	18	-	-	18	36
Total	**10,535**	**2,659**	**1,665**	**8,342**	**23,201**

GEL'000 31 December 2016	Less than 30 days	31 to 60 days	61 to 90 days	More than 90 days	Total
Loans to customers					
Consumer loans	6,279	1,922	604	4,156	12,961
Business loans	6,162	155	1,081	1,187	8,585
Mortgage loans	983	168	-	1,029	2,180
Gold pawn loans	356	-	-	-	356
Total	**13,780**	**2,245**	**1,685**	**6,372**	**24,082**

The Group is also exposed to credit risk arising from guarantees and letters of credit. Credit risk for off-balance sheet financial instruments is defined as the possibility of sustaining a loss as a result of another party to a financial instrument failing to perform in accordance with the terms of the contract. The Group uses the same credit policies in assuming conditional obligations as it does for on-balance sheet financial instruments, through established credit approvals, risk control limits and monitoring procedures.

Impairment assessment

The main considerations for the loan impairment assessment include whether any payments of principal or interest are overdue by more than 30 days or there are any known difficulties in the cash flows of counterparties, credit rating downgrades, or infringement of the original terms of the contract. The Group addresses impairment assessment in two areas: individually assessed allowances and collectively assessed allowances.

Individually assessed allowances

The Group determines the allowances appropriate for each individually significant loan on an individual basis. Realisable value of collateral and expected future cash flows is considered when determining allowance amounts. The impairment losses are evaluated at each reporting date, unless unforeseen circumstances require more careful attention.

Collectively assessed allowances

Allowances are assessed collectively for losses on loans to customers that are not individually significant and for individually significant loans where there is not yet objective evidence of individual impairment. Allowances are evaluated on each reporting date with each portfolio receiving a separate review.

The collective assessment takes account of impairment that is likely to be present in the portfolio even though there is no yet objective evidence of the impairment in an individual assessment. Impairment losses are estimated by taking into consideration historical losses on the portfolio.

Financial guarantees and letters of credit are assessed and provision made in a similar manner as for loans.

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

	2017				**2016**			
GEL'000	**Georgia**	**OECD**	**CIS and other foreign countries**	**Total**	**Georgia**	**OECD**	**CIS and other foreign countries**	**Total**
Assets								
Cash and cash equivalents	68,380	20,108	315	88,803	54,262	37,012	281	91,555
Mandatory reserve deposit with the NBG	76,551	-	-	76,551	72,573	-	-	72,573
Loans to customers	546,277	5,669	7,996	559,942	423,541	3,459	7,943	434,943
Investment securities	53,333	-	-	53,333	29,465	-	-	29,465
Other financial assets	2,428	-	-	2,428	1,465	-	-	1,465
	746,969	**25,777**	**8,311**	**781,057**	**581,306**	**40,471**	**8,224**	**630,001**

Liquidity risk and funding management

Liquidity risk is the risk that an entity will encounter difficulty in meeting obligations associated with financial liabilities. It refers to the availability of sufficient funds to meet deposit withdrawals and other financial commitments associated with financial instruments as they actually fall due. Liquidity risk exists when the maturities of assets and liabilities do not match. The matching and/or controlled mismatching of the maturities and interest rates of assets and liabilities is fundamental to the management of financial institutions.

In order to manage liquidity risk, the Group performs daily monitoring of future expected cash flows on clients' and banking operations, which is part of the assets/liabilities management process. The Management Board set limits on the minimum proportion of maturing funds available to meet deposit withdrawals and on the minimum level of interbank and other borrowing facilities that should be in place to cover withdrawals under both normal and stressed conditions. They also set parameters for the risk diversification of the liability base.

The Group's liquidity policy is comprised of the following:

- projecting cash flows and maintaining the level of liquid assets necessary to ensure liquidity in various time-bands;
- maintaining a funding plan commensurate with the Group's strategic goals;
- maintaining a diverse range of funding sources thereby increasing the Group's borrowing capacity, domestically as well as from foreign sources;
- maintaining highly liquid and high-quality assets;
- adjusting its product base by time bands against available funding sources;
- daily monitoring of liquidity ratios against regulatory requirements; and
- constant monitoring of asset and liability structures by time-bands.

Treasury function within the Group is charged with the following responsibilities:

- compliance with the liquidity requirements of the NBG as well as with the liquidity requirement covenants contained in the agreements with foreign lending sources;
- daily reports to management, including reporting to management on the levels of liquid assets in the main currencies (GEL, USD, EUR), cash positions;
- weekly reports to management on the forecasted levels of cash flows in the main currencies (GEL, USD, EUR);
- constantly controlling/monitoring the level of liquid assets;
- monitoring of deposit and other liability concentrations; and
- maintaining a plan for the instant increase of cash to provide liquidity under stressed conditions.

The liquidity position is assessed and managed by the Group primarily on a standalone basis, based on certain liquidity ratios established by the NBG. According to the NBG regulation monthly average liquidity ratio should not be less than 30%. ALCO is responsible for ensuring that Treasury properly manages the Group's liquidity position. The Risk Management Department is responsible for controlling these activities. Decisions on liquidity positions and management are made by ALCO.

The Group maintains an unused credit line of USD 5 million with the BSTDB (see note 10).

Analysis of financial liabilities by remaining contractual maturities

The tables below summarize the maturity profile of the Group's financial liabilities at 31 December based on contractual undiscounted repayment obligations. Repayments which are subject to notice are treated as if notice were to be given immediately. The maturity analysis does not reflect the historical stability of current accounts. Their liquidation has historically taken place over a longer period than indicated in the tables below. These balances are included in amounts due in less than three months in the tables below:

GEL'000 As at 31 December 2017	Less than 3 months	3 to 12 months	1 to 5 years	Over 5 years	Total
Financial liabilities					
Loans from financial institutions and deposits and balances from banks	43,802	7,520	37,673	6,654	95,649
Current accounts and deposits from customers	426,278	105,347	58,177	807	590,609
Other financial liabilities	11,933	-	-	-	11,933
Subordinated loans	286	2,925	11,961	26,455	41,627
Undiscounted financial liabilities	**482,299**	**115,792**	**107,811**	**33,916**	**739,818**

GEL'000 As at 31 December 2016	Less than 3 months	3 to 12 months	1 to 5 years	Over 5 years	Total
Financial liabilities					
Loans from financial institutions and deposits and balances from banks	3,325	2,874	5,534	-	11,733
Current accounts and deposits from customers	377,068	126,189	29,801	564	533,622
Other financial liabilities	11,389	-	-	-	11,389
Subordinated loans	733	3,284	14,290	28,949	47,256
Undiscounted financial liabilities	**392,515**	**132,347**	**49,625**	**29,513**	**604,000**

The Group considers the maximum liquidity risk of all its financial guarantees and undrawn loan commitments as less than 3 months, as this is the earliest period when the guarantees can be called or the loan commitments can be drawn. However, based on the past experience, the management believes, that the Group is exposed to liquidity risk from its financial commitments and contingencies according to their contractual expiry dates:

GEL'000	Less than 3 months	3 to12 months	1 to 5 years	Over 5 years	Total
31 December 2017	11,788	12,122	36,407	2,087	**62,404**
31 December 2016	10,625	10,823	17,343	49	**38,840**

The Group expects that not all of the contingent liabilities or commitments will be drawn before expiry of the commitments.

Market risk

Market risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in market prices. Market risk comprises currency risk, interest rate risk and other price risks. Market risk mainly arises from open positions in interest rate financial instruments, which are exposed to general and specific market movements and changes in the level of volatility of market prices and foreign currency rates. The objective of market risk management is to manage and control market risk exposures within acceptable parameters, while optimising the return on risk.

The Group manages its market risk by following NBG's prudential ratio requirements on open currency position limits. These limits are monitored on a daily basis and the monitoring process is supervised by the Management Board.

Interest rate risk

Interest rate risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in market interest rates. The portion of the Group's borrowings is at floating interest rate, while the Group's deposits and majority of loan portfolios are at fixed interest rate. NBG pays floating interest rate on minimum reserves that the Group holds with the NBG. The Group also holds floating interest rate earning loans, these financial assets have counter effect to offset the interest rate change impact on borrowings.

The table below summarizes impact of the 100 basis points interest rate change on the market to the Groups equity:

GEL'000	2017	2016
Financial assets	135,185	84,872
Financial liabilities	(40,763)	(10,587)
Net interest sensitivity position	**94,422**	**74,285**
100 Basis points increase of Market interest rates	**802**	**631**
100 Basis points decrease of Market interest rates	**(802)**	**(631)**

Average effective interest rates

The table below displays average effective interest rates for interest-bearing assets and liabilities as at 31 December 2017 and 2016. These interest rates are an approximation of the yields to maturity of these assets and liabilities.

	2017 Average effective interest rate, %			**2016 Average effective interest rate, %**		
	GEL	**USD**	**Other currencies**	**GEL**	**USD**	**Other currencies**
Interest bearing assets						
Cash and cash equivalents	7	-	-	6	-	-
Loans to customers	14	10	8	14	11	9
Investment securities	9	-	-	10	-	-
Interest bearing liabilities						
Deposits from banks	7	4	-	-	-	-
Loans from financial institutions	10	7	-	-	6	-
Current accounts and deposits from customers	7	3	2	7	4	1
Subordinated loans	-	6	-	-	8	-

Currency risk

The Group has assets and liabilities denominated in several foreign currencies. Currency risk is the risk that the fair value or the future cash flows of a financial instrument will fluctuate because of changes in foreign currency exchange rates.

The following tables show the foreign currency exposure structure of financial assets and liabilities as at 31 December 2017 and 2016:

GEL'000 31 December 2017	**GEL**	**USD**	**EUR**	**Other currencies**	**Total**
ASSETS					
Cash and cash equivalents	30,650	23,891	32,956	1,306	88,803
Mandatory reserve deposit with the NBG	-	63,333	13,218	-	76,551
Loans to customers	221,499	313,109	25,334	-	559,942
Investment securities	53,333	-	-	-	53,333
Other financial assets	578	437	1,413	-	2,428
Total assets	**306,060**	**400,770**	**72,921**	**1,306**	**781,057**
LIABILITIES					
Loans from financial institutions and deposits and balances from banks	64,292	17,844	30	-	82,166
Current accounts and deposits from customers	196,644	308,871	72,983	1,128	579,626
Subordinated loans	-	31,706	-	-	31,706
Other financial liabilities	6,083	5,647	195	8	11,933
Total liabilities	**267,019**	**364,068**	**73,208**	**1,136**	**705,431**
Net balance sheet position	**39,041**	**36,702**	**(287)**	**170**	**75,626**
Effect of Derivatives	**32,878**	**(32,878)**	**-**	**-**	**-**
Net Position	**71,919**	**3,824**	**(287)**	**170**	**75,626**

GEL'000 31 December 2016	GEL	USD	EUR	Other currencies	Total
ASSETS					
Cash and cash equivalents	26,040	39,462	23,472	2,581	91,555
Mandatory reserve deposit with the NBG	-	62,422	10,151	-	72,573
Loans to customers	147,012	272,487	15,444	-	434,943
Investment securities	29,465	-	-	-	29,465
Other financial assets	247	670	546	2	1,465
Total assets	**202,764**	**375,041**	**49,613**	**2,583**	**630,001**
LIABILITIES					
Loans from financial institutions and deposits and balances from banks	416	10,696	-	-	11,112
Current accounts and deposits from customers	180,623	288,273	49,250	2,456	520,602
Subordinated loans	-	33,705	-	-	33,705
Other financial liabilities	2,967	8,302	120	-	11,389
Total liabilities	**184,006**	**340,976**	**49,370**	**2,456**	**576,808**
Net balance sheet position	**18,758**	**34,065**	**243**	**127**	**53,193**
Effect of Derivatives	**34,439**	**(34,439)**	**-**	**-**	**-**
Net Position	**53,197**	**(374)**	**243**	**127**	**53,193**

A (weakening)/ strengthening of the GEL, as indicated below, against USD at 31 December 2017 and 2016, would have affected equity and profit or loss by the amounts shown below. This analysis is on a net-of-tax basis, and is based on foreign currency exchange rate variances that the Group considered to be reasonably possible at the end of the reporting period. The analysis assumes that all other variables, in particular interest rates, remain constant.

GEL'000	2017	2016
10% weakening of USD against GEL	(325)	32
10% strengthening of USD against GEL	325	(32)

The following significant exchange rates applied during the year:

in GEL	Average rate 2017	Average rate 2016	Reporting date spot rate 31 December 2017	Reporting date spot rate 31 December 2016
USD 1	2.5086	2.3667	2.5922	2.6468
EUR 1	2.8322	2.6172	3.1044	2.7940

Other price risk

Other price risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in market prices (other than those arising from interest rate risk or currency risk), whether those changes are caused by factors specific to the individual financial instrument or its issuer, or factors affecting all similar financial instruments traded in the market. As at 31 December 2017 and 2016, the Group is not significantly exposed to other price risk.

Operational risk

Operational risk is the risk of loss arising from systems failure, human error, fraud or external events. When controls fail to perform, operational risks can cause damage to reputation, have legal or regulatory implications, or lead to financial loss. The Group cannot expect to eliminate all operational risks, but a control framework and monitoring and responding to potential risks could be effective tools to manage the risks. Controls should include effective segregation of duties, access, authorisation and reconciliation procedures, staff education and assessment processes, including the use of internal audit.

22. Fair value measurements

Fair values are categorised into different levels in a fair value hierarchy based on the inputs used in the valuation techniques as follows:

- *Level 1*: quoted prices (unadjusted) in active markets for identical assets or liabilities.

- *Level 2*: inputs other than quoted prices included in Level 1 that are observable for the asset or liability, either directly (i.e. as prices) or indirectly (i.e. derived from prices).
- *Level 3*: inputs for the asset or liability that are not based on observable market data (unobservable inputs).

If the inputs used to measure the fair value of an asset or a liability might be categorised in different levels of the fair value hierarchy, then the fair value measurement is categorised in its entirety in the same level of the fair value hierarchy as the lowest level input that is significant to the entire measurement.

The Group estimates the fair value of financial assets (Ministry of Finance Treasury Bills and Bonds, Loans to Customers and Other financial assets) and financial liabilities (Loans from financial institutions, Deposits and balances from Banks, Other financial liabilities, Subordinated loans) to be not materially different from their carrying values. The fair value estimate for financial assets and liabilities at fair value through profit or loss are categorized into Level 2 of the fair value hierarchy, because of the use of valuation models where all significant inputs are observable.

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.

23. Maturity analysis of financial assets and liabilities

The table below shows an analysis of financial assets and liabilities according to when they are contractually due to be recovered or settled.

	2017			2016		
GEL'000	**Within one year**	**More than one year**	**Total**	**Within one year**	**More than one year**	**Total**
Cash and cash equivalents	88,803	-	88,803	91,555	-	91,555
Mandatory reserve deposit with the NBG	76,551	-	76,551	72,573	-	72,573
Loans to customers	241,945	317,997	559,942	207,980	226,963	434,943
Investment securities	6,864	46,469	53,333	3,486	25,979	29,465
Other financial assets	2,221	207	2,428	1,253	212	1,465
Total	**416,384**	**364,673**	**781,057**	**376,847**	**253,154**	**630,001**
Loans from financial institutions and deposits and balances from banks	50,905	31,261	82,166	5,815	5,297	11,112
Current accounts and deposits from customers	522,889	56,737	579,626	495,714	24,888	520,602
Subordinated loans	1,375	30,331	31,706	1,407	32,298	33,705
Other financial liabilities	11,933	-	11,933	11,389	-	11,389
Total	**587,102**	**118,329**	**705,431**	**514,325**	**62,484**	**576,808**
Net exposure	**(170,718)**	**246,344**	**75,626**	**(137,478)**	**190,671**	**53,193**

The Group'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 2017, total current accounts within amounts due to customers amounted to GEL 139,371 thousand (2016: GEL 241,063 thousand). The Group conducts an analysis of the stability of the current accounts within amounts due to customers for the period of the preceding two years on a monthly basis. Current accounts end-of-month balances have not fallen below GEL 119,074 thousand (2016: GEL 150,639 thousand)* for the preceding 24 months. A significant part of total current accounts represent current accounts from legal entities which historically are of long-term nature. As such, it is reasonable to treat these funds for estimation of liquidity position of the Group as with maturity of more than one year.

* These amounts are unaudited

24. Related party disclosures

(a) Control relationships

The Group does not have an ultimate controlling party or ultimate or immediate parent company. The shareholding structure of the Group is disclosed in note 1 of these consolidated financial statements.

(b) Transactions with key management

Total remuneration included in personnel expenses for the years ended 31 December 2017 and 2016 is as follows:

GEL'000	2017	2016
Salaries and other benefits	**1,293**	**1,253**

As at 31 December 2017 the Group has issued loans of GEL 75 thousand (2016: GEL 98 thousand) to its key management. The loans are mainly long-term and bear average interest rate of 13%. In 2017 interest income accrued on the loans to the key management is GEL 10 thousand (2016: GEL 26 thousand).

As at 31 December 2017 the key management placed deposits of GEL 301 thousand with the Group (2016: GEL 579 thousand). The deposits bear average interest rate of 3.8% and mature within 1 year from the reporting date. In 2017 interest expense accrued on the term deposits from the key management is GEL 21 thousand (2016: GEL 16 thousand).

(c) Transactions with other related parties

000 GEL	Transaction value 2017	Outstanding balance 2017	Transaction value 2016	Outstanding balance 2016
Other related parties (Entities under common control)				
Subordinated loan	-	20,742	-	21,181
Current accounts and term deposits	-	12,601	-	2,632

Terms and conditions of the subordinated loan is disclosed in note 11. In 2017 interest of GEL 905 thousand was accrued on subordinated loans from the related parties (2016: GEL 1,389 thousand). The current accounts and term deposits mainly do not bear interest rate and are on demand. Interest expense of GEL 50 thousand was accrued on terms deposits from related parties (2016: GEL 149 thousand).

25. Capital adequacy

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

The primary objectives of the Bank's capital management are (i) to ensure that the Bank complies with externally imposed capital requirements set by the NBG, (ii) to safeguard the Bank's ability to continue as a going concern and is monitored monthly with reports outlining their calculation reviewed and subsequently submitted to the NBG.

The Bank manages its capital structure and makes adjustments to it in the light of changes in economic conditions and the risk characteristics of its activities. In order to maintain or adjust the capital structure, the

Bank may adjust the amount of dividend payment to shareholders, return capital to shareholders or issue capital securities. No changes were made in the objectives, policies and processes from the previous years.

The Bank complied with all externally imposed capital requirement as at 31 December 2016 and 31 December 2017 reporting periods.

The NBG capital adequacy ratio

The NBG requires under Basel I guidelines banks to maintain a minimum total capital adequacy ratio of 9.6% (2016:10.8%) of risk-weighted assets and Tier 1 capital adequacy ratio of 6.4% (2016:7.2%), computed based on the Bank's standalone special purpose financial statements prepared in accordance with the NBG regulations and pronouncements. As at 31 December, the Bank's capital adequacy ratio on this basis was as follows:

GEL'000	2017	2016
Core capital*	70,157	82,902
Supplementary capital*	55,067	23,933
Total regulatory capital*	**125,224**	**106,835**
Risk weighted assets*	**871,933**	**711,096**
Total capital adequacy ratio*	14.36%	15.02%
Tier 1 capital adequacy ratio*	8.05%	11.66%

The NBG also requires all banks to comply with Basel II/III regulations in their capital adequacy assessment. In December 2017, the NBG has introduced an updated capital framework that is more compliant with Basel III guidelines. Under the updated capital framework capital requirements are divided into Pillar 1 and Pillar 2 buffers. The Bank's capital adequacy ratios on the current Basel II/III basis were as follows:

GEL'000	2017	2016
Core capital*	86,419	68,835
Supplementary capital*	35,691	36,117
Total regulatory capital*	**122,110**	**104,952**
Risk weighted assets*	**727,269**	**597,820**
Minimum total capital adequacy requirements	13.14%	13.36%
Total capital adequacy ratio*	16.79%	17.56%
Minimum Tier 1 capital adequacy requirements	10.48%	10.65%
Tier 1 capital adequacy ratio*	11.88%	11.51%

Under the previous NBG Basel II/III regulations effective in 2016 until December 2017 Capital ratios were as follows:

	2017	2016
Minimum total capital adequacy requirements	10.50%	10.50%
Total capital adequacy ratio*	13.17%	13.40%
Minimum Tier 1 capital adequacy requirements	8.5%	8.5%
Tier 1 capital adequacy ratio*	9.10%	8.63%

*These amounts are unaudited.

26. Contingencies

Litigation

In the ordinary course of business, the Group 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.

Taxation contingencies

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 consolidated financial statements, if the authorities were successful in enforcing their interpretations, could be significant.

27. Events after the reporting date

In March 2018, the bank received USD 2,500 thousand subordinated loan from Dhabi Contracting, with contractual maturity of six years.