

# **JSC Kor Standard Bank**

## **Consolidated Financial Statements**

*For the year ended 31 December 2014*

*Together with Independent Auditors' Report*

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## Independent auditors` report

To the Shareholders and Board of Directors of JSC Kor Standard Bank

We have audited the accompanying consolidated financial statements of JSC Kor Standard Bank and its subsidiary, which comprise the consolidated statement of financial position as at 31 December 2014, and the consolidated statements of comprehensive income, of changes in equity and of cash flows for the year then ended, and a summary of significant accounting policies and other explanatory information.

### **Management's responsibility for the consolidated financial statements**

Management is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with International Financial Reporting Standards, 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.

### **Auditors' responsibility**

Our responsibility is to express an opinion on the fairness of these consolidated financial statements based on our audit. We conducted our audit in accordance with International Standards on Auditing. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance whether the consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditors' judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the consolidated financial statements 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 entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

### **Opinion**

In our opinion, the consolidated financial statements present fairly, in all material respects, the financial position of JSC Kor Standard Bank and its subsidiary as at 31 December 2014, and their financial performance and their cash flows for the year 2014 in accordance with International Financial Reporting Standards.

*EY Georgia LLC*

11 May 2015

**Consolidated statement of financial position****As of 31 December 2014***(Thousands of Georgian lari)*

	<i>Notes</i>	<b>2014</b>	<b>2013</b>
<b>Assets</b>			
Cash and cash equivalents	5	71,865	47,167
Mandatory reserve deposit with the National Bank of Georgia		31,222	28,673
Loans to customers	6	308,856	252,888
Investment securities held to maturity	7	46,180	40,191
Premises and equipment	8	12,640	13,695
Goodwill	9	20,374	20,374
Other intangible assets	10	5,542	6,462
Current income tax asset		209	209
Other financial assets	12	993	6,716
Other assets	13	5,382	5,765
<b>Total assets</b>		<b>503,263</b>	<b>422,140</b>
<b>Liabilities</b>			
Amounts due to credit institutions	14	35,388	20,683
Amounts due to customers	15	339,969	296,478
Deferred tax liability	11	1,410	605
Other financial liabilities	12	5,242	2,837
Other liabilities	13	92	80
Subordinated debts	16	28,020	8,737
<b>Total liabilities</b>		<b>410,121</b>	<b>329,420</b>
<b>Equity</b>			
Share capital	17	99,516	99,516
Accumulated losses		(6,374)	(6,796)
<b>Total equity</b>		<b>93,142</b>	<b>92,720</b>
<b>Total liabilities and equity</b>		<b>503,263</b>	<b>422,140</b>

Signed and authorised for release on behalf of the Bank on 11 May 2015:

Thea Lortkipanidze

General Director

Maia Kakhetelidze

Chief Accountant

**Consolidated statement of comprehensive income****For the year ended 31 December 2014***(Thousands of Georgian lari)*

	<i>Notes</i>	<b>2014</b>	<b>2013</b>
Interest income		47,039	42,514
Interest expense		(23,195)	(21,523)
<b>Net interest income</b>	19	<b>23,844</b>	<b>20,991</b>
Loan impairment (charge) / reversal	6	(7,855)	1,893
<b>Net interest income after loan impairment charge</b>		<b>15,989</b>	<b>22,884</b>
Net fee and commission income	20	1,422	2,362
Net gains from trading in foreign currencies		1,865	2,282
Other income		401	249
Net loss from foreign exchange translation		(107)	(266)
<b>Other non-interest income</b>		<b>3,581</b>	<b>4,627</b>
Personnel expenses		(9,061)	(10,046)
Administrative and other operating expenses	21	(6,117)	(6,282)
Depreciation and amortisation	8,10	(3,165)	(3,071)
Loss on revaluation of investment property		-	229
<b>Other non-interest expenses</b>		<b>(18,343)</b>	<b>(19,170)</b>
<b>Income before income tax</b>		<b>1,227</b>	<b>8,341</b>
Income tax charge	11	(805)	(966)
<b>Profit for the year</b>		<b>422</b>	<b>7,375</b>
Other comprehensive income		-	-
<b>Total comprehensive income for the year</b>		<b>422</b>	<b>7,375</b>

**Consolidated statement of changes in equity****For the year ended 31 December 2014***(Thousands of Georgian lari)*

	<i>Notes</i>	<i>Share capital</i>	<i>Accumulated losses</i>	<i>Total equity</i>
31 December 2012	17	99,516	(14,171)	85,345
Total comprehensive income for the year		–	7,375	7,375
31 December 2013		99,516	(6,796)	92,720
Total comprehensive income for the year		–	422	422
31 December 2014		99,516	(6,374)	93,142

**Consolidated statement of cash flows****For the year ended 31 December 2014***(Thousands of Georgian lari)*

	<i>Notes</i>	<i>2014</i>	<i>2013</i>
<b>Cash flows from operating activities</b>			
Interest received		46,414	42,042
Interest paid		(22,711)	(20,842)
Fees and commissions received		3,956	5,255
Fees and commissions paid		(2,490)	(3,055)
Net gains received from trading in foreign currencies		1,865	2,282
Other operating income received		16	343
Personnel expenses paid		(9,008)	(9,717)
Administrative and other operating expenses paid		(5,199)	(5,138)
<b>Cash flows from operating activities before changes in operating assets and liabilities</b>		<b>12,843</b>	<b>11,170</b>
Net decrease / (increase) in mandatory reserve deposits with the National Bank of Georgia		204	(2,511)
(Increase) in loans to customers		(40,202)	(37,391)
(Increase) in other financial assets		(507)	(7,902)
(Increase) in other assets		1,865	(459)
Increase in amounts due to credit institutions		13,672	19,397
Increase in amounts due to customers		20,549	21,996
Increase in other financial liabilities		2,232	1,157
Increase/(decrease) in other liabilities		12	(648)
<b>Net cash from operating activities before income tax</b>		<b>10,668</b>	<b>4,809</b>
Income taxes paid		-	-
<b>Net cash from operating activities</b>		<b>10,668</b>	<b>4,809</b>
<b>Cash flows from investing activities</b>			
Acquisition of investment securities held to maturity		(41,954)	(52,899)
Proceeds from redemption of investment securities held to maturity		36,340	30,956
Acquisition of premises and equipment	8	(758)	(1,481)
Proceeds from disposal of premises and equipment		48	169
Acquisition of other intangible assets		(725)	(823)
<b>Net cash used in investing activities</b>		<b>(7,049)</b>	<b>(24,078)</b>
<b>Cash flows from financing activities</b>			
Proceeds from subordinated debt		18,636	-
<b>Net cash from financing activities</b>		<b>18,636</b>	<b>-</b>
Effect of exchange rates changes on cash and cash equivalents		2,443	1,652
<b>Net increase/(decrease) in cash and cash equivalents</b>		<b>24,698</b>	<b>(17,617)</b>
<b>Cash and cash equivalents, beginning</b>	5	<b>47,167</b>	<b>64,784</b>
<b>Cash and cash equivalents, ending</b>	5	<b>71,865</b>	<b>47,167</b>

(Thousands of Georgian lari)

## 1. Principal activities

JSC Kor Standard Bank ("the Bank") was registered on 6 March 2008 in accordance with Georgian legislation. The Bank operates under a general banking license issued by the National Bank of Georgia (the "NBG"; the central bank of Georgia) on 25 February 2008.

As at 31 December 2014, the Bank has 19 operating branches in all major cities of Georgia (2013:18). The Bank's registered legal address is 3, K. Tsamebuli Avenue, Tbilisi 0103, Georgia.

The Bank accepts deposits from the public and extends credit, transfers payments in Georgia and abroad, exchanges currencies and provides other banking services to its commercial and retail customers. Its head office is in Tbilisi.

As at 31 December 2014 and 2013, the following shareholders own the Bank:

Shareholder	%
Sheikh Nahayan Mabarak Al Nahayan	45%
Sheikh Hamdan Bin Zayed Al Nahayan	20%
Sheikh Mohammed Butti Al Hamed	15%
Sheikh Mansoor Bin Sultan Al Nahayan	15%
LTD Investment Trading Group	5%
<b>Total</b>	<b>100%</b>

## 2. Basis of preparation

### General

These consolidated financial statements of JSC Kor Standard Bank and its subsidiaries (collectively referred to as "the Bank") have been prepared in accordance with International Financial Reporting Standards ("IFRS").

The consolidated financial statements have been prepared under the historical cost convention except for the measurement at fair value of financial assets and liabilities and investment property.

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

### Subsidiary

The consolidated financial statements as of 31 December 2014 and 2013 include following subsidiary:

<i>Subsidiary</i>	<i>Country of incorporation</i>	<u>The Bank ownership %</u>		<i>Date of incorporation</i>	<i>Date of acquisition</i>
		<i>2014</i>	<i>2013</i>		
Standard Insurance LLC	Georgia	100%	100%	29-Sep-07	6-Mar-08

The subsidiary had no operations in 2014 and 2013.



(Thousands of Georgian lari)

### 3. Summary of significant accounting policies

#### Changes in accounting policies

The Bank has consistently applied its accounting policies and has adopted the following amended IFRS and new IFRIC interpretations during the year. The principal effects of these changes are as follows:

##### *IAS 32 Offsetting Financial Assets and Financial Liabilities – Amendments to IAS 32*

These amendments clarify the meaning of “currently has a legally enforceable right to set-off” and the criteria for non-simultaneous settlement mechanisms of clearing houses to qualify for offsetting. These amendments had no impact on the Bank’s financial position.

##### *IFRIC Interpretation 21 Levies (IFRIC 21)*

IFRIC 21 clarifies that an entity recognises a liability for a levy when the activity that triggers payment, as identified by the relevant legislation, occurs. For a levy that is triggered upon reaching a minimum threshold, the interpretation clarifies that no liability should be anticipated before the specified minimum threshold is reached. This IFRIC had no impact on the Bank’s consolidated financial statements as it has applied the recognition principles under IAS 37 *Provisions, Contingent Liabilities and Contingent Assets* consistent with the requirements of IFRIC 21 in prior years.

##### *IAS 39 Novation of Derivatives and Continuation of Hedge Accounting – Amendments to IAS 39*

These amendments provide relief from discontinuing hedge accounting when novation of a derivative designated as a hedging instrument meets certain criteria. This amendment is not relevant to the Bank, since the Bank has not novated its derivatives during the current period.

##### *Recoverable Amount Disclosures for Non-Financial Assets – Amendments to IAS 36*

These amendments remove the unintended consequences of IFRS 13 Fair Value Measurement on the Disclosures required under IAS 36 Impairment of Assets. In addition, these amendments require disclosure of the recoverable amounts for the assets or cash-generating units (CGUs) for which an impairment loss has been recognised or reversed during the period. These amendments had no impact on the Bank’s financial position or performance.

#### Basis of consolidation

Subsidiaries, which are those entities in which the Bank has an interest of more than one half of the voting rights, or otherwise has power to exercise control over their operations, are consolidated. Subsidiaries are consolidated from the date on which control is transferred to the Bank and are no longer consolidated from the date that control ceases. All intra-group transactions, balances and unrealized gains on transactions between group companies are eliminated in full; unrealized losses are also eliminated unless the transaction provides evidence of an impairment of the asset transferred. Where necessary accounting policies for subsidiaries have been changed to ensure consistency with the policies adopted by the Bank.

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

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

(Thousands of Georgian Lari)

### 3. Summary of significant accounting policies (continued)

#### Foreign currency translation

The functional currency of each of the Bank's consolidated entities is the currency of the primary economic environment in which the entity operates. The functional currency of the Bank and its subsidiaries, and the Bank's presentation currency, is Georgian Lari ("GEL").

Monetary assets and liabilities are translated into each entity's functional currency at the official exchange rate of the NBG at the end of the respective reporting period. Foreign exchange gains and losses resulting from the settlement of transactions and from the translation of monetary assets and liabilities into each entity's functional currency at year-end official exchange rates of the NBG are recognised in profit or loss. Translation at year-end rates does not apply to non-monetary items that are measured at historical cost. Non-monetary items measured at fair value in a foreign currency, including equity investments, are translated using the exchange rates at the date when the fair value was determined. Effects of exchange rate changes on non-monetary items measured at fair value in a foreign currency are recorded as part of the fair value gain or loss.

Differences between the contractual exchange rate of a transaction in a foreign currency and the NBG exchange rate on the date of the transaction are included in gains less losses from dealing in foreign currencies.

#### Fair value measurement

The Bank measures financial instruments, such as trading and available-for-sale securities, derivatives and non-financial assets such as investment property, at fair value at each balance sheet date.

Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. The fair value measurement is based on the presumption that the transaction to sell the asset or transfer the liability takes place either:

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

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

The Bank uses valuation techniques that are appropriate in the circumstances and for which sufficient data are available to measure fair value, maximising the use of relevant observable inputs and minimising the use of unobservable inputs.

All assets and liabilities for which fair value is measured or disclosed in the financial statements are categorized within the fair value hierarchy, described as follows, based on the lowest level input that is significant to the fair value measurement as a whole:

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

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

(Thousands of Georgian lari)

### 3. Summary of significant accounting policies (continued)

#### Financial assets

##### *Initial recognition*

Financial assets in the scope of IAS 39 are classified as either financial assets at fair value through profit or loss, loans and receivables, held-to-maturity investments, or available-for-sale financial assets, as appropriate. The Bank determines the classification of its financial assets upon initial recognition, and subsequently can reclassify financial assets in certain cases as described below.

##### *Date of recognition*

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

##### *Held-to-maturity investments*

Non-derivative financial assets with fixed or determinable payments and fixed maturity are classified as held-to-maturity when the Bank has the positive intention and ability to hold them to maturity. Investments intended to be held for an undefined period are not included in this classification. Held-to-maturity investments are subsequently measured at amortised cost. Gains and losses are recognised in profit or loss when the investments are impaired, as well as through the amortisation process.

##### *Loans and receivables*

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. They are not entered into with the intention of immediate or short-term resale and are not classified as trading securities or designated as investment securities available-for-sale. Such assets are carried at amortised cost using the effective interest method. Gains and losses are recognised in profit or loss when the loans and receivables are derecognised or impaired, as well as through the amortisation process.

#### Cash and cash equivalents

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

#### Mandatory reserve deposit with the NBG

Mandatory reserve deposits with the NBG are carried at amortised cost and represent interest bearing mandatory reserve deposits which are not available to finance the Bank's day to day operations and hence are not considered as part of cash and cash equivalents for the purposes of the consolidated statement of cash flows.

#### Borrowings

Borrowings include amounts due to credit institutions, amounts due to customers and subordinated debts. After initial recognition, borrowings are subsequently measured at amortised cost using the effective interest method. Gains and losses are charged to current profit or loss when the borrowings are derecognised as well as through the amortisation process.

#### Leases

##### Operating - Bank as lessee

Leases of assets under which the risks and rewards of ownership are effectively retained by the lessor are classified as operating leases. Lease payments under an operating lease are recognised as expenses on a straight-line basis over the lease term and included into other operating expenses.

(Thousands of Georgian lari)

### 3 Summary of significant accounting policies (continued)

#### Offsetting of financial instruments

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

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

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

#### Impairment of financial assets

The Bank 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

#### *Amounts due from credit institutions and loans to customers*

For amounts due from credit institutions and loans to customers carried at amortised cost. The Bank 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 Bank 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, recognised 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 asset. Loans 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 Bank. 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 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.

(Thousands of Georgian lari)

### 3. Summary of significant accounting policies (continued)

#### Impairment of financial assets (continued)

For the purpose of a collective evaluation of impairment, financial assets are grouped on the basis of the Bank'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.

#### *Held-to-maturity financial investments*

For held-to-maturity investments the Bank assesses individually whether there is objective evidence of impairment. If there is objective evidence that an impairment loss has been incurred, the amount of the loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows. The carrying amount of the asset is reduced and the amount of the loss is recognised in the consolidated statement of profit or loss.

If, in a subsequent year, the amount of the estimated impairment loss decreases because of an event occurring after the impairment was recognised, any amounts formerly charged are credited to current profit or loss.

#### *Renegotiated loans*

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

The accounting treatment of such restructuring is as follows:

- ▶ If the currency of the loan has been changed the old loan is derecognised and the new loan is recognised.
- ▶ If the loan restructuring is not caused by the financial difficulties of the borrower the Bank uses the same approach as for financial liabilities described below.
- ▶ If the loan restructuring is due to the financial difficulties of the borrower and the loan is impaired after restructuring, the Bank recognizes the difference between the present value of the new cash flows discounted using the original effective interest rate and the carrying amount before restructuring in the provision charges for the period. In case loan is not impaired after restructuring the Bank recalculates the effective interest rate.

Once the terms have been renegotiated, the loan is no longer considered past due. Management continuously reviews renegotiated loans to ensure that all criteria are met and that future payments are likely to occur. The loans continue to be subject to an individual or collective impairment assessment, calculated using the loan's original or current effective interest rate.

(Thousands of Georgian lari)

### 3. Summary of significant accounting policies (continued)

#### Derecognition of financial assets and liabilities

##### *Financial assets*

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

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

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

Where continuing involvement takes the form of a written and/or purchased option (including a cash-settled option or similar provision) on the transferred asset, the extent of the Bank's continuing involvement is the amount of the transferred asset that the Bank may repurchase, except that in the case of a written put option (including a cash-settled option or similar provision) on an asset measured at fair value, the extent of the Bank's continuing involvement is limited to the lower of the fair value of the transferred asset and the option exercise price.

##### *Financial liabilities*

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

Where an existing financial liability is replaced by another from the same lender on substantially different terms, or the terms of an existing liability are substantially modified, such an exchange or modification is treated as a derecognition of the original liability and the recognition of a new liability, and the difference in the respective carrying amounts is recognised in profit or loss.

#### Repossessed collateral

Repossessed collateral represents financial and non-financial assets acquired by the Bank in settlement of overdue loans. The assets are initially recognised at cost when acquired and included in premises and equipment, other financial assets or inventories within other assets depending on their nature and the Bank'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.

#### Credit related commitments

The Bank 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 Bank 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.

(Thousands of Georgian lari)

### 3. Summary of significant accounting policies (continued)

#### Taxation

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

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

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

Deferred income tax is provided on temporary differences arising on investments in subsidiaries, associates and joint ventures, except where the timing of the reversal of the temporary difference can be controlled and it is probable that the temporary difference will not reverse in the foreseeable future.

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

#### 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 and construction in progress are 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:

	<i>Average useful life in years</i>
Premises	25
Office and computer equipment	5
Vehicles	5
Furniture, fixtures and other fixed assets	5
Leasehold improvements	5 - 10

The residual value of an asset is the estimated amount that the Bank 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.

(Thousands of Georgian lari)

### 3. Summary of significant accounting policies (continued)

#### 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 on acquisitions of associates is included in the investment in associates. Goodwill is carried at cost less accumulated impairment losses, if any.

The Bank 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 Bank 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

The Bank's intangible assets other than goodwill have definite useful life.

Acquired computer software licences are capitalised on the basis of the costs incurred to acquire and bring them to use. Capitalised computer software is amortised on a straight line basis over expected useful lives of three years.

The value of customer relationship identified as a result of business combination is amortised on a straight line basis over expected customer relationship with duration of ten years.

#### Provisions for liabilities and charges

Provisions for liabilities and charges are non-financial liabilities of uncertain timing or amount. They are accrued when the Bank has a present legal or constructive obligation as a result of past events, it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation, and a reliable estimate of the amount of the obligation can be made.

#### Share capital

##### *Share capital*

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

##### *Dividends*

Dividends are recognised as a liability and deducted from equity at the reporting date only if they are declared before or on the reporting date. Dividends are disclosed when they are proposed before the reporting date or proposed or declared after the reporting date but before the consolidated financial statements are authorised for issue.



(Thousands of Georgian lari)

### 3. Summary of significant accounting policies (continued)

#### Recognition of income and expense

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

Interest income and expense are recorded for all debt instruments on an accrual basis using the effective interest method. This method defers, as part of interest income or expense, all fees paid or received between the parties to the contract that are an integral part of the effective interest rate, transaction costs and all other premiums or discounts.

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

When loans and other debt instruments become doubtful of collection, they are written down to the present value of expected cash inflows and interest income is thereafter recorded for the unwinding of the present value discount based on the asset's effective interest rate which was used to measure the impairment loss.

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

#### Standards and interpretations issued but not yet effective

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

##### *IFRS 9 Financial Instruments*

In July 2014, the IASB issued the final version of IFRS 9 Financial Instruments which reflects all phases of the financial instruments project and replaces IAS 39 *Financial Instruments: Recognition and Measurement* and all previous versions of IFRS 9. The standard introduces new requirements for classification and measurement, impairment, and hedge accounting. IFRS 9 is effective for annual periods beginning on or after 1 January 2018, with early application permitted. Retrospective application is required, but comparative information is not compulsory. Early application of previous versions of IFRS 9 (2009, 2010 and 2013) is permitted if the date of initial application is before 1 February 2015. The adoption of IFRS 9 will have an effect on the classification and measurement of the Bank's financial assets, but no impact on the classification and measurement of the Bank's financial liabilities.

##### *IFRS 15 Revenue from Contracts with Customers*

IFRS 15 was issued in May 2014 and establishes a new five-step model that will apply to revenue arising from contracts with customers. Revenue arising from lease contracts within the scope of IAS 17 *Leases*, insurance contracts within the scope of IFRS 4 *Insurance Contracts* and financial instruments and other contractual rights and obligations within the scope of IAS 39 *Financial Instruments: Recognition and Measurement* (or IFRS 9 *Financial Instruments*, if early adopted) is out of IFRS 15 scope and is dealt by respective standards.

Under IFRS 15 revenue is recognised at an amount that reflects the consideration to which an entity expects to be entitled in exchange for transferring goods or services to a customer. The principles in IFRS 15 provide a more structured approach to measuring and recognising revenue.

The new revenue standard is applicable to all entities and will supersede all current revenue recognition requirements under IFRS. Either a full or modified retrospective application is required for annual periods beginning on or after 1 January 2017 with early adoption permitted. The Bank is currently assessing the impact of IFRS 15 and plans to adopt the new standard on the required effective date.

(Thousands of Georgian lari)

### 3. Summary of significant accounting policies (continued)

#### Standards and interpretations issued but not yet effective (continued)

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

The amendments clarify the principle in IAS 16 and IAS 38 that revenue reflects a pattern of economic benefits that are generated from operating a business (of which the asset is part) rather than the economic benefits that are consumed through use of the asset. As a result, a revenue-based method cannot be used to depreciate property, plant and equipment and may only be used in very limited circumstances to amortise intangible assets. The amendments are effective prospectively for annual periods beginning on or after 1 January 2016, with early adoption permitted. These amendments are not expected to have any impact to the Bank given that the Bank has not used a revenue-based method to depreciate its non-current assets.

##### *IFRS 13 Short-term Receivables and Payables – Amendments to IFRS 13*

This amendment to IFRS 13 clarifies in the Basis for Conclusions that short-term receivables and payables with no stated interest rates can be measured at invoice amounts when the effect of discounting is immaterial.

##### *IAS 16 Property, Plant and Equipment and IAS 38 Intangible Assets*

The amendment is applied retrospectively and clarifies in IAS 16 and IAS 38 that the asset may be revalued by reference to observable data on either the gross or the net carrying amount. In addition, the accumulated depreciation or amortisation is the difference between the gross and carrying amounts of the asset.

##### *IAS 24 Related Party Disclosures*

The amendment is applied retrospectively and clarifies that a management entity (an entity that provides key management personnel services) is a related party subject to the related party disclosures. In addition, an entity that uses a management entity is required to disclose the expenses incurred for management services.

##### *IFRS 13 Fair Value Measurement*

The amendment is applied prospectively and clarifies that the portfolio exception in IFRS 13 can be applied not only to financial assets and financial liabilities, but also to other contracts within the scope of IFRS 9 (or IAS 39, as applicable).

### 4. Significant accounting judgments and estimates

The Bank makes estimates and assumptions that affect the amounts recognised in the consolidated financial statements and the carrying amounts of assets and liabilities within the next financial year. Estimates and judgements are continually evaluated and are based on management's experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances. Management also makes certain judgements, apart from those involving estimations, in the process of applying the accounting policies. Judgements that have the most significant effect on the amounts recognised in the consolidated financial statements and estimates that can cause a significant adjustment to the carrying amount of assets and liabilities within the next financial year include:

#### *Allowance for loan impairment*

The Bank regularly reviews its loans and receivables to assess impairment. As at 31 December 2014, GEL 302,015 of gross loan portfolio was assessed on collective basis and GEL 4,119 amount of loan loss allowance was created against it, which represents 1.36% of assessed loss rate on the loan portfolio assessed collectively (Note 6). Management uses estimates based on historical loss experience of past 5 years for assets with credit risk characteristics and objective evidence of impairment similar to those in the group of loans and receivables. Actual losses on the portfolio of loans assessed collectively can be significantly different from the allowance amount created as at 31 December 2014.

(Thousands of Georgian lari)

#### 4. Significant accounting judgments and estimates (continued)

##### *Allowance for loan impairment (continued)*

Determination of loss event has significant impact on assessment of loan loss allowance. The Bank annually assesses its determination of loss event and makes changes when necessary to reflect the actual behaviour of the borrowers that ultimately result in losses for the Bank. The Bank's current policy relies primarily on borrowers' debt service for determination of loss event. For loans to customers for which the Bank assessed that loss event exists as at 31 December 2014 the Bank makes individual assessment of the loan loss allowance as a difference between the carrying amount of the loan and the present value of estimated future cash flows. For such loans the Bank uses assumption that the future cash flow is the value of the collateral pledged. Management monitors market value of collateral on a regular basis. Management uses its experienced judgment or independent opinion to adjust the fair value to reflect current circumstances. As at 31 December 2014, GEL 22,563 (2013: GEL 14,885) of gross loan portfolio was determined to be individually impaired and an allowance of GEL 11,603 (2013: GEL 6,928) was created (Note 6).

##### *Deferred tax assets*

Deferred tax assets are recognised in respect of tax losses to the extent that it is probable that taxable profit will be available against which the losses can be utilised. Judgment is required to determine the amount of deferred tax assets that can be recognised, based upon the likely timing and level of future taxable profits, together with future tax planning strategies.

##### *Goodwill impairment and determination of the cash generating unit ("CGU")*

Goodwill reported in the statement of financial position 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. As required by IFRS the Bank tests goodwill for impairment at annually, at each reporting date. Testing of goodwill for impairment requires management to make significant judgments and estimates.

Management believes that the Bank consists of single CGU and therefore allocates existing goodwill entirely to the Bank's operations while testing it for an impairment. Management believes that its judgment is appropriate since JSC Kor had no material operations of its own prior to business combination and the Bank has not added any separate lines of business after business combination which could constitute a separate CGU.

Significant estimates made during impairment test of goodwill and the sensitivities of reported figures to those estimates are disclosed in Note 9.

#### 5. Cash and cash equivalents

Cash and cash equivalents comprise:

	<u>2014</u>	<u>2013</u>
Cash on hand	23,242	19,985
Cash balances with the NBS (other than mandatory reserve deposit)	37,752	12,197
Correspondent accounts and overnight placements with other banks	5,870	14,985
Time deposits with credit institutions up to 90 days from origination date	5,001	–
<b>Total cash and cash equivalents</b>	<b><u>71,865</u></b>	<b><u>47,167</u></b>

As at 31 December 2014, GEL 5,257 (2013: GEL 13,692) was placed on current and time deposit accounts with internationally recognized OECD banks that are the counterparties of the Bank in performing international settlements.

*(Thousands of Georgian lari)***6. Loans to customers**

Loans to customers comprise:

	<u>2014</u>	<u>2013</u>
Gold pawn loans	148,871	108,582
Corporate loans	74,482	73,151
Consumer loans	64,428	44,353
Mortgage loans	19,770	19,458
Loans to individual entrepreneurs	17,027	16,400
<b>Gross loans to customers</b>	<b>324,578</b>	<b>261,944</b>
Less: allowance for impairment	(15,722)	(9,056)
<b>Loans to customers</b>	<b>308,856</b>	<b>252,888</b>

**Allowance for impairment of loans to customers**

A reconciliation of the allowance for impairment of loans to customers by class is as follows:

	<i>Corporate loans 2014</i>	<i>Consumer loans 2014</i>	<i>Individual entrepreneurs 2014</i>	<i>Mortgage loans 2014</i>	<i>Total 2014</i>
At 1 January 2014	4,081	3,378	900	697	9,056
Charge for the year	3,209	1,873	2,335	438	7,855
Recoveries	3	116	31	-	150
Amounts written off	(48)	(1,057)	(229)	(5)	(1,339)
<b>At 31 December 2014</b>	<b>7,245</b>	<b>4,310</b>	<b>3,037</b>	<b>1,130</b>	<b>15,722</b>
Individual impairment	5,813	3,067	2,149	574	11,603
Collective impairment	1,432	1,243	888	556	4,119
	<b>7,245</b>	<b>4,310</b>	<b>3,037</b>	<b>1,130</b>	<b>15,722</b>
Gross amount of loans, individually determined to be impaired, before deducting any individually assessed impairment allowance	<b>14,281</b>	<b>3,462</b>	<b>3,291</b>	<b>1,529</b>	<b>22,563</b>

*(Thousands of Georgian lari)***6. Loans to customers (continued)**

	<i>Corporate loans 2013</i>	<i>Consumer loans 2013</i>	<i>Individual entrepreneurs 2013</i>	<i>Mortgage loans 2013</i>	<i>Total 2013</i>
At 1 January 2013	5,812	4,717	1,210	864	12,603
(Reversal) for the year	(152)	(1,359)	(216)	(166)	(1,893)
Recoveries	117	37	–	–	154
Amounts written off	(1,696)	(17)	(94)	(1)	(1,808)
<b>At 31 December 2013</b>	<b>4,081</b>	<b>3,378</b>	<b>900</b>	<b>697</b>	<b>9,056</b>
Individual impairment	3,144	2,856	514	414	6,928
Collective impairment	937	522	386	283	2,128
	<b>4,081</b>	<b>3,378</b>	<b>900</b>	<b>697</b>	<b>9,056</b>
Gross amount of loans, individually determined to be impaired, before deducting any individually assessed impairment allowance	<b>9,278</b>	<b>3,176</b>	<b>1,037</b>	<b>1,394</b>	<b>14,885</b>

Impairment rate applicable to Gold Pawn loans is 0%. This is due to the fact that the Bank has not incurred any losses for such loans.

**Collateral and other credit enhancements**

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

The main types of collateral obtained are as follows:

- ▶ For gold pawn lending, gold and other precious metals and jewelry,
- ▶ For commercial lending, charges over real estate properties, inventory and trade receivables,
- ▶ For retail lending, mortgages over residential properties.

The Bank also obtains guarantees from parent companies for loans to their subsidiaries.

Management monitors the market value of collateral, requests additional collateral in accordance with the underlying agreement, and monitors the market value of collateral obtained during its review of the adequacy of the allowance for loan impairment.

(Thousands of Georgian lari)

**6. Loans to customers (continued)****Concentration of loans to customers**

As at 31 December 2014, the Bank had a concentration of loans represented by GEL 90,736 due from the ten largest third party borrowers (27.95% of gross loan portfolio) (2013: GEL 84,583 or 32.29%). An allowance of GEL 1,187 (2013: GEL 549) was recognised against these loans.

Loans have been extended to the following types of customers:

	<u>2014</u>	<u>2013</u>
Private companies	217,568	182,294
Individuals	107,010	79,650
	<u>324,578</u>	<u>261,944</u>

Loans are to borrowers within Georgia in the following industry sectors:

	<u>2014</u>		<u>2013</u>	
	<i>Amount</i>	<i>%</i>	<i>Amount</i>	<i>%</i>
Gold pawn loans	139,005	42.83	108,582	41.45
Individuals	107,010	32.97	79,650	30.41
Trading and service sector	39,935	12.30	34,940	13.34
Agriculture and food processing	17,338	5.34	24,170	9.23
Construction sector	16,465	5.07	11,600	4.43
Energy sector	1,429	0.44	827	0.32
Other sector	3,396	1.05	2,175	0.82
	<u>324,578</u>	<u>100.00</u>	<u>261,944</u>	<u>100.00</u>

**7. Investment securities held to maturity**

Held-to-maturity securities comprise:

	<u>2014</u>	<u>2013</u>
Treasury bonds of the Ministry of Finance	35,341	22,715
Treasury bills of the Ministry of Finance	6,945	3,039
Deposit certificates of the NBG	3,894	14,437
<b>Held-to-maturity securities</b>	<u>46,180</u>	<u>40,191</u>

All securities are denominated in GEL and their contractual interest rates and maturities are as follows:

	<u>31 December 2014</u>		<u>31 December 2013</u>	
	<i>Average %</i>	<i>Maturity</i>	<i>Average %</i>	<i>Maturity</i>
Deposit certificates of the NBG	4.24	2015	4.01	2014
Treasury bills of the Ministry of Finance	6.32	2015	4.84	2014
Treasury bonds of the Ministry of Finance	6.96	2015-2019	6.52	2014-2018

(Thousands of Georgian lari)

**8. Premises and equipment**

The movements in premises and equipment were as follows:

	<i>Land</i>	<i>Premises</i>	<i>Office and computer equipment</i>	<i>Vehicles</i>	<i>Furniture, fixtures and other fixed assets</i>	<i>Leasehold improve- ments</i>	<i>Total</i>
<b>Cost 31 December 2013</b>	<b>32</b>	<b>11,862</b>	<b>3,476</b>	<b>720</b>	<b>5,580</b>	<b>3,799</b>	<b>25,469</b>
Additions	–	25	97	–	532	105	759
Disposals	–	(18)	(1)	(34)	–	(1,159)	(1,212)
Transfers	–	495	–	–	(593)	98	–
<b>31 December 2014</b>	<b>32</b>	<b>12,364</b>	<b>3,572</b>	<b>686</b>	<b>5,519</b>	<b>2,843</b>	<b>25,016</b>
<b>Accumulated depreciation</b>							
<b>31 December 2013</b>	–	1,536	2,693	459	4,433	2,653	11,774
Depreciation charge	–	497	250	73	382	327	1,529
Disposals	–	(3)	(1)	(7)	–	(916)	(927)
<b>31 December 2014</b>	–	<b>2,030</b>	<b>2,942</b>	<b>525</b>	<b>4,815</b>	<b>2,064</b>	<b>12,376</b>
<b>Net book value:</b>							
<b>31 December 2013</b>	<b>32</b>	<b>10,326</b>	<b>783</b>	<b>261</b>	<b>1,147</b>	<b>1,146</b>	<b>13,695</b>
<b>31 December 2014</b>	<b>32</b>	<b>10,334</b>	<b>630</b>	<b>161</b>	<b>704</b>	<b>779</b>	<b>12,640</b>

	<i>Land</i>	<i>Premises</i>	<i>Office and computer equipment</i>	<i>Vehicles</i>	<i>Furniture, fixtures and other fixed assets</i>	<i>Leasehold improve- ments</i>	<i>Total</i>
<b>Cost 31 December 2012</b>	<b>32</b>	<b>8,498</b>	<b>2,876</b>	<b>711</b>	<b>5,288</b>	<b>3,867</b>	<b>21,272</b>
Additions	–	–	600	196	654	31	1,481
Disposals	–	–	–	(187)	(9)	(452)	(648)
Transfers	–	–	–	–	(353)	353	–
Reclassification from investment property	–	3,364	–	–	–	–	3,364
<b>31 December 2013</b>	<b>32</b>	<b>11,862</b>	<b>3,476</b>	<b>720</b>	<b>5,580</b>	<b>3,799</b>	<b>25,469</b>
<b>Accumulated depreciation</b>							
<b>31 December 2012</b>	–	1,181	2,462	375	4,043	2,695	10,756
Depreciation charge	–	355	231	109	398	333	1,426
Disposals	–	–	–	(25)	(8)	(375)	(408)
<b>31 December 2013</b>	–	<b>1,536</b>	<b>2,693</b>	<b>459</b>	<b>4,433</b>	<b>2,653</b>	<b>11,774</b>
<b>Net book value:</b>							
<b>31 December 2012</b>	<b>32</b>	<b>7,317</b>	<b>414</b>	<b>336</b>	<b>1,245</b>	<b>1,172</b>	<b>10,516</b>
<b>31 December 2013</b>	<b>32</b>	<b>10,326</b>	<b>783</b>	<b>261</b>	<b>1,147</b>	<b>1,146</b>	<b>13,695</b>

Gross carrying value of premises and equipment fully depreciated as at 31 December 2014 but still in use was GEL 7,396 (2013: GEL 7,206).

(Thousands of Georgian lari)

**9. Goodwill***Impairment testing of goodwill*

As discussed in Note 4 management believes that entire Bank represents a single CGU, acquired in a business combination in 2008.

The recoverable amount of CGU was determined based on value-in-use calculations. These calculations use cash flow projections based on one year financial budgets approved by management and are adjusted for uncertainties taken into account during the budgeting process. The same cash flow is also used as a terminal amount and disclosed as a perpetuity applying a terminal growth rate of 5%, equal to long-term GDP growth rate forecast for Georgia.

The discount rates used are pre-tax and reflect specific risks relating to the CGU. The discount rate used as at 31 December 2014 is 7.1% p.a. (2013: 8.2%).

As at 31 December 2014, discount rate at which recoverable amount of the CGU equals the carrying value of the goodwill is 7.4% (2013: 9.3%).

**10. Other intangible assets**

The movements in other intangible assets were as follows:

	<i>Customer Relationships</i>	<i>Computer software licenses</i>	<i>Total</i>
<b>Cost</b>			
31 December 2013	13,657	2,396	16,053
Additions	–	716	716
31 December 2014	13,657	3,112	16,769
<b>Accumulated amortization</b>			
31 December 2013	7,954	1,637	9,591
Amortisation charge	1,366	270	1,636
31 December 2014	9,320	1,907	11,227
<b>Net book value</b>			
31 December 2013	5,703	759	6,462
31 December 2014	4,337	1,205	5,542
	<i>Customer Relationships</i>	<i>Computer software licenses</i>	<i>Total</i>
<b>Cost</b>			
31 December 2012	13,657	1,573	15,230
Additions	–	823	823
31 December 2013	13,657	2,396	16,053
<b>Accumulated amortization</b>			
31 December 2012	6,589	1,357	7,946
Amortisation charge	1,365	280	1,645
31 December 2013	7,954	1,637	9,591
<b>Net book value</b>			
31 December 2012	7,068	216	7,284
31 December 2013	5,703	759	6,462

Gross carrying value of intangible assets fully amortised as at 31 December 2014 but still in use was GEL 1,530 (2013: GEL 1,479).



(Thousands of Georgian lari)

**11. Taxation**

The corporate income tax expense comprises:

	<u>2014</u>	<u>2013</u>
Current tax charge	–	–
Deferred tax charge— origination and reversal of temporary differences	(805)	(966)
<b>Income tax charge</b>	<b>(805)</b>	<b>(966)</b>

The income tax rate applicable to the Bank's 2014 income is 15% (2013: 15%).

The effective income tax rate differs from the statutory income tax rates. A reconciliation of the income tax expense based on statutory rates with actual is as follows:

	<u>2014</u>	<u>2013</u>
<b>Profit before income tax</b>	<b>1,227</b>	<b>8,341</b>
Statutory tax rate	15%	15%
<b>Theoretical income tax expense at the statutory rate</b>	<b>(184)</b>	<b>(1,251)</b>
Tax effect of items which are not deductible for taxation purposes:		
Leasehold improvements and applicable VAT	(41)	(12)
Other	(6)	–
Expired tax losses carried forward	(1,225)	(616)
Change in unrecognized deferred tax assets	104	542
Tax exempt income:		
Interest income from HTM securities	423	235
Interest income from deposits in resident banks	42	31
Other	82	105
<b>Income tax charge</b>	<b>(805)</b>	<b>(966)</b>

Deferred tax assets and liabilities as of 31 December and their movements for the respective years comprise:

	<u>2012</u>	<u>In the income statement</u>	<u>2013</u>	<u>In the income statement</u>	<u>2014</u>
<b>Tax effect of taxable temporary differences:</b>					
Tax losses carried forward	2,632	(1,379)	1,253	385	1,638
Other financial liabilities	–	51	51	(9)	42
Other assets	(116)	148	32	75	107
Investment property	138	(138)	–	–	–
<b>Gross deferred tax assets</b>	<b>2,654</b>	<b>(1,318)</b>	<b>1,336</b>	<b>451</b>	<b>1,787</b>
<b>Unrecognised deferred tax assets</b>	<b>(646)</b>	<b>542</b>	<b>(104)</b>	<b>104</b>	<b>–</b>
<b>Gross deferred tax assets</b>	<b>2,008</b>	<b>(776)</b>	<b>1,232</b>	<b>555</b>	<b>1,787</b>
<b>Tax effect of deductible temporary differences:</b>					
Intangible assets, including goodwill	(1,394)	(184)	(1,578)	(138)	(1,716)
Loans to customers	(159)	(145)	(304)	(1,197)	(1,501)
Premises and equipment	(43)	34	(9)	33	24
Amounts due to customers	–	–	–	(1)	(1)
Other financial assets	(4)	58	54	(57)	(3)
Other liabilities	(47)	47	–	–	–
<b>Gross deferred tax liabilities</b>	<b>(1,647)</b>	<b>(190)</b>	<b>(1,837)</b>	<b>(1,360)</b>	<b>(3,197)</b>
<b>Net deferred tax assets/ (liabilities)</b>	<b>361</b>	<b>(966)</b>	<b>(605)</b>	<b>(805)</b>	<b>(1,410)</b>

In accordance with Georgian tax legislation current income tax losses may be carried forward for up to 5 years. As of 31 December 2014 tax loss carry forward amounting GEL 189 and GEL 10,734 will expire on 31 December 2015 and 31 December 2019, respectively.

(Thousands of Georgian lari)

**12. Other financial assets and liabilities**

Other financial assets comprise:

	<u>2014</u>	<u>2013</u>
Restricted cash	426	182
Financial assets from services rendered	318	6,222
Settlements on money transfer operations	140	70
Interest accrued on guarantees and letters of credit	45	95
Other accrued assets	64	147
<b>Other financial assets</b>	<b>993</b>	<b>6,716</b>

Restricted cash in amount of GEL 335 (2013: GEL182) represents balances on correspondent accounts with Georgian banks placed by the Bank as guarantees for transactions performed by the Bank's customers and processed by respective counterparty banks. Restricted cash in amount of GEL 91 (2013: nil) represents cash placed in foreign bank under a guarantee agreement with a single customer.

Other financial liabilities comprise:

	<u>2014</u>	<u>2013</u>
Swap agreements	3,976	1,486
Debit or credit card payables	565	593
Financial liabilities from services received	274	285
Liabilities for payments to utility companies	33	31
Settlements on money transfer operations	5	52
Other accrued liabilities	389	390
<b>Other financial liabilities</b>	<b>5,242</b>	<b>2,837</b>

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.

	<u>2014</u>		<u>2013</u>	
	<i>Notional Amount</i>	<i>Fair value Liabilities</i>	<i>Notional Amount</i>	<i>Fair value Liabilities</i>
<b>Foreign exchange contracts</b>				
Swaps – domestic	64,430	<u>3,976</u>	54,619	<u>1,486</u>
Total derivative liabilities		<u>3,976</u>		<u>1,486</u>

(Thousands of Georgian lari)

**13. Other assets and liabilities**

Other assets comprise:

	2014	2013
Repossessed collateral	4,636	4,092
Other tax prepayments	401	520
Prepayments for services	231	115
Prepayments for repossessed collateral and property & equipment	97	1,011
Other	17	27
<b>Other assets</b>	<b>5,382</b>	<b>5,765</b>

Repossessed collateral represents real estate assets acquired by the Bank in settlement of overdue loans. The Bank expects to dispose the assets in the foreseeable future. However, the assets do not meet the definition of non-current assets held for sale and are classified as inventories in accordance with IAS 2, *Inventories*. These assets were initially recognized at cost when acquired and subsequently measured at amount lower of cost and net realizable value.

Other liabilities comprise:

	2014	2013
Advances received from buyers of repossessed collateral	78	68
Taxes payable	14	12
<b>Other liabilities</b>	<b>92</b>	<b>80</b>

**14. Amounts due to credit institutions**

Amounts due to credit institutions comprise:

	2014	2013
Loans from financial organisations	33,388	6,033
Time deposits from credit institutions	2,000	14,552
Short-term placements of other banks	–	98
	<b>35,388</b>	<b>20,683</b>

Included in loans from financial organisations is GEL 30,003 loan from the NBG which was initiated on 31 December 2014, was bearing 4.2% annual interest rate and matured on 8 January 2015. The loan is denominated in GEL.

The Bank has credit facility equivalent of USD 5,000 thousand (equivalent of GEL 9,318) from the Black Sea Trade and Development Bank (BSTDB). As of 31 December 2014 the Bank has utilized equivalent of GEL 3,286 (2013: GEL 5,817) bearing average interest rate of 7.08% p.a (2013: 7.17% p.a.) out of available GEL 9,318 (2013: GEL 8,682). Loans from the BSTDB are denominated in USD and mature in 2015.

As at 31 December 2014, time deposits from credit institutions represent a single short-term deposits received from Georgian bank, denominated in GEL and bearing 4% interest rate p.a. As at 31 December 2013, the Bank had equivalent of GEL 1,736 as USD denominated deposit from one Georgian bank with contractual maturity of 6 months bearing interest rate of 4.25% p.a. and GEL 12,816 as deposits in USD and EUR from one foreign bank with contractual maturity of 9 months bearing average interest rate of 8% p.a.

The Bank recognised total of GEL 2,476 interest expense on amounts due to credit institutions in 2014 (2013 – GEL 2,350)

*(Thousands of Georgian lari)***15. Amounts due to customers**

Amounts due to customers comprise:

	<u>2014</u>	<u>2013</u>
Current accounts	158,283	163,603
Time deposits	181,686	132,875
<b>Amounts due to customers</b>	<b>339,969</b>	<b>296,478</b>
<b>Held as security against guarantees and letters of credit issued</b>	<b>13,341</b>	<b>21,273</b>

At 31 December 2014, amounts due to customers of GEL 178,745 (52.6%) were due to the ten largest customers (2013: GEL 151,874 (51.2%)).

Amounts due to customers comprise the following types of customers:

	<u>2014</u>	<u>2013</u>
Private enterprises	206,767	127,700
Individuals	93,838	120,454
State and budgetary organisations	39,364	48,324
<b>Customer accounts</b>	<b>339,969</b>	<b>296,478</b>

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

	<u>2014</u>		<u>2013</u>	
	Amount	%	Amount	%
Individuals	93,838	27.58	120,454	40.63
Energy	53,535	15.75	51,858	17.49
Not-for-profit organizations	43,550	12.81	51,720	17.44
Construction	39,319	11.57	7,166	2.42
Transport and communication	38,224	11.24	15,565	5.25
Trade and service	36,649	10.80	39,076	13.18
Other	34,854	10.25	10,639	3.59
<b>Amounts due to customers</b>	<b>339,969</b>	<b>100.00</b>	<b>296,478</b>	<b>100.00</b>

*(Thousands of Georgian lari)***16. Subordinated debts**

Subordinated debts comprise:

	<u>2014</u>	<u>2013</u>
Standard Capital Georgia Ltd (US dollar denominated, granted 29 September 2005; 10 equal annual payments of principal starting from 2016 and monthly payment of interest, with annual interest rate of 11%, maturing 29 September 2025)	5,620	5,234
Standard Capital Georgia Ltd (US dollar denominated, granted 15 December 2006; 10 equal annual payments of principal starting from 2017 and monthly payment of interest, with annual interest rate of 11%, maturing 15 December 2026)	3,761	3,503
Al Dhabi Contracting LLC (US dollar denominated, granted 31 December 2014 with annual interest rate of 6%, maturing 31 December 2020)	18,639	–
<b>Subordinated debts</b>	<b><u>28,020</u></b>	<b><u>8,737</u></b>

The debts rank after all other creditors in case of liquidation.

**17. Equity**

As of 31 December 2014, authorized, issued and fully paid share capital comprised of 995,159 ordinary shares (2013: 995,159). Each ordinary share has a nominal value of GEL 0.1 (2013: GEL 0.1). Each ordinary share carries one vote.

In accordance with Georgian legislation, dividends may only be declared to the Shareholders of the Bank from the net income as shown in the Bank's financial statements prepared in accordance with the NBG requirements. The NBG shall be informed regarding declaration of dividends. The NBG has right to suspend or restrict payment of dividends, if a commercial bank has violated regulatory requirements of the NBG.

No dividends were declared or paid in 2014 or 2013.

**18. Commitments and contingencies****Financial commitments and contingencies**

As of 31 December the Bank's commitments and contingencies comprised the following:

	<u>2014</u>	<u>2013</u>
<b>Credit related commitments</b>		
Guarantees	18,853	1,739
Letters of credit	1,321	19,747
	<u>20,174</u>	<u>21,486</u>
Less – Cash held as security against guarantees and letters of credit	(13,341)	(21,273)
<b>Net exposure to guarantees and letters of credit</b>	<b><u>6,833</u></b>	<b><u>213</u></b>
<b>Undrawn loan commitments</b>	<b>13,153</b>	<b>18,866</b>
<b>Operating lease commitments</b>		
Not later than 1 year	1,752	1,758
Later than 1 year but not later than 5 years	4,027	3,963
Later than 5 years	950	1,233
	<u>6,729</u>	<u>6,954</u>
<b>Capital expenditure commitments</b>	<b><u>662</u></b>	<b><u>1,267</u></b>

*(Thousands of Georgian lari)***19. Interest income and expense**

Interest income and expense comprises:

	<u>2014</u>	<u>2013</u>
Loans to customers	40,521	38,079
Amounts due from other banks and mandatory reserve with the NBG	3,700	2,870
Investment securities held to maturity	2,818	1,565
<b>Total interest income</b>	<b>47,039</b>	<b>42,514</b>
Amounts due to customers	19,748	18,258
Amounts due to credit institutions	2,476	2,350
Subordinated debts	971	915
<b>Total interest expense</b>	<b>23,195</b>	<b>21,523</b>
<b>Net interest income</b>	<b>23,844</b>	<b>21,228</b>

**20. Fee and commission income and expenses**

Fee and commission income comprises:

	<u>2014</u>	<u>2013</u>
Plastic card transactions	1,491	2,085
Settlement transactions	943	1,116
Cash transactions	689	1,561
Servicing of current accounts	476	350
Guarantees and letters of credit issued	305	318
Other	52	21
<b>Fee and commission income</b>	<b>3,956</b>	<b>5,451</b>

Fee and commission expense comprises:

	<u>2014</u>	<u>2013</u>
Plastic card transactions	975	1,136
Settlement transactions	264	696
Cash transactions	56	94
Currency conversion operations	-	35
Other	1,239	1,128
<b>Fee and commission expense</b>	<b>2,534</b>	<b>3,089</b>
<b>Net fee and commission income</b>	<b>1,422</b>	<b>2,362</b>

(Thousands of Georgian lari)

**21. Administrative and other operating expenses**

	<u>2014</u>	<u>2013</u>
Operating lease expense for premises and equipment	2,050	2,609
Losses from disposal of repossessed collateral	744	274
Building security expense	419	450
Repair and maintenance	414	323
Representative expenses	329	270
Office supply	318	296
Loss on disposal of property and equipment	243	10
Professional services	238	151
Advertising and marketing services	236	245
Taxes other than on income	228	285
Transportation and cash collection	226	310
Vehicle expenses	150	149
Insurance	93	117
Loss on recognition of financial assets from services rendered	–	358
Other expenses	429	435
<b>Administrative and other operating expenses</b>	<b><u>6,117</u></b>	<b><u>6,282</u></b>

**22. Risk management**

The risk management function within the Bank is carried out in respect of financial risks, operational risks and legal risks. Financial risk comprises market risk (including currency risk and interest rate risk), credit risk and liquidity risk. The primary objectives of the financial risk management function are to establish risk limits, and then ensure that exposure to risks stays within these limits. The operational and legal risk management functions are intended to ensure proper functioning of internal policies and procedures to minimize operational and legal risks.

**Credit risk**

The Bank 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 as a result of the Bank's lending and other transactions with counterparties giving rise to financial assets.

The Bank 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 Bank 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 sanctioned retail loans (payroll/credit card/overdraft) below GEL 10 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. Exposure to credit risk is also managed, in part, by obtaining collateral and corporate and personal guarantees.

(Thousands of Georgian lari)

**22. Risk management (continued)****Credit risk (continued)**

In order to monitor credit risk exposures, regular reports are produced by the corporate credit expert and reviewed by the credit risk department. Monitoring includes review of the customer's financial performance. Any significant exposures against customers with overdue days more than 90 days are reported to and reviewed by the Management Board. The financial assets of the Bank can be analysed as follows:

	Notes	<i>Neither past due nor impaired</i>				Total 2014
		<i>High grade 2014</i>	<i>Standard grade 2014</i>	<i>Sub-standard grade 2014</i>	<i>Past due but not impaired 2014</i>	
Cash and cash equivalents (except cash on hand)		48,623	–	–	–	48,623
Mandatory reserve deposit with the NBG		31,222	–	–	–	31,222
Loans to customers	6					
Corporate lending		2,964	37,317	7,589	12,331	74,482
Gold pawn loans		148,420	–	–	451	148,871
Consumer lending		5,890	8,104	45,741	1,231	64,428
Mortgage loans		–	15,558	260	2,423	19,770
Individual entrepreneurs		–	11,592	948	1,196	17,027
		<b>157,274</b>	<b>72,571</b>	<b>54,538</b>	<b>17,632</b>	<b>324,578</b>
Investment securities held to maturity	7	46,180	–	–	–	46,180
Other financial assets	12	675	–	–	318	993
		<b>46,855</b>	<b>–</b>	<b>–</b>	<b>318</b>	<b>47,173</b>
<b>Total</b>		<b>283,974</b>	<b>72,571</b>	<b>54,538</b>	<b>17,950</b>	<b>451,596</b>

	Notes	<i>Neither past due nor impaired</i>				Total 2013
		<i>High grade 2013</i>	<i>Standard grade 2013</i>	<i>Sub-standard grade 2013</i>	<i>Past due but not impaired 2013</i>	
Cash and cash equivalents (except cash on hand)		27,182	–	–	–	27,182
Mandatory reserve deposit with the NBG		28,673	–	–	–	28,673
Loans to customers	6					
Corporate lending		2,610	49,461	3,411	8,391	73,151
Gold pawn loans		108,582	–	–	–	108,582
Consumer lending		4,122	6,087	29,303	1,665	44,353
Mortgage loans		–	15,953	133	1,978	19,458
Individual entrepreneurs		–	11,094	3,481	788	16,400
		<b>115,314</b>	<b>82,595</b>	<b>36,328</b>	<b>12,822</b>	<b>261,944</b>
Investment securities held to maturity	7	40,191	–	–	–	40,191
Other financial assets	12	494	–	–	6,222	6,716
		<b>40,685</b>	<b>–</b>	<b>–</b>	<b>6,222</b>	<b>46,907</b>
<b>Total</b>		<b>211,854</b>	<b>82,595</b>	<b>36,328</b>	<b>19,044</b>	<b>364,706</b>



*(Thousands of Georgian lari)***22. Risk management (continued)****Credit risk (continued)**

An analysis of past due loans, by age, 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 Bank are classified as follows:

- ▶ A financial asset with no overdue days secured by deposit or precious metals is assessed as a financial asset with High Grade; The Bank treats mandatory reserve deposit amount with the NBG, together with Ministry of Finance treasury bills and bonds and deposit certificated of the NBG as High Grade financial assets;
- ▶ A financial asset with no overdue days secured by real estate is assessed as a financial asset with Standard Grade;
- ▶ A financial asset with no overdue days secured by other collateral is assessed as a financial asset with Substandard Grade.

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

	<i>Less than 30 days 2014</i>	<i>31 to 60 days 2014</i>	<i>61 to 90 days 2014</i>	<i>More than 90 days 2014</i>	<i>Total 2014</i>
<b>Loans to customers</b>					
Corporate lending	12,063	–	7	261	12,331
Consumer lending	916	54	118	143	1,231
Residential mortgages	1,402	132	–	889	2,423
Gold pawn loans	451	–	–	–	451
Individual entrepreneurs	601	88	89	418	1,196
<b>Total</b>	<b>15,433</b>	<b>274</b>	<b>214</b>	<b>1,711</b>	<b>17,632</b>

	<i>Less than 30 days 2013</i>	<i>31 to 60 days 2013</i>	<i>61 to 90 days 2013</i>	<i>More than 90 days 2013</i>	<i>Total 2013</i>
<b>Loans to customers</b>					
Corporate lending	2,269	–	5,890	232	8,391
Consumer lending	1,365	35	25	240	1,665
Residential mortgages	843	394	25	716	1,978
Individual entrepreneurs	339	21	–	428	788
<b>Total</b>	<b>4,816</b>	<b>450</b>	<b>5,940</b>	<b>1,616</b>	<b>12,822</b>

See Note 6 for more detailed information with respect to the allowance for impairment of loans to customers. 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 Bank 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.

(Thousands of Georgian lari)

**22 Risk management (continued)****Credit risk (continued)***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 Bank addresses impairment assessment in two areas: individually assessed allowances and collectively assessed allowances.

*Individually assessed allowances*

The Bank determines the allowances appropriate for each individually significant loan on an individual basis. Realisable value of collateral 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 (including credit cards, residential mortgages and unsecured consumer lending) 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 Bank's monetary assets and liabilities is set out below:

	2014				2013			
	Georgia	OECD	CIS and other foreign countries	Total	Georgia	OECD	CIS and other foreign countries	Total
<b>Assets:</b>								
Cash and cash equivalents	66,176	5,257	432	71,865	32,680	13,692	795	47,167
Mandatory reserves with the NBG	31,222	–	–	31,222	28,673	–	–	28,673
Loans to customers	308,856	–	–	308,856	252,888	–	–	252,888
Investment securities:								
- held-to-maturity	46,180	–	–	46,180	40,191	–	–	40,191
Other financial assets	902	91	–	993	6,715	–	–	6,715
All other assets	44,147	–	–	44,147	46,503	–	–	46,503
	<b>497,483</b>	<b>5,348</b>	<b>432</b>	<b>503,263</b>	<b>407,651</b>	<b>13,692</b>	<b>795</b>	<b>422,138</b>
<b>Liabilities:</b>								
Due to other banks	32,004	3,384	–	35,388	1,834	6,033	12,816	20,683
Customer accounts	335,711	73	4,185	339,969	293,266	3,211	–	296,478
Other financial liabilities	5,198	44	–	5,242	2,803	34	–	2,837
Subordinated debt	9,381	18,639	–	28,020	8,737	–	–	8,737
All other liabilities	1,502	–	–	1,502	685	–	–	685
	<b>383,796</b>	<b>22,140</b>	<b>4,185</b>	<b>410,121</b>	<b>307,325</b>	<b>9,278</b>	<b>12,816</b>	<b>329,420</b>
<b>Net assets / (liabilities)</b>	<b>113,687</b>	<b>(16,792)</b>	<b>(3,753)</b>	<b>93,142</b>	<b>100,326</b>	<b>4,414</b>	<b>(12,021)</b>	<b>92,718</b>

(Thousands of Georgian lari)

## 22 Risk management (continued)

### 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 Bank 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 and Supervisory 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 Bank'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 Bank's strategic goals;
- ▶ Maintaining a diverse range of funding sources thereby increasing the Bank'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 Bank 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 forecast levels of cash flows in the main currencies (GEL, USD, EUR), cash positions, statement of financial position changes;
- ▶ 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 Bank primarily on a standalone basis, based on certain liquidity ratios established by the NBG. As at 31 December, these ratios were as follows:

	<u>2014, %</u>	<u>2013, %</u>
Average liquidity ratio for the year	33.87%	39.68%
Maximum liquidity ratio	39.28%	47.44%
Minimum liquidity ratio	30.66%	36.76%

(Thousands of Georgian lari)

**22 Risk management (continued)****Liquidity risk and funding management (continued)**

Average liquidity ratio of the Bank for 2014, in accordance with the NBG liquidity regulation, comprises 33.87% (2013: 39.68%) as compared to the minimum required of 30%.

ALCO is responsible for ensuring that Treasury properly manages the Bank's liquidity position. The Risk Management Department is responsible for controlling these activities. Decisions on liquidity positions and management are made by the Management Board.

*Analysis of financial liabilities by remaining contractual maturities*

The tables below summarize the maturity profile of the Bank'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:

<b>Financial liabilities</b>	<i>Less than 3 months</i>	<i>3 to 12 months</i>	<i>1 to 5 years</i>	<i>Over 5 years</i>	<i>Total</i>
As at 31 December 2014					
Amounts due to credit institutions	32,878	2,669	–	–	35,547
Amounts due to customers	211,822	124,337	10,592	54	346,805
Other financial liabilities	5,242	–	–	–	5,242
Subordinated debts	506	1,328	7,083	35,073	43,990
<b>Total undiscounted financial liabilities</b>	<b>250,448</b>	<b>128,334</b>	<b>17,675</b>	<b>35,127</b>	<b>431,584</b>
<b>Financial liabilities</b>	<i>Less than 3 months</i>	<i>3 to 12 months</i>	<i>1 to 5 years</i>	<i>Over 5 years</i>	<i>Total</i>
As at 31 December 2013					
Amounts due to credit institutions	15,931	5,026	–	–	20,957
Amounts due to customers	196,018	96,130	9,327	81	301,556
Other financial liabilities	2,837	–	–	–	2,837
Subordinated debts	293	716	3,821	15,573	20,403
<b>Total undiscounted financial liabilities</b>	<b>215,079</b>	<b>101,872</b>	<b>13,148</b>	<b>15,654</b>	<b>345,753</b>

The table below shows the contractual expiry by maturity of the Bank's financial commitments and contingencies. Each undrawn loan commitment is included in the time band containing the earliest date it can be drawn down. For issued financial guarantee contracts, the maximum amount of the guarantee is allocated to the earliest period in which the guarantee could be called.

	<i>Less than 3 months</i>	<i>3 to 12 months</i>	<i>1 to 5 years</i>	<i>Over 5 years</i>	<i>Total</i>
2014	16,247	9,531	13,990	950	40,718
2013	23,044	18,302	5,993	1,234	48,573

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

(Thousands of Georgian lari)

## 22 Risk management (continued)

### Market risk

The Bank takes on exposure to market risks. Market risks arise from open positions in currency products which are exposed to general and specific market movements. Management is guided by the NBG's prudential ratio requirements on open currency position limits. These limits are monitored on a daily basis. However, the use of this approach does not prevent losses outside of these limits in the event of more significant market movements.

Interest rate risk arises from the possibility that changes in interest rates will affect future cash flows or the fair values of financial instruments. The only floating rate financial instruments as at 31 December 2014 are Loans from financial institutions in amount of GEL 3,378 (2013: GEL 6,033) (Note 14). The sensitivity of the net interest income to changes in the interest rate on these instruments is immaterial.

### Currency risk

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

The tables below indicate the currencies to which the Bank had significant exposure at 31 December on its non-trading monetary assets and liabilities and its forecast cash flows. The analysis calculates the effect of a reasonably possible movement of the currency rate against the Lari, with all other variables held constant on the statement of profit or loss (due to the fair value of currency sensitive non-trading monetary assets and liabilities). The effect on equity does not differ from the effect on the statement of profit or loss. A negative amount in the table reflects a potential net reduction in statement of profit or loss or equity, while a positive amount reflects a net potential increase

Currency	Change in currency rate in	Effect on profit	Change in	Effect on profit
	% 2014	before tax 2014	% 2013	before tax 2013
USD	3.77%	83,6	(0.6)	0.4
EUR	1.76%	(0.4)	0.81	0.2

### Operational risk

Operational risk is the risk of loss arising from systems failure, human error, fraud or external events. When controls fail to perform, operational risks can cause damage to reputation, have legal or regulatory implications, or lead to financial loss. The Bank cannot expect to eliminate all operational risks, but 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.

(Thousands of Georgian lari)

**23. Fair value measurements**

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

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

For the purpose of fair value disclosures, the Bank has determined classes of assets and liabilities on the basis of the level of the fair value hierarchy as explained above:

**At 31 December 2014**

	<i>Fair value measurement using</i>			<i>Total</i>
	<i>(Level 1)</i>	<i>(Level 2)</i>	<i>(Level 3)</i>	
<b>Assets for which fair values are disclosed</b>				
Cash and cash equivalents	--	--	71,865	71,865
Obligatory reserve with the NBG	--	--	31,222	31,222
Loans to customers	--	--	308,856	308,856
Investment securities held-to-maturity	--	46,180	--	46,180
Other financial assets	--	--	993	993
<b>Liabilities measured at fair value</b>				
Derivative financial instruments (valued at 31 December 2014)	--	3,976	--	3,976
<b>Liabilities for which fair values are disclosed</b>				
Amounts due to other banks	--	--	35,388	35,388
Amounts due to customers	--	--	339,969	339,969
Subordinated debts	--	--	28,020	28,020
Other financial liabilities	--	--	5,242	5,242

**At 31 December 2013**

	<i>Fair value measurement using</i>			<i>Total</i>
	<i>(Level 1)</i>	<i>(Level 2)</i>	<i>(Level 3)</i>	
<b>Assets for which fair values are disclosed</b>				
Cash and cash equivalents	--	--	47,167	47,167
Obligatory reserve with the NBG	--	--	28,673	28,673
Loans to customers	--	--	252,888	252,888
Investment securities held-to-maturity	--	40,191	--	40,191
Other financial assets	--	--	6,716	6,716
<b>Liabilities measured at fair value</b>				
Derivative financial instruments (valued at 31 December 2013)	--	1,486	--	1,486
<b>Liabilities for which fair values are disclosed</b>				
Amounts due to other banks	--	--	20,683	20,683
Amounts due to customers	--	--	296,478	296,478
Subordinated debts	--	--	8,737	8,737
Other financial liabilities	--	--	2,837	2,837

(Thousands of Georgian lari)

**23. Fair value measurements (continued)****Fair value of financial assets and liabilities not carried at fair value**

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

	<i>Carrying value 2014</i>	<i>Fair Value 2014</i>	<i>Unrecognised gain/(loss) 2014</i>	<i>Carrying value 2013</i>	<i>Fair value 2013</i>	<i>Unrecognised gain/(loss) 2013</i>
<b>Financial assets</b>						
Cash and cash equivalents	71,865	71,865	–	47,167	47,167	–
Obligatory reserve with the NBG	31,222	31,222	–	28,673	28,673	–
Loans to customers	308,856	308,579	(277)	252,888	252,698	(190)
Investment securities:						
- held-to-maturity	46,180	46,180	–	40,191	40,191	–
Other financial assets	993	993	–	6,716	6,716	–
<b>Financial liabilities</b>						
Amounts due to other banks	35,388	35,388	–	20,683	20,683	–
Amounts due to customers	339,969	339,969	–	296,478	296,478	–
Subordinated debts	28,020	32,894	(4,874)	8,737	8,737	–
Other financial liabilities	5,242	5,242	–	2,837	2,837	–
<b>Total unrecognised change in fair value</b>			<b>(5,151)</b>			<b>(190)</b>

**Valuation techniques and assumptions**

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

*Assets for which fair value approximates carrying value*

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

The Bank assumes that fair value of Held-to-maturity Investment securities equals its carrying value, due to the fact that secondary market for such instruments does not exist and it is irrelevant to consider the opportunity of disposing Investment securities. This is caused by the fact that the NBG permits the Georgian commercial banks to take loans of 95% of nominal amount by pledging these securities.

Based on the analysis performed in relation to long term credit lines, the Bank considers subordinated loans terms to be in line with current market range.

(Thousands of Georgian lari)

### 23. Fair value measurements (continued)

#### Valuation techniques and assumptions (continued)

##### Derivatives

Derivatives valued using a valuation technique with market observable inputs are currency swaps contracts. Due to the fact that these contracts have maturity of less than one year the Bank applies foreign exchange spot rates as at reporting date in order to calculate fair value of such contracts.

##### Fixed rate financial instruments

The fair values of unquoted debt instruments are estimated by discounting future cash flows using rates currently available for debt on similar terms, credit risk and remaining maturities.

### 24. Offsetting of financial instruments

The Bank offsets GEL 60,453 (2013: GEL 53,133) in derivative financial assets and liabilities. Net amount of derivative financial liabilities presented in the consolidated statement of financial position is GEL 3,976 (2012: GEL 1,486).

The table below shows financial assets offset against financial liabilities in the statement of financial position:

	<i>Gross amount of recognized financial assets set off in the consolidated statement of financial position</i>	<i>Gross amount of recognized financial liabilities set off in the consolidated statement of financial position</i>	<i>Net amount of financial liabilities presented in the consolidated statement of financial position</i>
<b>2014</b>			
Derivative financial liabilities (Note 12)	60,453	64,430	3,976
	<i>Gross amount of recognized financial assets set off in the consolidated statement of financial position</i>	<i>Gross amount of recognized financial liabilities set off in the consolidated statement of financial position</i>	<i>Net amount of financial liabilities presented in the consolidated statement of financial position</i>
<b>2013</b>			
Derivative financial liabilities (Note 12)	53,133	54,619	1,486



(Thousands of Georgian lari)

**25. 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. See Note 22 "Risk management" for the Bank's contractual undiscounted repayment obligations.

	2014			2013		
	Within one year	More than one year	Total	Within one year	More than one year	Total
Cash and cash equivalents	71,865	–	71,865	47,167	–	47,167
Mandatory reserve deposit with the NBG	31,222	–	31,222	28,673	–	28,673
Loans to customers	211,898	96,958	308,856	141,489	111,399	252,888
Investment securities:						
- held-to-maturity	22,659	23,521	46,180	20,467	19,724	40,191
Other financial assets	658	335	993	6,534	182	6,716
<b>Total</b>	<b>338,302</b>	<b>120,814</b>	<b>459,116</b>	<b>244,330</b>	<b>131,305</b>	<b>375,635</b>
Amounts due to credit institutions	35,388	–	35,388	20,683	–	20,683
Amounts due to customers	330,236	9,733	339,969	288,357	8,121	296,478
Subordinated debts	64	27,956	28,020	54	8,683	8,737
Other financial liabilities	5,242	–	5,242	2,837	–	2,837
<b>Total</b>	<b>370,930</b>	<b>37,689</b>	<b>408,619</b>	<b>311,931</b>	<b>16,804</b>	<b>328,735</b>
<b>Net</b>	<b>(32,628)</b>	<b>83,125</b>	<b>50,497</b>	<b>(67,601)</b>	<b>114,501</b>	<b>46,900</b>

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

As at 31 December 2014, total current accounts within amounts due to customers amounted to GEL 158,283 (2013: GEL 163,603). The Bank conducts 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 116,865 (2013: GEL 115,846) for the preceding 24 months. Significant part of total Current accounts represents interest bearing corporate current accounts which historically are of long-term nature. As such, it is reasonable to treat these funds for estimation of liquidity position of the Bank in Amounts due to customers as with maturity of more than one year.

As at 31 December 2014, the Bank has treasury bonds of Ministry of Finance with maturity ranging from 2016 to 2019 and nominal amount of GEL 23,403 which can be pledged to the NBG for refinancing purposes, anytime with 5% discount (generating GEL 22,233).

The Bank has access to interbank short-term facility which is not expensive and can be obtained with 2% to 5% annual interest rate for the period from overnight to six months. During 2014 the Bank utilized and repaid the total amount of GEL 152,610 (2013: GEL 112,359) of such interbank placements.

According to the NBG regulation monthly average liquidity ratio should not be less than 30%. The Bank was compliant with the NBG prudential ratio requirements in respect of liquidity during 2014 and 2013. Average liquidity ratio of the Bank for 2014 was 33.87%. For more details please refer to Note 22, Liquidity risk and funding management caption.

(Thousands of Georgian lari)

## 26. Related party disclosures

In accordance with IAS 24 "Related Party Disclosures", parties are considered to be related if one party has the ability to control the other party or exercise significant influence over the other party in making financial or operational decisions. In considering each possible related party relationship, attention is directed to the substance of the relationship, not merely the legal form. Related parties may enter into transactions which unrelated parties might not, and transactions between related parties may not be effected on the same terms, conditions and amounts as transactions between unrelated parties.

The volumes of related party transactions, outstanding balances at the year end and related income and expenses for the year are as follows:

	Note	2014			2013		
		Entities under common control	Key Management personnel	Other related parties	Entities under common control	Key Management personnel	Other related parties
Loans and advances to customers		–	257	–	907	5	72
Amounts due to customers		2,615	25	–	568	62	55
Subordinated debt	16	18,639	–	–	–	–	–
Interest income on loans		1	5	–	243	–	10
Interest expense on deposits		29	–	–	16	8	2

In 2014, the Bank issued letter of credit to entity under common control in amount of GEL 1,323 (2013: nil).

As at 31 December 2014, undrawn loan commitments of key management personnel consisted of GEL 6 (2013: GEL 6).

As at 31 December 2014 key management personnel comprised of 5 persons (2013: 6). Compensation of key management personnel comprised of salaries and short-term benefits and amounted to GEL 1,169 in 2014 (2013: GEL 1,140).

(Thousands of Georgian lari)

**27. 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 signed by the Bank's General Director and Chief Accountant 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 NBG capital adequacy ratio**

The NBG requires banks to maintain a minimum total capital adequacy ratio of 12% (2013 – 12%) of risk-weighted assets and tier 1 capital adequacy ratio of 8% (2013 – 8%)., computed based on the Bank's standalone special purpose financial statements prepared in accordance with the NBG regulations and pronouncements. As of 31 December, the Bank's capital adequacy ratio on this basis was as follows:

	<u>2014</u>	<u>2013</u>
Core capital	60,880	53,651
Supplementary capital	23,072	19,711
Less: Deductions from capital	–	(500)
<b>Total regulatory capital</b>	<b>83,952</b>	<b>72,862</b>
<b>Risk weighted assets</b>	<b>554,456</b>	<b>518,055</b>
Total Capital adequacy ratio	15.14%	14.06%
Tier 1 Capital adequacy ratio	10.98%	10.36%

Starting from 30 June 2014 the NBG requires that all banks comply with Basel II regulations in their capital adequacy assessment. This implies the minimum ratio of 10.50% for total regulatory capital coefficient and minimum 8.50 % for Tier 1 capital coefficient. As at 31 December 2014, the Bank's capital adequacy ratios on the Basel II basis were as follows:

	<u>2014</u>
Core capital	52,131
Supplementary capital	31,821
<b>Total regulatory capital</b>	<b>83,952</b>
<b>Risk weighted assets</b>	<b>570,994</b>
Total Capital adequacy ratio	14.7%
Tier 1 Capital adequacy ratio	9.13%

**28. Events after the reporting date**

Loan from the BSTDB included in amounts due to credit institutions (Note 14) was fully repaid at maturity on 4 February 2015.

The Bank has made capital increase agreement with the existing Shareholders. Starting from April 2015 within 5 months period the share capital will be increased by approximately GEL 10,000. As at the date of issuance of these financial statements the Shareholders have already injected GEL 2,233 in cash.