Pillar 3 Annual Report 2019

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TBC BANK

Contents

Introduction

The main purpose of this report is to detail the requirements of TBC Bank's Pillar 3 about capital adequacy and remuneration as defined by the National Bank of Georgia in line with the Basel III framework.

Management Statement

The Bank's Supervisory Board confirms the accuracy and the authenticity of all the data and information outlined in the Pillar 3's present statement. The document is prepared in full compliance with the internal processes agreed with the Supervisory Board. It is in line with all the requirements of "Rule for disclosure of information by commercial banks within the framework of Pillar 3" approved by the Order #92/04 of the President of the National Bank of Georgia, on 22 June, 2017 and other rules and norms established by the National Bank of Georgia.

Location of Pillar 3 Disclosures

This report provides the Basel 3 Pillar 3 disclosures to the extent that these required pillar 3 disclosures are not included in the TBC Bank Group PLC Annual Report 2019.

The Following table provides the location of the required Pillar 3 disclosures in the TBC Bank Group PLC Annual Report 2019:

Pillar 3 disclosure topic	Primary location in Annual Report 2019
Shareholder rights	Director's Governance Statement – Special rights and transfer restrictions and Major Shareholders (page 132-133)
Governance – committee membership and responsibilities	Director's Governance Statement – Board's committees (page 126); Corporate Governance Structure (page 127)
Governance – Independence of the Board	Director's Governance Statement – Division of Responsibilities and Board Composition (page 127)
Governance – Board members' biographies	Governance – Board's biographies (page 136-139)
Governance – Viability	Governance – Viability statement (page 134-135)
Governance – Committee meetings	Director's Governance Statement – Board and Committee Meeting attendance (page 128-129)
Governance – Board's effectiveness	Governance – Annual Board effectiveness evaluation (page 129-130)

Governance – Delegation of authorities	Governance – The Board and Board's Committees (page 125-126)
Bank's Management Board – Biographies	The Bank's Management Board Biographies (page 123-142)
Bank's strategy	Business Model and Strategy – Strategy (page 12-17)

Pillar 3 disclosure topic	Primary location in other report 2019
Shareholders' income	http://www.tbcbank.ge/web/en/financial-reporting-to-nbg Transfer to shareholder

Key Indicators of Bank

Capital Ratios as a Percentage of Risk Weighted Assets ("RWA"):

	31 December 2019	31 December 2018	31 December 2017
Common equity Tier 1 ratio	12.01%	12.39%	12.90%
Tier 1 ratio	14.63%	12.76%	13.37%
Total regulatory capital ratio	19.08%	17.87%	17.53%

Profit Indicators:

	31 December 2019	31 December 2018	31 December 2017
Total Interest Income / Average Annual Assets	7.93%	8.62%	8.50%
Total Interest Expense / Average Annual Assets	3.99%	3.75%	4.05%
Earnings from Operations / Average Annual Assets	3.63%	4.47%	3.97%
Net Interest Margin	3.94%	4.87%	4.45%
Return on Average Assets (ROA)	2.40%	2.72%	2.77%
Return on Average Equity (ROE)	19.93%	21.30%	20.10%

Asset Quality:

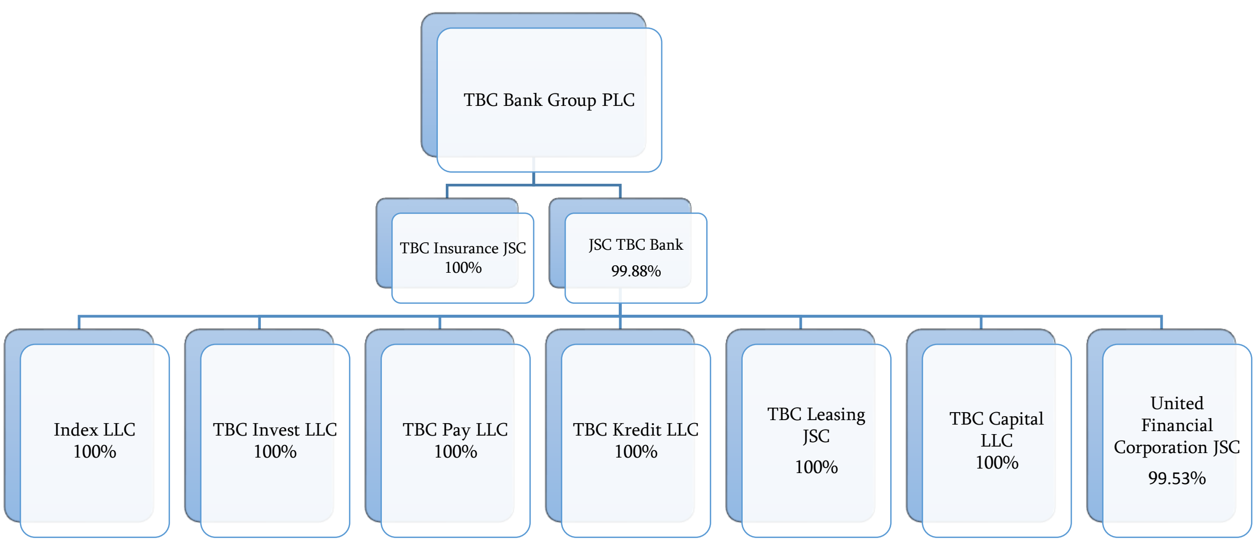
	31 December 2019	31 December 2018	31 December 2017
Non-Performing Loans / Total Loans	3.09%	3.59%	3.22%
LLR / Total Loans	3.90%	4.15%	4.31%
FX Loans / Total Loans	58.76%	59.84%	59.37%
FX Assets / Total Assets	53.23%	55.45%	55.86%
Loan Growth – YTD	22.28%	20.98%	44.63%

Liquidity:

	31 December 2019	31 December 2018	31 December 2017
Liquid Assets/Total Assets	17.18%	21.27%	20.87%
FX Liabilities/Total Liabilities	63.40%	63.32%	64.60%
Current & Demand Deposits/Total Assets	36.79%	39.28%	40.03%

Group Structure

The chart below illustrates the structure of the TBC Group:



For additional information about the consolidation of enterprises, please see the Annex.

As of 31 December 2019, the shareholders directly owning more than 5% of the Bank's total outstanding shares were as follows:

Beneficiary Owner	Share
Mamuka Khazaradze	10.25%
Badri Japaridze	5.99%
European Bank for Reconstruction and Development	8.03%
JPMorgan Asset Management	6.21%
Schroder Investment Management	6.47%
Dunross & Co.	6.61%

The Bank's Management Board and Committees

The Bank's Board of Directors consisted of eight members:

Vakhtang Butskhrikidze
David Chkonia [1]
Tornike Gogichaishvili
Nino Masurashvili
Giorgi Shagidze
Nikoloz Kurdiani
George Tkhelidze

The following committees are at the Directors' level:

Committee Member	Managing of Conflict of Interests Committee	Information Security Steering Committee	Assets and Liabilities Management Committee (ALCO)	Management Board Risk Committee	Operational Risks Committee	Business segment Credit Committee
CEO	X	X	X	X	X	X
CFO			X	X		
CIO		X				
CRO	X	X	X	X	X	X
COO		X			X	
Head of Retail Banking			X	X	X	
Head of Marketing and MSME			X	X	X	

[1]David Chkonia stepped down from the Management Board of TBC Bank on January 24, 2020.

Head of Corporate and Investment Banking			X	X	X	
Head of Operational Risks		X			X	
Head of Compliance Risk Department	X	X			X	
Head of Compliance Risk and Control Unit	X					
Head of Analytic Department of Security Service		X				
Head of Information Security		X				
Deputy CFO[2]			X			
Head of Debt Capital Markets			X			
Head of ERM			X			
Head of FRMD			X			
Head of Treasury			X			
Head of Customer Experience Department						
Heads of Underwriting						X
Head of Problem						X

[2] Member since January, 2020

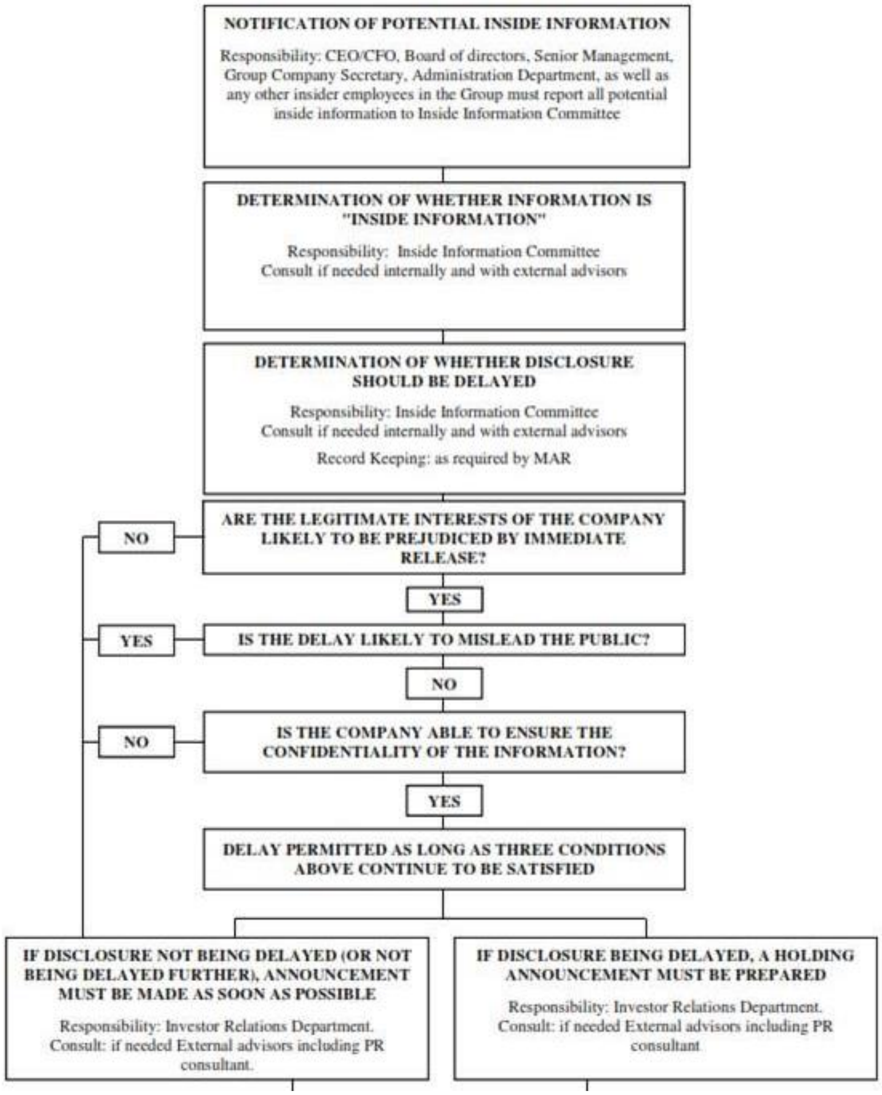
Assets Management						
Head of Corporate Rehabilitation						X
Head of IT Operations		X				

The Bank has adopted Inside Information Disclosure Policy, which is designed to ensure that the Company's regulatory public announcements in relation to inside information are made in a timely manner, are factually correct, do not omit any material information and are expressed in a clear and objective manner that allows investors to assess the impact of the information when making investment decisions.

For this purpose, the Bank has established the Inside Information Committee, which is chaired by the CEO and consist of the following members: the CEO, CFO, and Head of IR, General Counsel and Head of Compliance Department.

The Inside Information Committee will decide whether the information provided is inside information and requires disclosure. If deemed necessary, the Inside Information Committee will consult internally and with external advisors on a timely basis and as appropriate in making this decision. If disclosure is required, the Investor Relations Department will make the necessary arrangements for the disclosure of the relevant information via a RIS unless a delay in making an announcement is permitted.

The chart below summarizes the disclosure process of inside information within TBC Bank:


NOTIFICATION OF POTENTIAL INSIDE INFORMATION
Responsibility: CEO/CFO, Board of directors, Senior Management, Group Company Secretary, Administration Department, as well as any other insider employees in the Group must report all potential inside information to Inside Information Committee
DETERMINATION OF WHETHER INFORMATION IS "INSIDE INFORMATION"
Responsibility: Inside Information Committee
Consult if needed internally and with external advisors
DETERMINATION OF WHETHER DISCLOSURE SHOULD BE DELAYED
Responsibility: Inside Information Committee
Consult if needed internally and with external advisors
Record Keeping: as required by MAR
ARE THE LEGITIMATE INTERESTS OF THE COMPANY LIKELY TO BE PREJUDICED BY IMMEDIATE RELEASE?
NO
YES
IS THE DELAY LIKELY TO MISLEAD THE PUBLIC?
YES
NO
IS THE COMPANY ABLE TO ENSURE THE CONFIDENTIALITY OF THE INFORMATION?
NO
YES
DELAY PERMITTED AS LONG AS THREE CONDITIONS ABOVE CONTINUE TO BE SATISFIED
IF DISCLOSURE NOT BEING DELAYED (OR NOT BEING DELAYED FURTHER), ANNOUNCEMENT MUST BE MADE AS SOON AS POSSIBLE
Responsibility: Investor Relations Department.
Consult: if needed External advisors including PR consultant.
IF DISCLOSURE BEING DELAYED, A HOLDING ANNOUNCEMENT MUST BE PREPARED
Responsibility: Investor Relations Department.
Consult: if needed External advisors including PR consultant

The Banks Management Board Responsibilities

Deputy CEO, Chief Financial Officer

The Chief Financial Officer (CFO) reports to the Chief Executive Officer and to the Supervisory Board and has a strategic role in the overall management of the Bank. The CFO has the primary responsibility for planning, implementing, managing and controlling all finance-related activities. These include investor relations and fund raising, treasury activities, financial analysis, strategic planning and budgeting, financial accounting, regulatory reporting, taxation and all other relevant matters.

Deputy CEO, Corporate and Investment Banking

The Director of Corporate and Investment Banking reports to the Chief Executive Officer and to the Supervisory Board and assumes an important role in the overall management of the Bank. He has primary responsibility for planning, implementing, managing and controlling of the Bank's corporate and investment business. The Director of Corporate and Investment Banking manages the division to the end of provision of the wide range of financial services to its clients. Activities include lending, clearing, investing deposits as well as organizing specialized products for clients with high turnovers, such as financial institutions, major companies and commercial state companies.

Deputy CEO, Chief Risk Officer

The Chief Risk Officer (CRO) reports to the Chief Executive Officer and to the Supervisory Board. The CRO holds the primary responsibility for managing the Bank's risk management-related activities, including risk identification, measurement, mitigation, monitoring and reporting.

Deputy CEO, Chief Operating Officer

The Chief Operating Officer (COO) reports to the Chief Executive Officer. The COO's responsibilities include the management of the centralized back office, card processing, cash management, loan administration, customer experience and support, correspondent banking, procurement, logistics, collateral management and appraisal and cash center.

Deputy CEO, Retail Banking

The Director of Retail Banking reports to the Chief Executive Officer and holds the primary responsibility for designing and delivering the strategy for the Bank's retail business, its product range and designated market. The Retail Director is hence responsible of developing new product and service delivery channels as well as planning and managing business activities for the retail segment, such as sales, service quality, profitability, risk, branch operations, digital and other channels and retail reporting, budgeting and analysis.

Deputy CEO, Marketing Communications and MSME Banking

The Director of Marketing Communications and MSME Banking reports to the Chief Executive Officer. The role entails planning, implementing, managing, and controlling all the Bank's activities related to the micro and SME segments as well as to marketing.

Risk Management

Risk Management Strategy

One of TBC Bank's main priorities is to establish and maintain a functioning strong and sustainable risk management, adaptable to on-going business developments and able to respond promptly to emerging risks.

The key objective of the risk strategy is to promote a solid and independent, business minded risk management system. The risk management aims primarily to contribute to the development of TBC's business strategy by supporting risk-adjusted profitability maximisation and guaranteeing TBC's sustainable development through the implementation of an efficient risk management system.

Four major principles are adopted to enable the accomplishment of the risk management's major objectives:

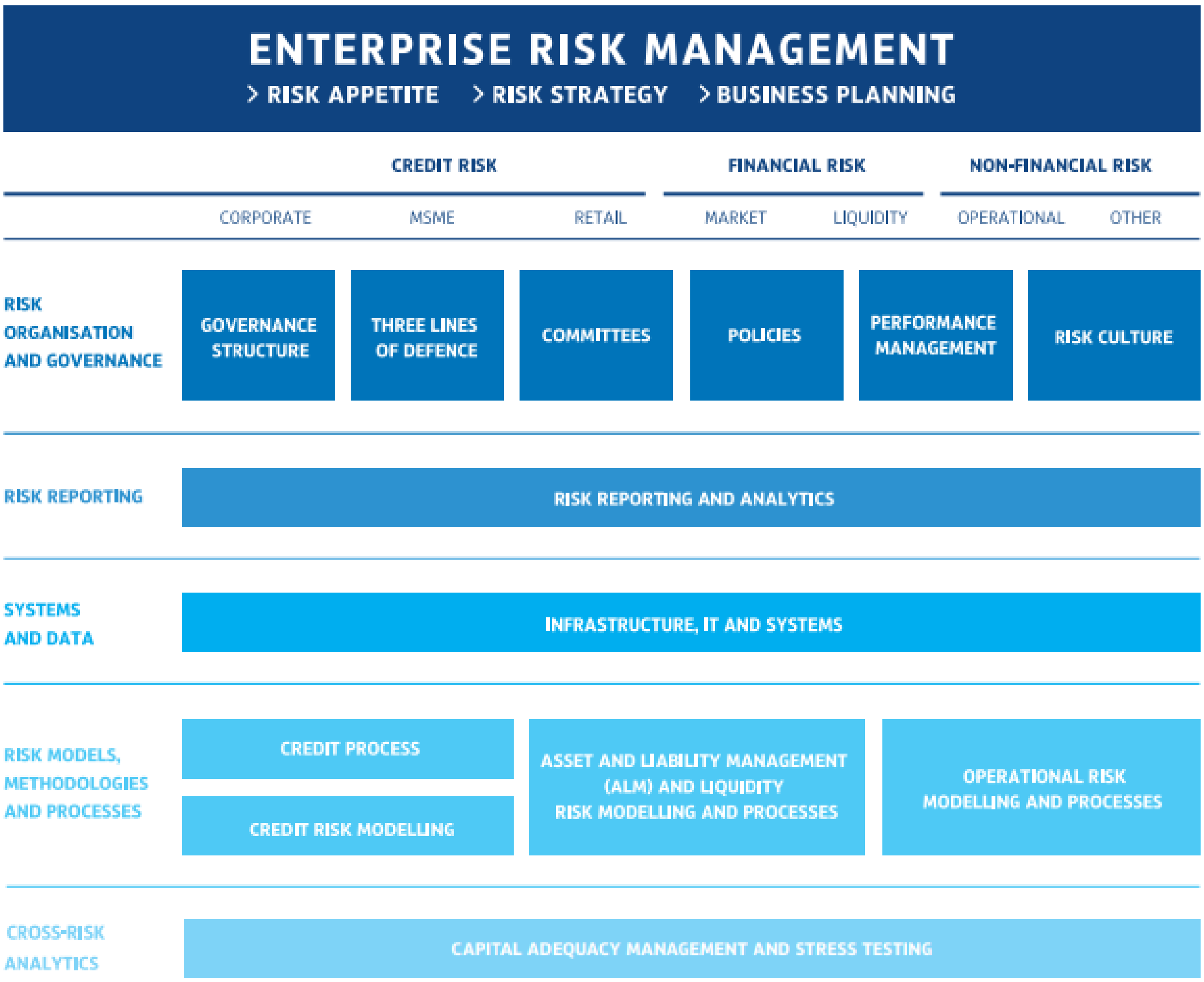
- **Governing risks transparently in order to earn understanding and trust.** Consistency and transparency in risk-related processes and policies are preconditions for gaining the trust of the various stakeholders. Communicating risk goals and strategic priorities to governing bodies and business departments and providing a comprehensive follow-up in an accountable manner are key priorities for the risk management staff;
- **Managing risks prudently to promote sustainable growth and resiliency.** Risk management acts as a backstop against excessive risk-taking. The capital adequacy management and strong forward-looking tools and decision-making processes ensure the Bank's sustainability and resiliency;
- **Ensuring that risk management underpins the strategy implementation.** The staff responsible for the risk management provide assurance on the objectives' feasibility through the risk identification and management. Identifying and adequately pricing risks, as well as taking risk mitigation actions, support the achievement of the desired returns and planned targets;
- **Using risk management to gain a competitive advantage.** Comprehensive, transparent, and prudent risk governance facilitates understanding and trust from multiple stakeholders, ensuring the sustainability and resilience of the business model and the positioning of risk management as the Bank's competitive advantage and strategic enabler.

The abovementioned principles must be embedded into the overall risk governance structure as well as individual risk management tools and techniques.

Risk Management Framework

The risk management framework incorporates all necessary components for a comprehensive risk governance. It is comprised of the enterprise risk management, credit, financial and non-financial risk management, risk reporting and supporting IT infrastructure, cross-risk analytical tools and techniques such as capital adequacy management and stress-testing.

The diagram below illustrates the risk management framework:

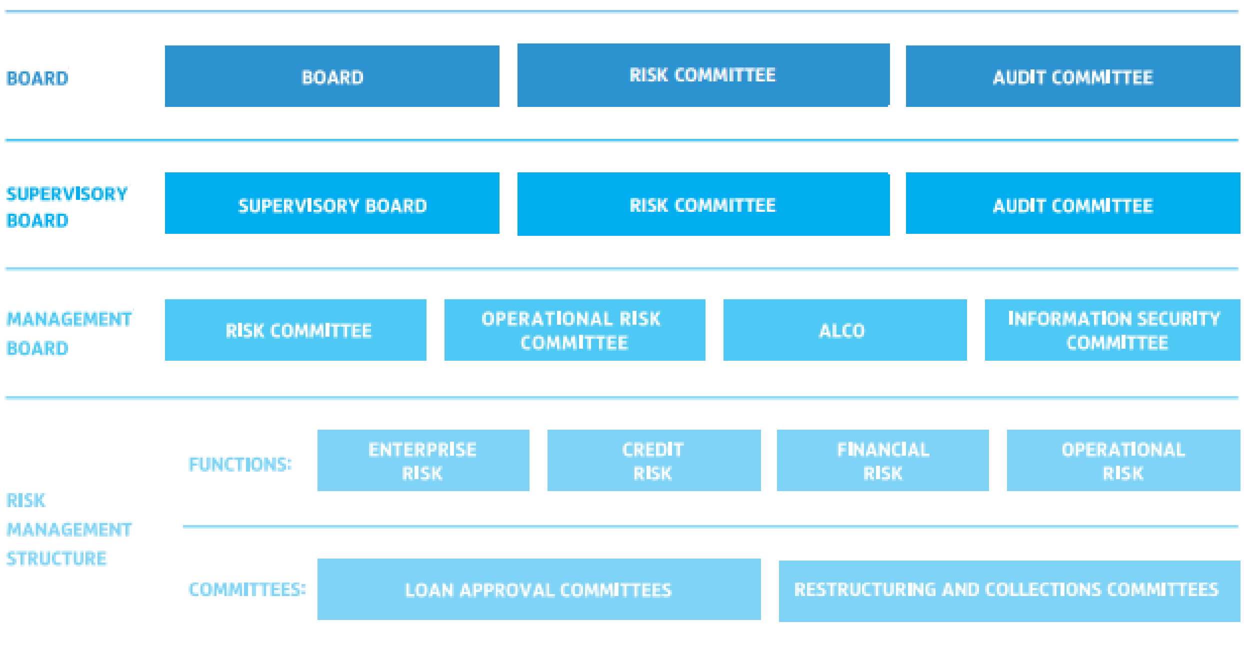


Risk Governance

The Bank conducts its risk management activities within the framework of its unified risk management system. The involvement of all levels of governance, the clear division of authority, and the effective communication between the different entities facilitates the accuracy of the Bank's strategic and risk objectives, the adherence to the established risk appetite, and the sound risk management.

The Bank's governance structure ensures an adequate oversight and accountability, as well as a clear separation of duties. The Supervisory Board hold the joint overall responsibility to set the tone at the Bank's top and monitor the compliance with the established objectives, while the Management Board governs and directs the Bank's daily activities.

The Supervisory Board's oversight is coupled with the permanent involvement of the senior management in the Bank's risk management and the exercise of top-down risk allocation by the enterprise risk management function. This ensures a clarity of the risk objectives, a constant monitoring of the risk profile against the risk appetite, and a rapid response and actions to address a prompt escalation of risk-related concerns.



The risk governance structure consists of two board levels: the Supervisory Board and the Management Board, each with their dedicated risk committees. The Supervisory Board and the Bank's senior management govern the risk objectives through the Risk Appetite Statement (details about Risk Appetite Framework are on page 31).

The Supervisory Board features two committees:

- **The Risk Committee** supervises the risk profile and risk governance practice within the Bank;
- **The Audit Committee** is responsible for implementing key accounting policies and facilitating both internal and external auditor activities.

The Management Board comprises four committees:

- **The Risk Committee** was established to guide the Bank-wide risk management activities and monitor major risk trends in order to ensure that the risk profile complies with the established risk appetite;
- **The Operational Risk Committee** takes decisions related to the operational risk governance;

- **The Assets and Liabilities Management Committee (ALCO)** is responsible for the implementation of asset-liability management policies;
- **Information security committee** is responsible for managing the security of the Bank's IT systems.

The individual risks' daily management is based on the "three lines of defence" principle. Business lines are the primary risks' holders. Risk teams act as the second line of defence by sanctioning transactions and developing tools and techniques for risk identification as well as the required analysis, measurement, monitoring and reporting.

The committees established at the operational levels are charged with making transaction-level decisions as part of a framework comprised of clear and sophisticated delegations of authority based on the "four-eye" principle. All new products and projects pass through risk teams to ensure risks are comprehensively analysed. These control arrangements guarantee that the Bank makes informed decisions that are adequately priced and that no risks exceeding the Bank's established targets are taken. Dedicated teams manage credit, liquidity, market, operational and other non-financial risks.

Apart from these risk teams, the Risk governance includes the centralized enterprise risk management (ERM). The ERM Department is tasked to ensure the effective development, communication, and implementation of the risk strategy and risk appetite across the Bank. Its function facilitates cross-risk activities such as aggregation, analytics and reporting and also addresses issues that are not specific to a single type of risk. Accordingly, the ERM complements the role of other risk actions to ensure the coverage of key risk activities and responsibilities and builds capabilities in a centralised team.

The Bank's strong and independent risk-management structure enables to fulfil all required risk management functions within the second line of defence by highly skilled professionals.

In addition to the risk teams subordinated to the Chief Risk Officer, the Compliance Department reports directly to the CEO and is specifically in charge of anti-money laundering and compliance risk management.

As the third line of defence, the internal audit department is responsible for providing an independent and objective assurance, as well as recommendations, to the Bank about how further improve operations and risk management.

Key Risks

The Risk of Macroeconomic Environment Deterioration of the Country

The slowdown of economic growth in Georgia will have an adverse impact on borrowers' repayment capacity and restrain their future investment and expansion plans. These occurrences will be reflected in the Bank's portfolio quality and profitability, and also slow down the portfolio growth rates. Negative macroeconomic developments can compromise the Bank's performance through different parameters such as increasing unemployment slowing down of economic growth, exchange rate and inflation volatility, investment environment deterioration, worsening of consumer and business confidence etc.

Given that Georgia is a small open economy, the political and economic instability in the neighbouring and main trading partner countries negatively affects the country's economic outlook through a worsening current account (e.g. decreasing exports and inflows from tourism as well as lower remittances and foreign direct investments).

According to the Geostat, real GDP increased by 5.1% in 2019. A slightly more than 5.0% economic growth for the full year 2019 once more underlines the resilience and high growth potential of the Georgian economy. This growth is particularly encouraging on the backdrop of the challenges that the economy faced in 2019, the most important being flight ban imposed by the Russian Federation. The GEL exchange rate depreciation and above target inflation remained additional challenges in 2019, however, the response of the macro policymakers have been appropriate. The NBG tightened the monetary policy rate from 6.5% at the beginning of September to 9.0% as of the end of December 2019. Fiscal spending significantly supported the growth in 2019, with the budget deficit coming in at estimated 2.4% of GDP in 2019. The actual impact of the fiscal sector on growth was even higher, taking into consideration the advance payments made by the end of 2018. As for the system – wide credit growth, while the penetration has increased, the credit to GDP ratio was still close to its long-term trend, especially when measured at a constant exchange rate. Despite some acceleration in FX lending, the de-dollarization of the financial sector remains a top priority for the central bank, however, going forward, it is expected that relatively more attention will be devoted to the liabilities' side. Overall, from a macro perspective there were no signs of a build-up of system- wide risks in 2019. At the same time, Georgia remains vulnerable to external and to some extent internal shocks, which could have an adverse impact on the Georgian economy, resulting in lower growth or, in some severe circumstances, a contraction of the economy. These negative developments could also have a negative impact on the GEL exchange rate. To decrease its vulnerability to economic cycles, the Bank identifies cyclical industries and proactively manages its underwriting approach and clients within its risk appetite framework. The Bank has in place a macroeconomic monitoring process that relies on close, recurrent observation of the economic developments in Georgia, as well as in neighbouring countries, to identify early warning signals indicating imminent economic risks. This system allows the Bank to promptly assess significant economic and political occurrences and analyse their implications for the Bank's performance. The identified implications are duly translated into specific action plans with regards to reviewing the underwriting standards, risk appetite metrics or limits, including the limits for each of the most vulnerable industries. Additionally, the stress-testing and scenario analysis applied during the credit review and portfolio monitoring processes enable the Bank to have an advance evaluation of the impact of macroeconomic shocks on its business. The resilience towards a changing macroeconomic environment is incorporated into the Bank's credit underwriting standards. As such, borrowers are expected to withstand certain adverse economic developments through prudent financials, debt-servicing capabilities and conservative collateral coverage.

Credit risk

Credit risk is the greatest material risk faced by the Bank, given the Bank is engaged principally in traditional lending activities. The Bank'scustomers include legal entities as well as individual borrowers. Thus, the Bank allocates significant resources to its management.

Due to the Georgian economy's significant reliance on foreign currencies, the currency-induced credit risk is significant and it relates to risks arising from foreign currency-denominated loans to unhedged borrowers in the portfolio. Credit risk also includes concentration risk, which is associated to the quality deterioration of the credit portfolio, due to large exposures provided to single borrowers or groups of connected borrowers, or loan concentration in specific economic industries.

The credit risk management's major objectives are to develop a sound credit approval process for informed risk-taking and procedures for effective risk identification, monitoring and measurement.

The Bank's credit portfolio is highly diversified structurally across customer types, product types and industry segments, which minimizes credit risk at Bank level. As of 31 December 2019, the retail segment represented 40% of the total portfolio, which was split between mortgage and non-mortgage exposures 63% and 37%, respectively. No single business sector represented more than 8.6% of the total portfolio at the end of 2019.

Currency-induced credit risk

Currency induced credit risk is one of the most significant risks that could negatively impact the Bank's portfolio quality given that a large part of its exposure is denominated in foreign currency. As of 31 December 2019, 58.8% of total gross loans and advances to customers (before provision for loan impairment) were denominated in foreign currencies. In January 2019, government authorities continued their efforts to reduce the economy's dependence on foreign currency financing by increasing the cap to GEL 200,000, under which loans must be disbursed in local currency. In addition, the NBG, under its responsible lending initiative, which came into force on 1 January 2019, introduced significantly more conservative PTI and LTV thresholds for unhedged retail borrowers, further limiting their exposure to currency induced credit risk. The changes are more relevant to hedged borrowers. For unhedged borrowers PTI and LTV thresholds will stay significantly more conservative. As a result, FX denominated loans in the retail segment decreased to 52% in 2019 compared to 56% in 2018. . Apart from the measures, which are in place throughout the underwriting process, the Bank regularly monitors and assesses the quality of foreign currency denominated loans to assess potential impact of currency depreciation on the portfolio. Based on this assessment the Bank ensures that it holds sufficient capital buffers against unexpected losses. The Bank applies conservative lending standards to un-hedged borrowers to ensure that they can withstand a certain amount of currency depreciation without credit quality deterioration.

Given the experience and knowledge built throughout the recent currency volatility, the Bank is in a good position to promptly address and mitigate emerging exchange rate depreciation risks.

Concentration Risk

The Bank is exposed to concentration risk, defined as potential deterioration in portfolio quality due to large exposures or individual industries. Deterioration of financial standing of individual borrowers, with large outstanding liabilities may entail increased credit losses and high impairment charges. Credit losses may also increase due to negative macroeconomic developments in certain industries in case the Bank's concentration in this industry is relatively high.

In order to manage concentration risks effectively, as a part of its risk appetite framework, the Bank limits both single-name and sector concentrations. Lower limits are assigned to industries with perceived higher risks.

Stringent monitoring tools are in place to ensure compliance with the established limits. The Bank constantly checks the concentrations of its exposure to single counterparties, as well as sectors. Significant counterparties are assessed on an individual basis, and in-depth analysis of industries is undertaken. These processes ensure that the Bank's concentration levels and associated risks are in compliance with predefined limits.

Along with managing concentration levels in the portfolio, the Bank estimates unexpected losses and respective capital for concentrations of both single name borrower and sectors using the Herfindahl-Hirschman Index (HHI), thus ensuring that sufficient capital is held against concentration risk.

Liquidity Risk

The liquidity risk is the risk that the Bank may either not have sufficient financial resources available to meet all its obligations and commitments as they fall due, or be only able to access those resources at a high cost.

Both funding and market liquidity risks can emerge from various factors that are beyond the Bank's control. Due to the financial market instability, factors such as a downgrade in credit ratings or other negative developments may affect the price or ability to access funding necessary to make payments in respect of the Bank's future indebtedness.

Liquidity risk is managed by the financial risk management and treasury departments and is monitored by the Management Board's Risk Committee or the Assets and Liabilities Management Committee (ALCO) within their predefined functions. The principal objectives of the bank's Liquidity Risk Management Policy are to: ensure the availability of funds to meet claims arising from total liabilities and off-balance sheet commitments, both actual and contingent, at an economic price; recognise any structural mismatch existing within the bank's statement of financial position and set monitoring ratios to manage funding in line with the bank's well-balanced growth; and monitor liquidity and funding on an ongoing basis to ensure that approved business targets are met without compromising the bank's risk profile. The Management Board reviews the Liquidity Risk Management Policy, which is then presented to the Supervisory Board for approval.

Liquidity risk is categorised into two risk types: funding liquidity risk and market liquidity risk.

Funding Liquidity Risk

The Funding liquidity risk is the risk that the Bank will not be able to efficiently meet both expected and unexpected current and future cash flows without affecting either its daily operations or its financial condition under both normal conditions and during a crisis. To manage funding liquidity risk, the Bank has an internally developed model using a liquidity coverage ratio (LCR) and a net stable funding ratio (NSFR), both under Basel III liquidity guidelines. Additionally, the Bank applies stress tests and "what if" scenario analyses and monitors the NBG's minimum liquidity ratio. In 2017, the NBG introduced its own LCR for liquidity risk management purposes. In addition to the Basel III guidelines, the ratio applies conservative approaches to the deposit withdrawal rates depending on the client group's concentration. Since September 2017, the Bank has also monitored compliance with the NBG's LCR limits. In addition to the total LCR limit, the NBG has also defined limits per currency for the GEL and foreign currencies. The LCR is calculated by reference to the qualified liquid assets divided by 30-day cash net outflows. It is used to help manage short-term liquidity risks. To promote larization in the country of Georgia, NBG defines lower limit for GEL LCR than that for FX LCR. From October 2019 FC Mandatory Reserves are considered at 100% within HQLA for NBG LCR purposes. In addition, in the same period, NBG lowered FC mandatory reserves requirements from 30% to 25%.

In September 2019, the NBG introduced a Net Stable Funding Ratio ("NBG NSFR") for funding liquidity risk management purposes. The NSFR is calculated by dividing the available stable funding by the required stable funding. It is used for long-term liquidity risk management to promote resilience over a longer time horizon by creating additional incentives for the Bank to rely on more stable sources of funding on a continuing basis. On a monthly basis, the Bank monitors compliance with the set limit for NBG NSFR.

Market Liquidity Risk

The market liquidity risk is the risk that the Bank cannot easily offset or eliminate a position at the then-current market price because of inadequate market depth or market disruption. To manage it, the Bank follows the Basel III guidelines on high-quality liquidity asset eligibility in order to ensure that the Bank's high-quality liquid assets can be sold without causing a significant movement in price and with minimum value loss.

In addition, the Bank has a liquidity contingency plan, which forms part of the overall prudential liquidity policy. The plan is designed to ensure that the Bank can meet its funding and liquidity requirements and maintain its core business operations in deteriorating liquidity conditions that could arise outside the ordinary course of its business.

As a result of COVID-19 pandemic, the NBG will implement certain countercyclical measures in relation to liquidity requirements, if necessary: decreasing LCR limits, decreasing mandatory reserve requirements in foreign currency, Updating criteria for security or repo pledging to support GEL liquidity.

Market Risk

The market risk is the risk of losses in on- and off-balance-sheet positions arising from movements in market prices.

The Bank's strategy does not foresee the involvement in trading financial instruments or investments in commodities. Accordingly, the Bank's only exposure to market risk is the foreign exchange risk in its "structural book", comprising its regular commercial banking activities, which have no trading, arbitrage or speculative intent.

Foreign Currency Risk

Due to the Georgian economy's significant reliance on foreign currencies, movements in foreign exchange rates can adversely affect the Bank's financial position. This risk stems from the open currency positions created due to mismatches in foreign currency assets and liabilities. The National

Bank of Georgia requires the Bank to monitor both balance sheet and total aggregate balance (including off-balance-sheet) open currency positions and to maintain the latter within 20% of the Bank's regulatory capital. For the year ended 31 December 2019, the Bank maintained an aggregate balance open currency position of 0.5%. From March 2019, special reserves assigned to FX balance-sheet assets started to be deductible gradually for OCP calculation purposes and as of December 2019 25% of special reserves is deductible.

As a result of COVID-19 pandemic, the NBG implemented countercyclical measure in relation to OCP requirements: postponing the phasing in of special reserved planned to be fully implemented by July 2022.

In addition, the Supervisory Board sets further limits on open currency positions. The ALCO has set limits on the level of exposure by currency and for total aggregate position that are more conservative than those set by the NBG and the Supervisory Board. The heads of the treasury and financial risk management departments separately monitor the Bank's compliance with these limits daily. Compliance with these limits is also reported daily to the Management Board and periodically to the Supervisory Board and its Risk Committee. On a Bank-wide level, foreign-exchange risk is monitored and reported monthly. To assess the currency risk the Bank performs a value-at-risk ("VAR") sensitivity analysis on a quarterly basis. The analysis calculates the effect on the bank's income determined by possible worst movement of currency rates against the GEL, with all other variables held constant. During the years ended 31 December 2019, 2018 and 2017, the sensitivity analysis did not reveal any significant potential effect on the bank's equity.

Interest Rate Risk

Interest rate risk arises from potential changes in market interest rates that can adversely affect the value of the bank's financial assets and liabilities. This risk can arise from maturity mismatches of assets and liabilities, as well as from the repricing characteristics of such assets and liabilities. The deposits, and a part of the loans offered by the bank, are at fixed interest rates, while a portion of the bank's borrowing is based on a floating interest rate. The bank's floating rate borrowings are, to a certain extent, hedged because the NBG pays a floating interest rate on the minimum reserves that TBC Bank holds with it. Furthermore, many of TBC Bank's loans to customers contain a clause allowing it to adjust the interest rate on the loan in case of adverse interest rate movements, thereby limiting exposure to interest rate risk. The management also believes that TBC Bank's interest rate margins provide a reasonable buffer to mitigate the effect of a possible adverse interest rate movement. The Bank also applies for interest rate risk hedging instruments in order to mitigate interest rate risk. The bank employs an advanced framework for the management of interest rate risk by establishing appropriate limits, monitoring compliance with them and preparing forecasts. Interest rate risk is managed by the financial risk management department and is monitored by the ALCO, which decides on actions that are necessary for effective interest rate risk management and follows up on their implementation. The major aspects of interest rate risk management development and the respective reporting are periodically provided to the Management Board, the Supervisory Board and the Risk Committee. The bank measures four types of interest-rate risk based on the source of the risk: (i) re-pricing risk; (ii) yield curve risk; (iii) basis risk; and (iv) optionality (embedded option) risk. The bank considers numerous stress scenarios, including different yield curve shifts and behavioural adjustments to cash flows (such as deposit withdrawals or loan prepayments), to calculate the impact on one-year profitability and enterprise value. Appropriate limits are set by the Supervisory Board and the Management Board's Risk Committee.

Net Interest Margin

Any decline in the Bank's net interest income or net interest margin could lead to a reduction in profitability.

The net interest income accounts for the majority of the Bank's total income. Consequently, fluctuations in its net interest margin affect the results of operations. High competition on the local banking sector could drive interest rates down, compromising the Bank's profitability. At the same time, the cost of funding is largely exogenous to the Bank and is derived based on both the national and international markets.

In 2019, the NIM decreased by 1.3 pp YoY to 5.5%. The decrease was driven by the introduction of the responsible lending regulation from 1 January 2019, limiting the Bank's ability to lend money to higher-yield retail customers.

The Bank manages its direct exposure to the LIBOR and local refinancing rates through respective limits and appropriate pricing. As of 31 December 2019, GEL 5,788 million in assets (31%) and GEL 3,813 million in liabilities (24%) were floating, related to the LIBOR/FED/ ECB (deposit facility) rates and as per internal judgment, whereas GEL 5,320 million of assets (29%) and GEL 3,360 million of liabilities (21%) were floating, related to the NBG's refinancing rate. The reprising maturity of floating liabilities within a one-year horizon exceeds the one of floating assets. The strong increase in net fee and commission income and other operating income safeguards against margin declines and profitability concerns for the Bank. The decrease in credit loss allowance driven by improved performance across all segments also supports the Bank's profitability.

To mitigate the asset-liability maturity mismatch, in cases where loans are extended on fixed rather than floating terms, the interest rate risk is translated into price premiums, safeguarding against changes in interest rates.

Counterparty Risk

TBC Bank performs banking services such as lending in the interbank money market, settling a transaction in the interbank foreign exchange market, entering into interbank transactions related to trade finance or investing in securities. Hence, the Bank is exposed to the risk of losses due to the failure of a counterparty bank to meet its obligations. To manage the counterparty risk, the Bank defines limits on an individual basis for each counterparty and as well on a portfolio basis by limiting the expected loss from both treasury and trade finance exposures. As of 31 December 2019, TBC Bank's interbank exposure was concentrated with banks that external agencies, such as Fitch Ratings, Moody's and Standard and Poor's, have assigned high A-grade credit ratings.

Operational Risk

One of the main risks that the bank faces is operational risk, which is the risk of loss resulting from inadequate or failed processes and systems, human error, fraud or external events. However, reputational risk management is also given high importance and priority and is an integral part of the organisation's overall risk culture. The bank is exposed to many types of operational risk, including: fraudulent and other internal and external criminal activities; breakdowns in processes, controls or procedures; and system failures or cyber-attacks from an external party with the intention of making the bank's services or supporting infrastructure unavailable to its intended users, which in turn may jeopardise sensitive information and the financial transactions of the bank, its clients, counterparties or customers. Moreover, the bank is subject to risks that cause disruption to systems performing critical functions or business disruption arising from events wholly or partially beyond its control, such as natural disasters, transport or utility failures etc., which may result in losses or reductions in service to customers and/or economic losses to the bank. The operational risks discussed above are also applicable where the bank relies on outside suppliers of services. Considering the fast-changing environment and sophistication of both banking services and possible fraudsters, the importance of constantly improving processes, controls, procedures and systems is heightened to ensure risk prevention and reduce the risk of loss to the bank. To oversee and mitigate operational risk, the bank has established an operational risk management framework, which is an overarching document that outlines the general principles for effective operational risk management and defines the roles and responsibilities of the various parties involved in the process. Policies and procedures enabling effective management of operational risks are an integral part of the framework. The Management Board ensures a strong internal control culture within the bank, where control activities are an integral part of operations. The Supervisory Board sets the operational risk appetite and the Operational Risk Committee oversees compliance with the limits. The Operational Risk Committee discusses the bank's operational risk profile and risk minimisation recommendations on a regular basis. The operational risk management department acts as second line of defence. It is responsible for implementing the framework and appropriate policies and procedures to enable the bank to manage operational risks, as well as monitoring operational risk events, risk exposures against risk appetite and material control issues. The department is also responsible for the day-to-day management of operational risks using various techniques. These include, but are not limited to: running risk and control self-assessments, which are aimed at detecting possible gaps in operations and processes with the purpose of suggesting appropriate corrective actions; forming an internal risk event database for further quantitative and qualitative analysis; performing internal control to detect systematic errors in banking operations, internal fraud events and monitoring key risk indicators; conducting scenario and root-cause analyses; providing business advisory services regarding nonstandard cases as well as assessments of new products and procedures; monitoring IT incident occurrence and overseeing activities targeted at solving identified problems; and obtaining insurance policies to transfer the risk of losses from operational risk events. The operational risk management department has reinforced its internal control, risk assessment teams and methodologies to further fine-tune the existing control environment. The same applies to the set of actions directed to homogenise operational risk management processes throughout the bank's member companies. The operational risk management department reports to the Chief Risk Officer. Various policies, processes and procedures are in place to control and mitigate operational risks, including: enacting an outsourcing risk management policy, which enables the bank to control outsourcing (vendor) risk arising from adverse events and risk concentrations due to failures in vendor selection, insufficient controls and oversight over a vendor and/or services provided by a vendor and other impacts to the vendor; implementing procedures to analyse systemic flaws and take corrective measures to prevent the reoccurrence of significant losses; involving the operational risk management department in the approval process for new products and services to minimise risks relating thereto; and developing a special operational risk awareness programme for the bank's employees and providing regular training to further strengthen the bank's internal risk culture. During the reporting period, one of the key operational risk management focus areas was the Risk and Control Self-Assessment (RCSA) exercise, under which the Bank's top priority processes were reviewed and areas of improvement were identified. Additionally, the Bank was actively working on the development of a Bank-wide operational risk registry.

Cyber Attack

The threat posed by cyber-attacks has increased in recent years and it continues to grow. The risk of potential cyber-attacks, which have become more sophisticated, may lead to significant security breaches. Such risks change rapidly and require continued focus and investment. No major cyber-attack attempts have targeted Georgian commercial banks in recent years. Nonetheless, the bank's rising dependency on IT systems increases its exposure to potential cyber-attacks

The bank actively monitors, detects and prevents risks arising from cyber-attacks. Staff members monitor the developments on both the local and international markets to increase awareness of emerging forms of cyber-attacks. Intrusion prevention and Distributed Denial of Service (DDoS) protection systems are in place to protect the bank from external cyber-threats. Security incident and event monitoring systems, in conjunction with the respective processes and procedures, are in place to handle cyber -incidents effectively. Processes are continuously updated and enhanced to respond to new potential threats. A data recovery policy is in place to ensure business continuity in case of serious cyber-attacks. In addition, an Information Security Steering Committee is actively involved in improving information security and business continuity management processes to minimise information security risks. As a result of COVID-19 pandemic, the Bank activated secure remote working policies, which ensures that home-working environments are protected against relevant cyber-threats and security team provides effective oversight of teleworking channels.

Reputational Risk

The Bank is currently exposed to reputational risk. The media coverage in Georgia surrounding the founders' of the Bank represents a risk to the reputation of the Bank

There are principal risks, which may arise from negative publicity surrounding TBC Bank and its public perception, as well as that of the banking sector in Georgia as a whole. In particular, the media exposure in relation to TBC Bank and its founders' has threatened to have an adverse impact on the Bank's operations. An inability to manage such reputational risks could have an adverse impact upon the Bank and its stakeholders, including its clients, employees and shareholders

To mitigate possibility of reputational risks, the Bank works continuously to maintain strong brand recognition within its stakeholders. The Bank actively monitors its brand value by receiving feedback from stakeholders on an ongoing basis. The Bank tries to identify early warning signals of potential reputational or brand damage in order to both mitigate it and elevate it to the attention of the Supervisory Board before escalation. Dedicated internal and external marketing and communications teams are in place, which have the responsibility to monitor risks, develop scenarios and create respective action plans.

Regulatory Risk

The Bank's activities are highly regulated and thus, face regulatory risk. The national regulator, the National Bank of Georgia, can increase the prudential requirements across the whole sector as well as for specific institutions within it. Therefore, the Bank's profitability and performance may be compromised by an increased regulatory burden, including higher capital requirements.

Alongside with mandatory capital adequacy ratios, the regulator sets lending limits and other economic ratios, including lending, liquidity and investment ratios.

During 2019, the NBG introduced the full version of the responsible lending regulation limiting the growth of the consumer loans. The regulation defined income verification techniques and introduced caps on payment-to-income (PTI) ratios, loan-to-value (LTV) ratios and the maximum maturity of retail loans; stricter thresholds are applied to loans denominated in foreign currency. Under the Georgian banking regulations, the Bank is required, among other things, to comply with minimum reserve requirements and mandatory financial ratios and regularly file periodic reports. The Bank is also regulated by respective tax code or other relevant laws in Georgia. The Bank's operations remain in full compliance with all relevant legislation and regulations. The Bank is also subject to financial covenants in its debt agreements.

The Bank has established systems and processes to ensure full regulatory compliance, which are embedded in all levels of the Bank's operations. The dedicated Compliance Department reports directly to the Chief Executive Officer and bears the primary responsibility for regulatory compliance. The Bank's Risk Committee is responsible for regulatory compliance at the Supervisory Board level. In terms of banking regulations and Georgia's taxation system, the Bank is closely engaged with the regulator to ensure that new procedures and requirements are discussed in detail before their implementation. There was also an extensive dialogue with the regulator regarding the new regulation on responsible lending. Together with the new regulation on responsible lending, the government introduced initiatives to ensure continuous broad access to financing. These include simplification of the tax code to incentivize income registration rate. Although decisions made by regulators are beyond the Bank's control, significant regulatory changes are usually preceded by a consultation period that allows all lending institutions to provide feedback and adjust their business practice.

The Bank was subject to an inspection by the NBG in connection with certain transactions, which took place in 2007 and 2008. The inspection alleged that these transactions between the Bank and certain entities were not in technical compliance with the Georgian law regulating conflicts of interest. In

February 2019, the parent Company of the bank, the Bank and the NBG issued a joint statement. confirming the settlement of this investigation and stating that the Bank fully complied with the economic normative requirements and limits set by the NBG In parallel, the Georgian Office of Public Prosecution launched an investigation into the same matter and has charged the founders of the Bank. The court case with the founders is ongoing. However, the founders have stood down from all their positions within the Group and the Bank. The Bank, with the assistance of external advisers, undertook a review of the Bank's relevant internal controls systems. Although these reviews did not identify any material deficiencies in the Bank's existing internal controls and compliance systems, they did make certain technical recommendations for further improvements of the Bank's processes and procedures, which are being implemented.

Compliance Risk

The compliance risk is defined as the risk of regulatory or legal sanctions, material financial losses or reputation defamation, which may result from the Bank's negligence or inappropriate implementation of the relevant laws, regulations and rules, ethics, and behaviour code.

Georgia is a fast-paced developing country with the goal of European integration and its legislative base is constantly updated.

Besides the national legislation, JSC TBC Bank is subject to the certain UK regulations, since the shares of the Bank's mother company are traded in the premium segment of the London Stock Exchange.

Consequently, continuous monitoring, analysis, and timely implementation of national and international legislative amendments pose a significant challenge to the Bank.

The risk management of the Bank's compliance handles the following processes:

- Introduction of corporate ethics and risk sensing culture;
- Management of related party transaction process;
- Management of Whistleblowing process
- Prevention of bribery, anti-corruption, and tax avoidance;
- Prevention of illicit income legalisation and terrorism funding;
- Protection of consumers' rights;
- Regulatory change management.

In order to ensure the management of these processes, the Bank has developed policies, instructions, rules, and provisions, which are mandatory for all its employees.

The Bank's Compliance Risk Management Department provides the identification, assessment, monitoring and periodic review of the compliance risk.

The Bank's Compliance Risk Management Department is directly subordinated to the CEO and is accountable to the Risk Committee of the Supervisory Board.

Capital Risk

The Bank faces the capital risk of not meeting the minimum regulatory requirements under the increasing capital requirement framework, which may compromise growth and strategic targets. Additionally, adverse changes in FX rates may affect the capital adequacy ratios.

In December 2017, the NBG introduced a new capital adequacy framework. Under the updated regulation, capital requirements consist of a Pillar 1 minimum requirement, combined buffers (systemic, countercyclical and conservation buffers) and Pillar 2 buffers, which are introduced gradually over a four-year period. As of 31 December 2019, the Bank's minimum capital requirements increased by 0.6%, 0.7% and 0.8% for CET1, Tier 1 and Total Capital, respectively, compared to the end of 2018. The increase in minimum requirements is mainly driven by a planned increase in the systemic risk buffer of 0.5%. The Bank's capitalization as of December 2019 stood at 12.0%, 14.6% and 19.1% compared to the regulatory minimum requirement of 10.4%, 12.5% and 17.5% for CET1, Tier 1 and Total capital, respectively. The ratios were well above the respective regulatory minimums. In 2019, the Bank further strengthened and optimized its capital position by issuing an Additional Tier 1 instrument in the amount of US$ 125 million.

As a result of COVID-19 pandemic, the NBG implemented certain countercyclical measures in relation to capital adequacy requirements:

- Postponing the phasing in of concentration risk and the net GRAPE (General Risk Assessment Program) buffer capital requirements on CET1 capital, planned in March 2020;
- Allowing banks to use the conservation buffer and 2/3 of currency induced credit risk (CICR) buffer;
- Leaving possibility of releasing all the remaining pillar 2 buffers (remaining 1/3 CICR, concentration risk and Net Grape buffers) in case of necessity.

During the time the Bank utilizes conservation and Pillar 2 buffers, it is restricted to make any capital distribution. If the NBG changes the decision with regards to capital adequacy limits, the banking sector shall have one year to comply with the changes.

Besides the expected negative impact of COVID-19 pandemic, GEL volatility still remains one of the significant risks impacting the Bank's capital adequacy. A 10% GEL depreciation would translate into a 0.80pp, 0.69pp and 0.51pp drop in the Bank's CET 1, Tier 1 and Total regulatory capital adequacy ratios, respectively.

The Bank undertakes stress-testing and sensitivity analysis to quantify extra capital consumption under different scenarios. Such analyses indicate that the Bank holds sufficient capital to meet the current minimum regulatory requirements. Capital forecasts, as well as the results of the stress-testing and what-if scenarios, are actively monitored with the involvement of the Bank's Management Board and Risk Committee to ensure prudent management and timely actions when needed.

The Bank created an extra loan loss provision buffer to prepare for the potential impact of the COVID-19 pandemic on the Georgian economy. As of 31 March 2020, TBC Bank booked additional provisions in accordance with local standards in amount of approximately 3.1% of the loan book.

Strategic Initiatives Risk

The Bank may face the risk of developing a business strategy that does not safeguard long-term value creation in an environment of changing customer needs, competitive environment and regulatory restrictions. In addition, the Bank may be exposed to the risk that it will not be able to effectively deliver on its strategic priorities and thereby compromise its capacity for long-term value creation.

The Bank conducts annual strategic review sessions involving the Bank's top and middle management in order to ensure that it remains on the right track and assess business performance across different perspectives, concentrating analysis on key trends and market practices, both in the regional and global markets. In addition, the Bank continuously works with the world's leading consultants in order to enhance its strategy. Further, the Bank conducts quarterly analysis and monitoring of metrics used to measure strategy execution, and in case of any significant deviations, it ensures the development of corrective or mitigation actions.

Qualified employees risk

The Bank faces the risk of losing of key personnel or the failure to attract, develop and retain skilled or qualified employees. In particular, the strategic decision to transform into a digital company entails increased demands on high calibre IT professionals across the Bank. In addition, in order to adapt to the fast changing business environment, the Bank needs to foster an "Agile" culture and equip employees with the necessary skills.

The Bank pays significant attention to human capital management strategies and policies, which include approaches to the recruitment, retention and development of talent, and offers competitive reward packages to its employees. The Bank has also developed and implemented an "Agile" framework that aims to increase employee engagement and satisfaction. Moreover, the Bank set up an IT academy to attract and train young professionals. The best students are offered employment at the Bank. In addition, the Bank has an in-house academy that provides various courses for the employees in different fields.

Emerging Risks

Emerging risks are those that have large unknown components and may affect the performance of the Bank over a longer time horizon. We believe the following are risks that have a potential to increase in significance overtime and could have the same impact on the Bank as the principal risks.

Climate change risk

The risks associated with climate change have both physical impact arising from more frequent and severe weather changes and transitional impact that may entail extensive policy, legal and technological changes to reduce ecological footprint of the households and businesses. For the Bank, both of these risks can materialise through the impairment of asset values and deteriorating creditworthiness of our customers, which could result in reduction of the Bank's profitability. The

Bank may also become exposed to reputational risks as a result of its lending to or other business operations with the customers deemed to be contributing to climate change.

The Bank's objective is to act responsibly and manage the environmental and social risks associated with its operations in order to minimise negative impacts on the environment. This approach enables us to reduce our ecological footprint by using resources efficiently and promoting environmentally friendly measures in order to mitigate climate change.

The Bank has in place an Environmental Policy, which governs its Environmental Management System (the "EMS") and promotes adherence of the Ban's operations to the applicable environmental, health and safety and labour regulations and practices. We take all reasonable steps to support our customers in fulfilling their environmental and social responsibilities. Management of environmental and social risks is embedded in the Bank's lending process through the application of the EMS. The Bank has developed risk management procedures to identify, assess, manage and monitor environmental and social risks. These procedures are fully integrated in the Bank's credit risk management process. Our Environmental Policy is fully compliant with Georgian environmental legislation and follows international best practices

The Bank's performance may be affected by Libor discontinuation and transition

There is a number of different types of financial instruments on the Bank's balance sheet, each of which carries interest rates benchmarked to the London Interbank Offered Rate ("LIBOR"). LIBOR is also used by the Bank in its risk measurement, accounting and valuation processes. In 2017, the FCA announced that it has agreed with LIBOR panel banks to sustain LIBOR until the end of 2021 and called financial sector participants to start working towards the transition to other reference rates. The discontinuation of LIBOR and the process of transition exposes the Bank to execution, conduct, financial and operational risks, and may result in earnings volatility, customer complaints and legal proceedings, or have other adverse impact on the Bank's business and operations

The Bank is in the process of identifying implications of such transition to other reference rates on its risk profile by analysing its execution, conduct, financial and operational risks and how such risks could be addressed. TBC is proactively working with industry participants, such as the NBG, the Banking Association of Georgia and IFI lenders to facilitate orderly transition to other reference rates. The Bank is starting its efforts to raise awareness of the transition, both internally and externally, to ensure that staff has all the necessary knowledge and tools to facilitate the transition and that all of the Bank's customers are treated fairly. We actively monitor the international as well as local transition-related developments to regulate and align the Bank's transition process with the market practice.

Spread of coronavirus (COVID-19) comes with unpredictable economic and social consequences risk

COVID-19 outbreak, declared as a pandemic by the World Health Organisation, started in China and spread rapidly around the world in early 2020. COVID-19 pandemic has already caused major economic disruptions, halted international travel and resulted in country lockdowns. COVID-19 pandemic results in a decreased economic growth in Georgia, increased unemployment, depreciation of the GEL, decreased commodity and real estate prices and impaired creditworthiness of the private sector, and increases financial and non-financial risks of the Bank.

As tourism contribution in Georgian economy was significant, the impact is likely to be sizable. The growth is also expected to be impacted negatively through lower exports, remittances and FDI inflows, as well as the lockdown to prevent the widespread of the virus. At the same time, imports should also adjust. Nevertheless, there will be increase in current account balance.

However, Georgia is acting very actively to attract support from the international financial organisations. According to the government's announcement as of 15 March, around US$ 1.7 billion, or 10% of 2019 GDP would be mobilized to support predominantly the government's financing needs and partially the central bank's international reserves. In addition, around US$ 1.5 billion should be used to support the private sector. This injections are expected to materially counteract the negative impact of the COVID-19 crisis. Per IMF projections, as of 14th April, Georgian economy is expected to contract by 4.0% in 2020, while in 2021 the growth is expected to recover to 4.0%.

Together with the international support, it is also important to take into account that there we no signs of overheating of the Georgian economy during the pre-distress period, including the housing market. Therefore, assuming the COVID-19 is predominantly temporary, rather than permanent shock, most of the industries should recover relatively quickly with the hospitality sector likely lagging behind for some additional period.

The Bank actively analyses various scenarios of economic consequences of COVID-19 pandemic. We introduced three month grace period on payments of principal and interest for all retail and MSME customers and hardly-hit corporate borrowers.

We have close communications with our business customers discussing their strategies and sharing our outlook on the economy and its key sectors.

In addition, as part of the stress testing exercise, we have analysed multiple scenarios to ensure that the Bank has sufficient liquidity and capital to meet updated regulatory capital and liquidity requirements. The NBG implemented countercyclical measures to support financial stability of the banking system by relaxing capital and liquidity requirements if necessary.

Moreover, the government has come up with a number of initiatives to support businesses and the economy such as (i) deferral of income taxes for companies operating in tourism industry, (ii) subsidizing interest payments for small and medium sized hotels (iii) doubling the volume of VAT refunds to companies (iv) increasing capital expenditure and providing additional economic incentives.

Credit Risk Mitigation

For the purposes of credit risk mitigation, the Bank actively uses various types of collateral. Real estate, movable property, intangible assets, financial assets, suretyship and third party guarantee can be used by the Bank as collateral. The Bank has appropriate processes in place to ensure that the market value of collateral is defined properly and collaterals serve as an effective tool for credit risk mitigation.

Key Policy and Procedures for Collateral Management & Appraisal

Collateral represents the most significant credit risk mitigation tool for the Bank, making effective collateral management one of the key risk management components. Collateral on loans extended by the Bank may include, but is not limited to, real estate, cash deposits, vehicles, equipment, inventory, precious metals, securities and third-party guarantees. The collateral accepted against a loan depends on the type of credit product and the borrower's credit risk. The Bank has a largely collateralized portfolio in all its segments, with real estate representing a major share of collateral. A centralized unit for collateral management governs the Bank'sview and strategy in relation to collateral management, and ensures that collateral serves as an adequate mitigating factor for credit risk management. The collateral management framework consists of a policy-making process, a sound independent valuation process, a haircut system throughout the underwriting process, collateral monitoring (including revaluations and statistical analysis) and collateral portfolio analysis.

The Collateral Management and Appraisal Department (CMAD) defines Collateral Management Policy & Collateral Management Procedures (approved by the Board), purchases an appraisal service that must be in line with International Valuation Standards IVS), acting NBG regulations and internal rules (policy/procedures and etc.), authorizes appraisal reports, manages collateral monitoring process (assets with high FV are revaluated annually, while statistical monitoring is used for collaterals with low value). The CMAD uses a mixed quality check scheme for valuation: appraisal reports are reviewed internally by its staff and separately by an external company. Almost all activities under the collateral management are automated through an in-house web application. The collateral management function uses market researches conducted under the project: Real Estate Market laboratory (REM lab).

Main Types of Collateral

According to the Bank's Collateral Management Policy, collaterals are divided into 5 groups:

- Real estate;
- Movable property;
- Intangible asset;
- Suretyship, guarantee.

Required collaterals are defined based on the credit product type and borrower's risk profile. The Bank's credit portfolio is well secured, with the main type of collateral being real estate.

For the purpose of capital adequacy calculation, the Bank uses the following types of collateral:

- Cash deposits;
- Third party guarantees.

In order collateral to be used for the purpose of capital adequacy estimations, the requirements of the National Bank shall be satisfied in accordance with the provisions of the Capital Adequacy Requirements of the Commercial Banks.

Information on Credit Risk Concentrations According to Mitigation Tools

The Bank's credit portfolio is well secured. 68% of the portfolio is secured with real estate, 5% is secured by cash deposits and jewellery (3.5% and 1.5% respectively). Other types of collateral are: movable property and third-party guarantees.

Main Types of Guarantees and Contracts Received as Collateral

The significant part of guarantees and counter guarantees that are used as collateral for credit risk mitigation, are banking guarantees/counter guarantees. The Bank's assessment process is held by the Financial Risk Management (FRM) department in accordance with the business requirements. In particular, the request for financing of various banking products arises from the Treasury, Trade Financing and Business Units.

Interbank Limit Assessment Procedure

According to the procedure, the Trade Finance department receives the application about the guarantee/letter of credit/factoring request from a counter guarantee bank and provides the financial risk management department with the respective information. In addition, the Treasury and Financial Service department sends a request about setting the limit on the bank for treasury purposes. The Compliance Department checks the counter-party bank, the applicant, the beneficiary and the financing operation in case of Trade Finance request, and the counter-party bank, in case of Treasury request. After receiving a positive recommendation from Compliance Department, the assessment of counter-party bank is conducted by the FRM department based on the "Counterparty risk limits assessment methodology".

The limits of counter-party banks are set according to ratings assigned by the international rating agencies (Moody's; Fitch Ratings; S&P) and/or ratings derived from an internally-developed model[3], based on which maturity of transactions is defined with the respective limits.

If the counter-guarantee banks average international rating is more than or equal to "BBB", the FRM uses the latter rating for defining the limit and assesses the bank's main financial and non-financial metrics.

If the bank is assessed by one international rating agency, or its average credit rating is less than "BBB", the bank's assessment is done by an internally developed model, based on the following factors:

- **Bank's Financial Metrics:**
  - Capital adequacy;
  - Credit portfolio quality;
  - Liquidity and funding;
  - Profitability.

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[3]If the counterparty is a resident bank, the final rating is defined based on the internal model developed. In case of non-resident banks, where the average international rating is more than or equal to "BBB", the final rating is derived as a minimum between average international and internal ratings.

- **Warning Signals:**
  - Governance;
  - Risk management framework;
  - International credit rating;
  - Operating environment;
  - Regulatory environment and other signals.

After analysing the counter-guarantee bank's financial and non-financial metrics, the FRM presents its recommendation to the respective decision-making committee. In order to ensure the compliance with the decision-making tiers and flawless implementation of risk approval process, the FRM uses the "Asset and Liability Management Committee Policy" and the "Instruction on Counter-party Risk Approval Committee Decision-Making Process" as a guideline.

The FRM may consider setting general limit for the counter-party bank, if the Trade Finance department deems it necessary, due to possible frequent future transactions.

The counterparty limits monitoring is carried out on a daily basis by the Assets and Liabilities Management Group (ALM). In case of limit breaches, the ALM informs the FRM and Settlements and Correspondent Banking Department in order to take immediate actions for mitigation

TBC Bank has in place a Counter-Party Risk Management Policy, which determines the principles of the process for the counterparty risk management and it regulates the activities of the departments and employees involved.

The FRM reviews the Interbank Limit Assessment Methodology on an annual basis.

International Ratings

With regards to the credit rating, the Bank may use the evaluations made by the following organisations: Fitch, Moody's, and S&P. The credit ratings are used for the following risk classes:

- unconditional and conditional requirements for multilateral development banks;
- unconditional and conditional requirements for commercial banks;
- Unconditional and conditional requirements for central governments and central banks.

The credit rating mapping to credit rating quality is outlined in the table below:

Allowed Credit Rating	Credit rating quality	Fitch	Moody's	S&P
Mapping of credit rating quality– with long-term credit rating	1	From AAA to AA-	From Aaa to Aa3	From AAA to AA-
	2	From A+ to A-	From A1 to A3	From A+ to A-
	3	From BBB+ to BBB-	From Baa1 to Baa3	From BBB+ to BBB-
	4	From BB+ to BB-	From Ba1 to Ba3	From BB+ to BB-

	5	From B+ to B-	From B1 to B3	From B+ to B-
	6	CCC+ and worse	Caa1 and worse	CCC+ and worse

Risk Appetite

The Bank has developed a risk appetite framework that ensures risk-culture communication with the Bank's management and Supervisory Board.

The risk appetite framework includes quantitative and qualitative risk indicators, sets limits and defines acceptable levels for identified risks to support the Bank's business strategy.

The risk appetite framework includes the risk assessment and management for all major categories of risk (credit, financial, operational, liquidity, market, capital, supervisory indicators). The cascading indicators of risk appetite support identification of risks in a more efficient and timely manner, dissemination of information, and planning of relevant activities prior to risk occurrence.

For the effective risk management, the process involves identifying, assessing, determining the desired level of risks, monitoring, and carrying out risk mitigation activities, in case, it exceeds the boundaries established by the Bank.

The risk identification is a continuous process. Once the risk is identified, it is assessed and materiality level is determined. For all potential and principal risks, the risk appetite framework sets limits that are acceptable for each parameter to comply with the Bank's risks and business strategies.

The risk appetite framework sets three levels, corresponding to the Bank's three-layered approach to risk:

- **Green Zone** – desired risk level for the bank, which is important to maintain the Bank's long-term strategy;
- **Yellow zone** – an acceptable level of risk, but it is necessary to take actions to return the risk to the desired green zone;
- **Red zone** – A warning risk level that requires quick solutions and activities to mitigate the risk.

For each level, the risk appetite framework sets out necessary actions to ensure the continuous management and monitoring of risk parameters and prompt activities, in case the desired green zone of risk profile is violated.

The Bank's Supervisory Board is responsible for approving the risk appetite. The enterprise risk department is responsible for day to day management of risk appetite framework.

The information about the risk appetite outcomes and the necessary updates are provided in the monthly reports of the Bank's Management Board. Quarterly results are presented at the Risk Ethics and Compliance Committee session.

Capital Management

For the effective management of capital adequacy the Bank is carrying out short and long term capital adequacy forecasting, to timely identify factors that can affect it and avoid breaching capital adequacy limits; The Bank conducts enterprise wide stress testing exercises in order to estimate losses under the predefined scenario. The enterprise-wide stress testing is held annually and results are reported to the management and risk committee of the Supervisory Board. The Bank periodically provides additional sensitivity analysis against currency depreciation and changes in the macroeconomic environment to ensure prudent capital management. Determination of Capital Adequacy Limits.

Within risk appetite framework, the Bank sets capital adequacy limits as for CET1, Tier1 and Total Capital ratios. These limits ensure that the Bank holds enough capital to meet Basel III rising requirements, which are compliant with estimated economic capital and stress test results.

Capital Allocation and Pricing

Effective capital governance implies determination of accurate capital levels for all assets and its effective allocation, for loan pricing purposes. The process ensures capital optimization and generation of target profitability.

Risk Reporting

The effective risk analysis and management process facilitates a correct, reliable, and timely reporting which is provided by the Risk Reporting Department.

The Risk Management Department analyses the credit portfolio on a monthly basis. It analyses all portfolio's indicators such as the volume, growth rate, structure, overdoes, vintage analysis, concentration level, maturity, non-performing loans, write-off coefficients, provision charges etc.

Each ratio is analysed for the total portfolio, as well as for each segment with the respect of historical and planned indicators. In addition, operational and financial risks are also examined monthly, alongside the compliance of the risk profile with the risk appetite limits.

The risk management results and analysis are presented to the Management Board in a monthly report and quarterly results are discussed with the Risk Committee of the Supervisory Board.

These reports cover the following main issues:

- Risk appetite;
- Credit risk results;
- Liquidity risk results;
- Operational risk results;
- Financial risk results;
- Market risk results;
- Capital management.

In addition to the above-mentioned topics, the committee get updates and discusses other relevant topics such as:

- Regulatory changes;
- Update on the risk strategic objectives;
- Important methodological or strategic changes, etc.

Remuneration Policy for Top Management and Non-executive Directors

Please refer to the Annual Report 2018 (pages 136-155) and Annual Report 2019 (pages 151-179) for the information on the Remuneration Policy for the non-executive directors and top management.

Material Risk Takers

Material risk takes are considered the staff who have a material impact on the Bank's risk profile. Below is outlined the key criteria the Bank applies to define the material risk takers (MRT):

- The staff being a member of the management function;
- The staff being a member of the supervisory board function;
- Any other staff the Bank considers having a significant influence on the Bank's risk profile.

There were 16 employees identified as MRTs as of December 2019.

Remuneration throughout the Bank

The middle management in the Bank including material risk takers as well as some other key employees receive their entire salary in cash and are also eligible to cash and share bonus. The share bonuses granted are subject to 3 years of continued employment condition and holding period gradually lifting the conditions.

All other employees in the Bank receive cash salaries and may be eligible to receive cash bonuses. Executive director and employee pay is studied and determined through the use of appropriate market data usually with input from a compensation consultant.

All employees receive a competitive benefit package in line with Georgian market practice and are entitled to participate in the pension scheme on a voluntary basis.

Share-based compensation scheme

Each year, subject to predefined performance conditions, a certain number of shares will be awarded to the Bank's middle managers. The performance features represent the performance indicators that are set on an individual basis are used to calculate the number of shares to be awarded to each employee. Share salaries are subject to a condition of continuous employment for 3 years and malus and clawback provisions. These conditions are lifted as follows: 33% of the award on the first anniversary from the award date, a further 33%, on the second anniversary from award date and the final 34% of the on the third anniversary from the award date.

Before those conditions are met, the awarded shares cannot be sold or transferred to third parties. This approach ensures that the participants' interests are closely aligned with the Group's long-term strategy and shareholders' interests.

The share-based compensation scheme was also introduced for the employees within the agile structure.

Considering Risks in the Bank's Remuneration System

Remuneration policies and procedures at the Bank provide maintaining the balance between the Bank's business goals and the desired risk profile.

The remuneration system ensures that the evaluation and relevant compensation for the employees with controlling performance (risk management, compliance and internal audit) are independent from the business results of the business units under their supervision and/or control and are assessed taking into account their performance's effectiveness and quality.

The Bank's remuneration system is consistent with the risk management strategy. It includes a variable payment component that covers the Bank's main risks: credit, operational, financial (liquidity and market risks), regulatory and compliance risk (detailed information on each risk is given in chapter on Key Risks).

The variable remuneration includes components with both a quantitative and qualitative evaluation. It is set at the beginning of each year and is assigned on an individual basis, according to the activity and function of the structural unit. The quantitative and qualitative goals of each direction are defined in accordance with the Bank's strategy and risk appetite and ensure the fulfillment of the Bank's overall objectives. The goals in the remuneration component are taken into consideration for the risk management staff as well as the employees of business lines. For a better understanding of the remuneration's variable components, there are a number of possible risk indicators representing an example of a quantitative goal:

- Non-performing loans ratio – In a variable remuneration system, credit risks are taken into consideration according to the given risk indicator. Performance levels are defined both at the business segment level and the overall Bank level;
- Cost of risk – This risk indicator is another quantitative goal of the credit risks and is also defined both at the business segment level and the overall Bank level;
- Net operational loss ratio – The quantitative indicator of these operational risks provides the motivation for reducing losses generated from the Bank's operational risks.

Examples of qualitative goals may include particular objectives, such as improving current risk models or implementing new risk assessment tools that serve effective implementation of the bank's strategic goals, optimize processes or improve risk management.