

JSC Isbank Georgia

Financial Statements

for the year ended 31 December 2016

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Independent Auditors' Report

To the Shareholder of JSC Isbank Georgia

Opinion

We have audited the financial statements of JSC Isbank Georgia (the "Company"), which comprise the statement of financial position as at 31 December 2016, the statements of profit or loss and other comprehensive income, changes in equity and cash flows for the year then ended, and notes, comprising significant accounting policies and other explanatory information.

In our opinion, the accompanying financial statements present fairly, in all material respects, the financial position of the Company as at 31 December 2016, and its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards (IFRS).

Basis for Opinion

We conducted our audit in accordance with International Standards on Auditing (ISAs). Our responsibilities under those standards are further described in the Auditors' Responsibilities for the Audit of the Financial Statements section of our report. We are independent of the Company in accordance with the International Ethics Standards Board for Accountants' Code of Ethics for Professional Accountants (IESBA Code), and we have fulfilled our other ethical responsibilities in accordance with the IESBA Code. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Responsibilities of Management and Those Charged with Governance for the Financial Statements

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

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

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

Auditors' Responsibilities for the Audit of the Financial Statements

Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditors' report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISAs will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could

Independent Auditors' Report

JSC Isbank Georgia

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reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.


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

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

We communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

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

Andrew Coxshall



KPMG Georgia LLC

Tbilisi, Georgia

8 May 2017



JSC Isbank Georgia
Statement of Profit or Loss and Other Comprehensive Income for the year ended 31 December 2016

	Notes	2016 000'GEL	2015 000'GEL	2014 000'GEL
Interest income	4	16,373	12,767	5,060
Interest expense	4	(7,892)	(6,060)	(1,464)
Net interest income	4	8,481	6,707	3,596
Fee and commission gain		1,334	803	288
Fee and commission expense		(1,041)	(677)	(243)
Net fee and commission income		293	126	44
Net foreign exchange income		1,189	1,308	280
Operating income		9,963	8,141	3,921
Impairment losses	5	861	(1,324)	(1,091)
Personnel expenses	6	(3,615)	(2,739)	(1,696)
Other general administrative expenses	7	(2,757)	(2,202)	(1,274)
Profit/(loss) before income tax		4,452	1,876	(140)
Income tax (expense)/benefit	8	(665)	(205)	30
Profit/(loss) and total comprehensive income/(loss) for the year		3,787	1,671	(110)

The financial statements as set out on pages 5 to 49 were approved by management on 8 May 2017 and were signed on its behalf by:


Ozan Gür
 Chief Executive Officer


Ucha Saralidze
 Chief Financial Officer

The statement of profit or loss and other comprehensive income for the year ended is to be read in conjunction with the notes to, and forming part of, the financial statements.

JSC Isbank Georgia
Statement of Financial Position as at 31 December 2016

	Notes	2016 000'GEL	2015 000'GEL	2014 000'GEL
ASSETS				
Cash and cash equivalents	9	44,098	38,889	14,034
Mandatory reserves at National Bank of Georgia		46,607	25,819	5,436
Held-to-maturity investments		1,018	-	-
Loans to customers	10	179,786	145,285	69,091
Property, equipment and intangible assets	11	2,283	2,831	1,951
Deferred tax assets	8	-	-	142
Other assets	19	2,258	233	758
Total assets		276,050	213,057	91,412
LIABILITIES				
Deposits and balances from banks	12	173,884	126,224	8,932
Current accounts and deposits from customers	13	65,100	55,016	32,843
Other borrowed funds	14	-	-	36,709
Deferred tax liabilities	8	579	40	-
Other liabilities	20	1,203	280	722
Total liabilities		240,766	181,560	79,206
EQUITY				
Share capital		30,000	30,000	-
Statutory reserve		-	-	13,013
Retained earnings/(accumulated losses)		5,284	1,497	(807)
Total equity	16	35,284	31,497	12,206
Total liabilities and equity		276,050	213,057	91,412

The statement of financial position is to be read in conjunction with the notes to, and forming part of, the financial statements.

JSC Isbank Georgia
Statement of Cash Flows for the year ended 31 December 2016

	Notes	2016 000'GEL	2015 000'GEL	2014 000'GEL
CASH FLOWS FROM OPERATING ACTIVITIES				
Profit/(loss) before income tax		4,452	1,876	(140)
<i>Adjustments for:</i>				
Depreciation and amortization	11	836	563	289
Interest income	4	(16,373)	(12,767)	(5,060)
Interest expense	4	7,892	6,060	1,464
(Reversal of impairment losses)/impairment losses	5	(861)	1,324	1,091
Net foreign exchange gain		(1,189)	(1,308)	(280)
		<u>(5,243)</u>	<u>(4,252)</u>	<u>(2,636)</u>
<i>Change in operating assets and liabilities:</i>				
Increase in mandatory reserves at National Bank of Georgia		(16,203)	(18,334)	(4,670)
Increase in loans to customers		(17,863)	(55,611)	(49,487)
(Increase)/decrease in other assets		(1,891)	525	(754)
Increase in deposits and balances from banks		30,061	63,527	6,590
Increase in current accounts and deposits from customers		5,368	14,093	28,519
Increase/(decrease) in other liabilities		923	(443)	712
Cash flows used in operations before interest and foreign exchange		<u>(4,848)</u>	<u>(495)</u>	<u>(21,726)</u>
Interest receipts		14,541	11,837	4,037
Interest payments		(7,925)	(4,762)	(1,248)
Net receipts from foreign exchange		957	998	400
Income tax paid		(126)	-	-
Cash flows from/(used in) operations		<u>2,599</u>	<u>7,578</u>	<u>(18,537)</u>
CASH FLOWS FROM INVESTING ACTIVITIES				
Purchases of held-to-maturity investments		(1,018)	-	-
Purchases of property, equipment and intangible assets	11	(288)	(1,443)	(1,228)
Cash flows used in investing activities		<u>(1,306)</u>	<u>(1,443)</u>	<u>(1,228)</u>
CASH FLOWS FROM FINANCING ACTIVITIES				
Receipts from other borrowed funds		-	-	23,010
Repayment of other borrowed funds		-	-	(2,216)
Receipts from increase of share capital/statutory reserve		-	17,620	156
Cash flows from financing activities		<u>-</u>	<u>17,620</u>	<u>20,950</u>
Net increase in cash and cash equivalents		1,293	23,755	1,185
Effect of changes in exchange rates on cash and cash equivalents		3,916	1,100	231
Cash and cash equivalents as at the beginning of the year		38,889	14,034	12,618
Cash and cash equivalents as at the end of the year	9	<u>44,098</u>	<u>38,889</u>	<u>14,034</u>

The statement of cash flows is to be read in conjunction with the notes to, and forming part of, the financial statements.

JSC Isbank Georgia
Statement of Changes in Equity for the year ended 31 December 2016

000'GEL	Statutory reserve	Share capital	Retained earnings/ (accumulated losses)	Total equity
Balance as at 1 January 2014	12,857	-	(697)	12,160
Loss and total comprehensive loss for the year		-	(110)	(110)
Transactions with shareholder, recorded directly in equity				
Increase of statutory reserve	156	-	-	156
Total transactions with shareholder	156	-	-	156
Balance as at 31 December 2014	13,013	-	(807)	12,206
Balance as at 1 January 2015	13,013	-	(807)	12,206
Profit and total comprehensive income for the year	-	-	1,671	1,671
Transactions with shareholder, recorded directly in equity				
Transfer of statutory reserve to the share capital	(13,013)	13,013	-	-
Transfer of accumulated losses as at 31 December to the share capital (Note 1a)	-	(807)	807	-
Transfer of accumulated gain as at 31 July 2015 to the share capital (Note 1a)	-	174	(174)	-
Cash contribution into the share capital	-	17,620	-	17,620
Total transactions with shareholder	(13,013)	30,000	633	17,620
Balance as at 31 December 2015	-	30,000	1,497	31,497
Balance as at 1 January 2016	-	30,000	1,497	31,497
Profit and total comprehensive income for the year	-	-	3,787	3,787
Balance as at 31 December 2016	-	30,000	5,284	35,284

The statement of changes in equity is to be read in conjunction with the notes to, and forming part of, the financial statements.

1 Background

(a) Organisation and operations

Batumi Branch of JSC Isbank Turkey (the “Branch”) was registered on 13 July 2012 as a branch of a foreign bank Türkiye İş Bankası Anonim Şirketi (the “Parent”/the “Shareholder”) which was incorporated in Turkey in 1924. On 1 August 2015 the Branch was reorganized into JSC Isbank Georgia (the “Bank”) and all assets and liabilities of the Branch were transferred to the Bank as at that date. At the same date statutory reserves and accumulated losses as at 31 December 2014 and accumulated gain for the seven-month period ended 31 July 2015 of GEL 13,013 thousand, GEL 807 thousand and GEL 174 thousand, respectively were transferred to the share capital (see Statement of Changes in Equity).

The principal activities of the Bank are deposit taking and customer account maintenance, lending, cash and settlement operations and foreign exchange transactions. The Bank has a general banking license and its activities are regulated by the National Bank of Georgia (the “NBG”).

The registered office of the Bank is D. Aghmashenebeli Ave. 140/B, Tbilisi, Georgia. The Bank has two branches in Tbilisi and Batumi and two service centers in Batumi.

The majority of the funding (45% as at 31 December 2016, 51% as at 31 December 2015 and 64% as at 31 December 2014) of the Bank is from the Parent. As a result the Bank is economically dependent upon the Parent. In addition, the activities of the Bank are closely linked with the requirements of the Parent.

The Bank is ultimately controlled by Isbank Members’ Supplementary Pension Fund. Related party transactions are disclosed in note 22.

(b) Business environment

Georgian business environment

The Bank’s operations are located in Georgia. Consequently, the Bank is exposed to the economic and financial markets of Georgia, which display emerging-market characteristics. Legal, tax and regulatory frameworks continue to develop, but are subject to varying interpretations and frequent changes that, together with other legal and fiscal impediments, contribute to the challenges faced by entities operating in Georgia. The financial statements reflect management’s assessment of the impact of the Georgian business environment on the operations and financial position of the Bank. The future business environment may differ from management’s assessment.

2 Basis of preparation

(a) Statement of compliance

The accompanying financial statements are prepared in accordance with International Financial Reporting Standards (IFRS). The Bank presents comparative information for all amounts reported in the current period’s financials statement for the two preceding periods – years ended 31 December 2015 and 2014. The Bank management considers such disclosure more useful and informative for the stakeholders of the Bank.

(b) Basis of measurement

The financial statements are prepared on the historical cost basis.

(c) Functional and presentation currency

The national currency of Georgia is the Georgian Lari (GEL), which is the Bank's functional currency and the currency in which these financial statements are presented. All financial information presented in GEL has been rounded to the nearest thousand, except otherwise stated.

(d) Use of estimates and judgments

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

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

Information about significant areas of estimation uncertainty and critical judgments in applying accounting policies is described in the note 10 (b) – key assumptions and judgments for estimating loan impairment.

3 Significant accounting policies

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

(a) Foreign currency

Transactions in foreign currencies are translated to the respective functional currency of the Bank at exchange rates at the dates of the transactions. Monetary assets and liabilities denominated in foreign currencies at the reporting date are retranslated to the functional currency at the exchange rate at that date. The foreign currency gain or loss on monetary items is the difference between amortized cost in the functional currency at the beginning of the period, adjusted for effective interest and payments during the period, and the amortized cost in foreign currency translated at the exchange rate at the end of the reporting period. Non-monetary assets and liabilities denominated in foreign currencies that are measured at fair value are retranslated to the functional currency at the exchange rate at the date that the fair value is determined. Non-monetary items that are measured in terms of historical cost in a foreign currency are translated using the exchange rate at the date of the transaction. Foreign currency differences arising on revaluation are recognized in profit or loss.

(b) Cash and cash equivalents

Cash and cash equivalents include notes and coins on hand, unrestricted balances (Nostro accounts) held with the NBG and other banks and highly liquid financial assets with original maturities of less than three months, which are subject to insignificant risk of changes in their fair value, and are used by the Bank in the management of short-term commitments.

Resident financial institutions are required to maintain an interest-earning obligatory reserve with the NBG, the amount of which depends on the level of funds attracted by the financial institutions. The mandatory reserve deposit with the NBG is not available to finance the Company's day to day operations and hence is not considered as part of cash and cash equivalents.

Cash and cash equivalents are carried at amortized cost in the statement of financial position.

(c) Financial instruments

(i) Classification

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

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

(ii) Recognition

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

(iii) Measurement

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

Subsequent to initial recognition, financial assets are measured at amortized cost using the effective interest method.

All financial liabilities are measured at amortized cost.

(iv) Amortized cost

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

(v) Fair value measurement principles

Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date in the principal, or in its absence, the most advantageous market to which the Bank has access at that date. The fair value of a liability reflects its non-performance risk.

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

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

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

(vi) Gains and losses on subsequent measurement

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

(vii) Derecognition

The Bank derecognizes a financial asset when the contractual rights to the cash flows from the financial asset expire, or when it transfers the financial asset in a transaction in which substantially all the risks and rewards of ownership of the financial asset are transferred or in which the Bank neither transfers nor retains substantially all the risks and rewards of ownership and it does not retain control of the financial asset. The Bank derecognizes a financial liability when its contractual obligations are discharged or cancelled or expire.

The Bank writes off assets deemed to be uncollectible.

(viii) Offsetting

Financial assets and liabilities are offset and the net amount reported in the statement of financial position when there is a legally enforceable right to set off the recognized amounts and there is an intention to settle on a net basis, or realize the asset and settle the liability simultaneously.

(d) Property and equipment

(i) Owned assets

Items of property and equipment are stated at cost less accumulated depreciation and impairment losses.

Where an item of property and equipment comprises major components having different useful lives, they are accounted for as separate items of property and equipment.

(ii) Depreciation

Depreciation is charged to profit or loss on a straight-line basis over the estimated useful lives of the individual assets. Depreciation commences on the date of acquisition or, in respect of internally constructed assets, from the time an asset is completed and ready for use. The estimated useful lives are as follows:

- leasehold improvements	5 years
- computers and office equipment	5 years
- furniture and fixtures	5 years
- motor vehicles	5 years

Leasehold improvements are depreciated over the shorter of the lease term and their useful lives.

Depreciation methods, useful lives and residual values are reviewed at each reporting date and adjusted if appropriate.

(e) Intangible assets

Acquired intangible assets are stated at cost less accumulated amortization and impairment losses.

Acquired computer software licenses are capitalized on the basis of the costs incurred to acquire and bring to use the specific software.

Amortization is charged to profit or loss on a straight-line basis over the estimated useful lives of intangible assets. The estimated useful lives range from 6 to 7 years.

(f) Impairment

The Bank assesses at the end of each reporting period whether there is any objective evidence that a financial asset or group of financial assets is impaired. If any such evidence exists, the Bank determines the amount of any impairment loss.

A financial asset or a group of financial assets is impaired and impairment losses are incurred if, and only if, there is objective evidence of impairment as a result of one or more events that occurred after the initial recognition of the financial asset (a loss event) and that event (or events) has had an impact on the estimated future cash flows of the financial asset or group of financial assets that can be reliably estimated.

Objective evidence that financial assets are impaired can include default or delinquency by a borrower, breach of loan covenants or conditions, restructuring of financial asset or group of financial assets that the Bank would not otherwise consider, indications that a borrower or issuer will enter bankruptcy, the disappearance of an active market for a security, deterioration in the value of collateral, or other observable data related to a group of assets such as adverse changes in the payment status of borrowers in the group, or economic conditions that correlate with defaults in the group.

(i) Financial assets carried at amortized cost

Financial assets carried at amortized cost consist principally of loans and other receivables (loans and receivables). The Bank reviews its loans and receivables to assess impairment on a regular basis.

The Bank first assesses whether objective evidence of impairment exists individually for loans and receivables that are individually significant, and individually or collectively for loans and receivables that are not individually significant. If the Bank determines that no objective evidence of impairment exists for an individually assessed loan or receivable, whether significant or not, it includes the loan or receivable in a group of loans and receivables with similar credit risk characteristics and collectively assesses them for impairment. Loans and receivables that are individually assessed for impairment and for which an impairment loss is or continues to be recognized are not included in a collective assessment of impairment.

If there is objective evidence that an impairment loss on a loan or receivable has been incurred, the amount of the loss is measured as the difference between the carrying amount of the loan or receivable and the present value of estimated future cash flows including amounts recoverable from guarantees and collateral discounted at the loan or receivable's original effective interest rate. Contractual cash flows and historical loss experience adjusted on the basis of relevant observable data that reflects current economic conditions provide the basis for estimating expected cash flows.

In some cases the observable data required to estimate the amount of an impairment loss on a loan or receivable may be limited or no longer fully relevant to current circumstances. This may be the case when a borrower is in financial difficulties and there is little available historical data related to similar borrowers. In such cases, the Bank uses its experience and judgment to estimate the amount of any impairment loss.

All impairment losses in respect of loans and receivables are recognized in profit or loss and are only reversed if a subsequent increase in recoverable amount can be related objectively to an event occurring after the impairment loss was recognized.

When a loan is uncollectable, it is written off against the related allowance for loan impairment. The Bank writes off a loan's outstanding amount (and any related allowances for loan losses) when management determines that the loans are uncollectible and when all necessary steps to collect the loan are completed.

(ii) Non-financial assets

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

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

(g) Credit related commitments

In the normal course of business, the Bank enters into credit related commitments, comprising undrawn loan commitments and guarantees.

Financial guarantees are contracts that require the Bank to make specified payments to reimburse the holder for a loss it incurs because a specified debtor fails to make payment when due in accordance with the terms of a debt instrument.

A financial guarantee liability is recognized initially at fair value net of associated transaction costs, and is measured subsequently at the higher of the amount initially recognized, less cumulative amortization or the amount of provision for losses under the guarantee. Provisions for losses under financial guarantees and other credit related commitments are recognized when losses are considered probable and can be measured reliably.

Financial guarantee liabilities and provisions for other credit related commitment are included in other liabilities.

(h) Share capital and statutory reserve

According to the Georgian Law on Entrepreneurs, a branch does not have registered charter capital. In accordance with the NBG requirements the Branch had a statutory reserve as at 31 December 2014.

After the reorganization of the Branch into a Bank on 1 August 2015 the Bank registered its share capital (see note 1 (a)).

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

The ability of the Bank to declare and pay dividends is subject to the rules and regulations of Georgian legislation.

Dividends in relation to ordinary shares are reflected as an appropriation of retained earnings in the period when they are declared.

(i) Income tax

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

Current tax

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

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

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

Tax reimbursement is available for the current tax paid on the undistributed earnings in the years 2008-2016, if those earnings are distributed in 2019 or further years.

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

Deferred tax

Deferred tax is provided for temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes. The following temporary differences are not provided for: goodwill not deductible for tax purposes, the initial recognition of assets or liabilities that affect neither accounting nor taxable profit and temporary differences related to investments in subsidiaries, branches and associates where the parent is able

to control the timing of the reversal of the temporary difference and it is probable that the temporary difference will not reverse in the foreseeable future. The amount of deferred tax provided is based on the expected manner of realisation or settlement of the carrying amount of assets and liabilities until 1 January 2019, using tax rates enacted or substantially enacted at the reporting date.

A deferred tax asset is recognised only to the extent that it is probable that future taxable profits will be available until 1 January 2019 against which the temporary differences, unused tax losses and credits can be utilised. Deferred tax assets are reviewed at each reporting date and are reduced to the extent that it is no longer probable that the related tax benefit will be realised.

Due to the nature of the new taxation system described above, the financial institutions registered in Georgia will not have any differences between the tax bases of assets and their carrying amounts from 1 January 2019 and hence, no deferred income tax assets and liabilities will arise, there on.

(j) **Income and expense recognition**

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

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

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

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

4 **Net interest income**

	2016 000'GEL	2015 000'GEL	2014 000'GEL
Interest income			
Cash and cash equivalents	1,251	671	212
Held-to-maturity investments	16	-	-
Loans to customers	15,106	12,096	4,848
	<u>16,373</u>	<u>12,767</u>	<u>5,060</u>
Interest expense			
Deposits and balances from banks	(5,996)	(3,437)	(88)
Current accounts and deposits from customers	(1,896)	(2,437)	(206)
Other borrowed funds	-	(186)	(1,170)
	<u>(7,892)</u>	<u>(6,060)</u>	<u>(1,464)</u>
Net interest income	<u>8,481</u>	<u>6,707</u>	<u>3,596</u>

5 Reversal of impairment losses /(impairment losses)

	2016 000'GEL	2015 000'GEL	2014 000'GEL
Reversal of impairment losses /(impairment losses) on loans to customers	<u>861</u>	<u>(1,324)</u>	<u>(1,091)</u>

6 Personnel expenses

	2016 000'GEL	2015 000'GEL	2014 000'GEL
Employee compensation	<u>3,615</u>	<u>2,739</u>	<u>1,696</u>

7 Other general administrative expenses

	2016 000'GEL	2015 000'GEL	2014 000'GEL
Operating lease	1,003	814	412
Depreciation and amortization	836	563	289
Professional services	384	350	238
Communications and information services	58	115	73
Utilities	38	32	24
Entertainment expenses	34	48	36
Travel expenses	17	58	73
Office supplies	19	15	27
Taxes other than on income	15	40	10
Insurance	11	18	8
Advertising and marketing	11	10	3
Repairs and maintenance	5	21	14
Other	326	118	67
	<u>2,757</u>	<u>2,202</u>	<u>1,274</u>

8 Income tax expense

	2016 000'GEL	2015 000'GEL	2014 000'GEL
Current year tax expense	<u>(126)</u>	<u>(23)</u>	<u>-</u>
Deferred tax (expense)/benefit			
Movement in deferred tax assets and liabilities due to origination and reversal of temporary differences	(376)	(182)	30
Write off of tax loss carried forward	(163)	-	-
	<u>(539)</u>	<u>(182)</u>	<u>30</u>
Total income tax (expense)/benefit	<u>(665)</u>	<u>(205)</u>	<u>30</u>

In 2016, the applicable tax rate for current and deferred tax is 15% (2015: 15%; 2014: 15%).

Reconciliation of effective tax rate for the year ended 31 December:

	2016		2015		2014	
	000'GEL	%	000'GEL	%	000'GEL	%
Profit/(loss) before tax	4,452	100%	1,876	100%	(140)	100%
Income tax at the applicable tax rate	(668)	(15%)	(281)	(15%)	21	15%
Non-taxable income and other differences	3	0%	76	4%	9	6%
	(665)	(15%)	(205)	(11%)	30	21%

(a) Deferred tax assets and liabilities

The deductible temporary differences do not expire under current tax legislation. For expected changes in profit tax legislation please refer to note 20 (c).

Movements in temporary differences during the years ended 31 December 2016, 2015 and 2014 are presented as follows.

000'GEL	Balance 1 January 2016	Recognized in profit or loss	Balance 31 December 2016
Property, equipment and intangible assets	7	17	24
Loans to customers	(210)	(393)	(603)
Tax loss carry-forwards	163	(163)	-
Net tax assets/(liabilities)	(40)	(539)	(579)

000'GEL	Balance 1 January 2015	Recognized in profit or loss	Balance 31 December 2015
Property, equipment and intangible assets	(21)	28	7
Loans to customers	-	(210)	(210)
Tax loss carry-forwards	163	-	163
Net tax assets/(liabilities)	142	(182)	(40)

000'GEL	Balance 1 January 2014	Recognized in profit or loss	Balance 31 December 2014
Property, equipment and intangible assets	(19)	(2)	(21)
Tax loss carry-forwards	131	32	163
Net tax assets	112	30	142

9 Cash and cash equivalents

	2016 000'GEL	2015 000'GEL	2014 000'GEL
Cash on hand	3,865	2,646	2,242
Cash equivalents			
Nostro accounts with the NBG	423	528	339
Nostro accounts with other banks rated BB-	3,198	17,710	6,892
Term deposits with other banks:			
- rated BB-	33,964	13,503	4,561
- not rated	2,648	4,502	-
Total cash equivalents	40,233	36,243	11,792
Total cash on hand and cash equivalents	44,098	38,889	14,034

No cash and cash equivalents are impaired or past due.

As at 31 December 2016 the Bank has two banks (2015: three banks; 2014: three banks), whose balances exceed 10% of equity. The gross value of these balances as at 31 December 2016 is GEL 34,799 thousand (2015: GEL 34,557 thousand; 2014: GEL 11,453 thousand).

The above ratings are based on Fitch Ratings agency.

10 Loans to customers

	2016 000'GEL	2015 000'GEL	2014 000'GEL
Loans to legal entities			
Loans to corporate customers	162,872	140,507	54,703
Loans to small and medium size companies	10,828	2,867	14,194
Total loans to legal entities	173,700	143,374	68,897
Loans to individuals			
Consumer loans	5,774	3,344	776
Mortgage loans	2,073	1,297	836
Overdrafts	130	22	10
Total loans to individuals	7,977	4,663	1,622
Gross loans to customers	181,677	148,037	70,519
Impairment allowance	(1,891)	(2,752)	(1,428)
Net loans to customers	179,786	145,285	69,091

Movements in the loan impairment allowance by classes of loans to customers for the year ended 31 December 2016 are as follows:

	Loans to legal entities 000'GEL	Loans to individuals 000'GEL	Total 000'GEL
Balance at the beginning of the year	2,568	184	2,752
Net charge/(reversal)	(1,165)	304	(861)
Balance at the end of the year	1,403	488	1,891

Movements in the loan impairment allowance by classes of loans to customers for the year ended 31 December 2015 are as follows:

	Loans to legal entities 000'GEL	Loans to individuals 000'GEL	Total 000'GEL
Balance at the beginning of the year	1,395	33	1,428
Net charge	1,173	151	1,324
Balance at the end of the year	2,568	184	2,752

Movements in the loan impairment allowance by classes of loans to customers for the year ended 31 December 2014 are as follows:

	Loans to legal entities 000'GEL	Loans to individuals 000'GEL	Total 000'GEL
Balance at the beginning of the year	334	3	337
Net charge	1,061	30	1,091
Balance at the end of the year	1,395	33	1,428

(a) Credit quality of loans to customers

The following table provides information on the credit quality of loans to customers as at 31 December 2016:

	Gross loans 000'GEL	Impairment allowance 000'GEL	Net loans 000'GEL	Impairment allowance to gross loans, %
Loans to legal entities				
Loans to corporate customers				
Individually assessed impaired loans	67,104	(92)	67,012	0.14%
Individually assessed not impaired loans	95,768	(1,046)	94,722	1.09%
Total loans to corporate customers	162,872	(1,138)	161,734	0.70%
Loans to small and medium size companies				
Individually assessed impaired loans	1,988	(40)	1,948	2.01%
Individually assessed not impaired loans	4,270	(73)	4,197	1.71%
Collectively assessed not impaired loans	4,570	(152)	4,418	3.33%
Total loans to small and medium size companies	10,828	(265)	10,563	2.45%
Total loans to legal entities	173,700	(1,403)	172,297	0.81%
Loans to individuals				
Consumer loans				
- not overdue	4,814	(162)	4,652	3.37%
-overdue less than 90 days	347	(12)	335	3.46%
-overdue more than 90 days	613	(286)	327	46.66%
Mortgage loans				
- not overdue	2,032	(19)	2,013	0.94%
-overdue less than 90 days	41	(1)	40	2.44%
-overdue more than 90 days	-	-	-	0.00%
Overdrafts				
- not overdue	130	(8)	122	6.15%
Total loans to individuals	7,977	(488)	7,489	6.12%
Total loans to customers	181,677	(1,891)	179,786	1.04%

No provision was provided on individually assessed loans with signs of impairment of GEL 62,224 thousand as they are fully collateralized by cash and deposits, see note 10 (c) (i) and therefore the credit risk is fully mitigated; In case of a default of those loans the cash collaterals can be repossessed. Cash and deposits are provided as a cash cover against loans to customers to be in compliance with single borrower lending limits in accordance with the NBG regulation. From individually assessed impaired loans of GEL 67,104 thousand, GEL 17,967 thousand is not overdue and GEL 49,137 thousand is overdue for less than 90 days. From total loans to customers of GEL 181,677 thousand GEL 2,744 thousand is overdue for more than 90 days, which amounts 1.51% of total loans to customers.

The following table provides information on the credit quality of loans to customers as at 31 December 2015:

	Gross loans	Impairment allowance	Net loans	Impairment allowance to gross loans,
	000'GEL	000'GEL	000'GEL	%
Loans to legal entities				
Loans to corporate customers				
Individually assessed impaired loans	57,447	-	57,447	0.00%
Individually assessed not impaired loans	82,913	(2,498)	80,415	3.01%
Collectively assessed not impaired loans	147	(14)	133	9.52%
Total loans to corporate customers	140,507	(2,512)	137,995	1.79%
Loans to small and medium size companies				
Individually assessed not impaired loans	709	(14)	695	1.97%
Collectively assessed not impaired loans	2,158	(42)	2,116	1.95%
Total loans to small and medium size companies	2,867	(56)	2,811	1.95%
Total loans to legal entities	143,374	(2,568)	140,806	1.79%
Loans to individuals				
Consumer loans				
- not overdue	3,070	(131)	2,939	4.27%
-overdue less than 90 days	247	(12)	235	4.86%
-overdue more than 90 days	27	(27)	-	100.00%
Mortgage loans				
- not overdue	1,184	(12)	1,172	1.01%
-overdue less than 90 days	113	(1)	112	0.88%
Overdrafts				
- not overdue	22	(1)	21	4.55%
Total loans to individuals	4,663	(184)	4,479	3.95%
Total loans to customers	148,037	(2,752)	145,285	1.86%

No provision was provided on loans of GEL 57,447 thousand with individual signs of impairment as they are fully collateralized by cash and deposits, see note 10 (c) (i) and therefore the credit risk is fully mitigated; in case of a default of those loans the cash collaterals can be repossessed. Cash and deposits are provided as a cash cover against loans to customers to be in compliance with single borrower lending limits in accordance with the NBG regulation.

The following table provides information on the credit quality of the loans to customers as at 31 December 2014:

	Gross loans 000'GEL	Impairment allowance 000'GEL	Net loans 000'GEL	Impairment allowance to gross loans, %
Loans to legal entities				
Loans to corporate customer				
Individually assessed not impaired loans	54,703	(1,098)	53,605	2.01%
Total loans to corporate customers	54,703	(1,098)	53,605	2.01%
Loans to small and medium size companies				
Individually assessed not impaired loans	824	(17)	807	2.06%
Collectively assessed not impaired loans	13,370	(281)	13,089	2.10%
Total loans to small and medium size companies	14,194	(298)	13,896	2.10%
Total loans to legal entities	68,897	(1,396)	67,501	2.03%
Loans to individuals				
Consumer loans				
- not overdue	776	(16)	760	2.06%
Mortgage loans				
- not overdue	836	(16)	820	1.91%
Overdrafts				
- not overdue	10	-	10	0.00%
Total loans to individuals	1,622	(32)	1,590	1.97%
Total loans to customers	70,519	(1,428)	69,091	2.02%

As at 31 December 2016 in the loan portfolio renegotiated loans to legal entities and individuals that would otherwise be past due or impaired were GEL 60,380 thousand (2015: GEL 48,173 thousand, 2014: nil).

(b) Key assumptions and judgments for estimating loan impairment

(i) Individually significant loans

The Bank uses a threshold of 2% of total equity to consider a borrower as individually significant. Impairment for loans to significant borrowers is determined based on an analysis of following triggers:

- the loan meets the definition of a non-performing loan
- the loan has been restructured
- there was a material decrease in the collateral value
- there was a material decrease in the estimated future cash flows of the borrower
- there is an evident deterioration in the borrower's debt servicing capacity

The amount of impairment is measured as the difference between the carrying amount of the credit facility and the present value of estimated future cash flows, discounted at the credit facility's original effective interest rate. The estimated future cash flows will include any expected cash flows from the borrowers operations, any other sources of funds and the expected proceeds from the liquidation of collateral, where applicable.

(ii) Collectively assessed loans

For the assessment of collectively assessed loans, the Bank estimates loan impairment based on the following criteria:

- Credit facility type
- Collateral type
- Days in arrears
- Economic sectors

Based on the above criteria, the Bank creates the following groups for collective assessment and determines impairment provision rates, based on the banking sector financial information as provided by the NBG to the financial institutions.

The resulting collective provision rates are as follows:

- Mortgage loans: 0.96%
- Consumer loans: 3.38%
- Loans to employees: 2.37%
- Overdrafts: 6.27%
- Loans to small and medium size companies: 1.70%
- Corporate loans: 2%-7% considering the economic environment and market loss experience.

(c) Analysis of collateral and other credit enhancements**(i) Loans to legal entities**

Loans to legal entities are subject to individual credit appraisal and impairment testing. The general creditworthiness of a legal entity tends to be the most relevant indicator of credit quality of the loan extended to it. However, collateral provides additional security and the Bank generally requests corporate borrowers to provide it.

The following tables provides information on collateral and other credit enhancements securing loans to legal entities, net of impairment, by types of collateral:

31 December 2016 000'GEL	Loans to customers, carrying amount	Fair value of collateral assessed as of loan inception date
Loans to legal entities		
Loans to corporate customers		
Cash and deposits	134,336	134,336
Real estate	27,398	27,398
Total loans to corporate customers	161,734	161,734
Loans to small and medium size companies		
Cash and deposits	17	17
Real estate	10,150	10,150
Unsecured	396	-
Total loans to small and medium size companies	10,563	10,167
Total loans to legal entities	172,297	171,901

31 December 2015 000'GEL	Loans to customers, carrying amount	Fair value of collateral assessed as of loan inception date
Loans to legal entities		
Loans to corporate customers		
Cash and deposits	111,396	111,396
Real estate	22,199	22,199
Unsecured	4,400	-
Total loans to corporate customers	137,995	133,595
Loans to small and medium size companies		
Cash and deposits	695	695
Real estate	2,116	2,116
Total loans to small and medium size companies	2,811	2,811
Total loans to legal entities	140,806	136,406
31 December 2014 000'GEL	Loans to customers, carrying amount	Fair value of collateral assessed as of loan inception date
Loans to legal entities		
Loans to corporate customers		
Cash and deposits	53,605	53,605
Real estate	-	-
Total loans to corporate customers	53,605	53,605
Loans to small and medium size companies		
Real estate	13,853	13,853
Unsecured	43	-
Total loans to small and medium size companies	13,896	13,853
Total loans to legal entities	67,501	67,458

The tables above excludes overcollateralization. The fair value of collateral is updated as at the reporting date. Information on the valuation of collateral is based on when this estimate was made, if any.

For loans secured by multiple types of collateral, collateral that is most relevant for impairment assessment is disclosed. Sureties received from individuals, such as shareholders of small and medium size borrowers, are not considered for impairment assessment purposes. Accordingly, such loans and unsecured portions of partially secured exposures are presented as loans without collateral or other credit enhancement.

The recoverability of loans which are neither past due nor impaired primarily depends on the creditworthiness of borrowers rather than the value of collateral, and the Bank does not necessarily update the valuation of collateral as at each reporting date.

(ii) Loans to individuals

Mortgage loans and partly consumer loans are secured by the underlying real estate. The Bank's policy is to issue loans to individuals with a loan-to-value ratio at the date of loan issuance of a maximum of 70%.

The following tables provide information on real estate collateral securing loans to individuals, net of impairment:

31 December 2016 000'GEL	Loans to customers, carrying amount	Fair value of collateral assessed as of loan inception date
Loans to individuals		
Consumer loans		
Real estate	1,950	1,950
Other	75	75
Unsecured	3,289	-
Mortgage loans		
Real estate	2,053	2,053
Overdrafts		
Unsecured	122	-
Total loans individuals	7,489	4,078

31 December 2015 000'GEL	Loans to customers, carrying amount	Fair value of collateral assessed as of loan inception date
Loans to individuals		
Consumer loans		
Real estate	1,169	1,169
Unsecured	2,005	-
Mortgage loans		
Real estate	1,284	1,284
Overdrafts		
Unsecured	21	-
Total loans individuals	4,479	2,453

31 December 2014 000'GEL	Loans to customers, carrying amount	Fair value of collateral assessed as of loan inception date
Loans to individuals		
Consumer loans		
Unsecured	760	-
Mortgage loans		
Real estate	820	820
Overdrafts		
Unsecured	10	-
Total loans individuals	1,590	820

The tables above exclude overcollateralization.

For certain loans above the Bank updates the appraised values of collateral obtained at inception of the loan to the current values, taking into account the approximate changes in property values. The Bank may also obtain a specific individual valuation of collateral at each reporting date where there are indications of impairment. For the remaining loans the fair value of collateral was estimated at inception of the loans and was not adjusted for subsequent changes to the reporting date.

For overdrafts, there is no collateral or it is impracticable to determine the fair value of the collateral. Per management estimates recoverability of these loans is primarily dependent on the creditworthiness of the borrowers rather than the collateral.

(d) Industry and geographical analysis of the loan portfolio

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

	2016 000'GEL	2015 000'GEL	2014 000'GEL
Trade and service	49,509	42,039	46,769
Hospitality	82,323	65,970	13,660
Real estate	39,880	33,373	6,772
Agriculture	1,988	1,992	1,696
Loans to individuals	7,977	4,663	1,622
	181,677	148,037	70,519
Impairment allowance	(1,891)	(2,752)	(1,428)
	179,786	145,285	69,091

(e) Significant credit exposures

As at 31 December 2016 the Bank has eight borrowers or groups of connected borrowers (2015: eight; 2014: nine), whose loan balances exceed 10% of equity. The gross value of these loans as at 31 December 2016 is GEL 157,824 thousand (2015: GEL 128,372 thousand; 2014: GEL 66,965 thousand).

To comply with the NBG requirements, the Bank received deposits and borrowed funds from the Parent to finance the loans to eight borrowers (2015: eight; 2014: six), whose balances exceed 10% of equity. The gross value of these loans as at 31 December 2016 is GEL 157,824 thousand (2015: GEL 128,372 thousand; 2014: GEL 44,684 thousand). Deposits from customers and borrowed funds from the Parent have the same maturity as the loans to the borrowers mentioned above and are not payable unless the loans from the customers are repaid or the collateral is realized.

(f) Loan maturities

The maturity of the loan portfolio is presented in note 15 (f) which shows the remaining period from the reporting date to the contractual maturity of the loans. Due to the short-term nature of the loans issued by the Bank, it is likely that many of the loans will be renewed at maturity. Accordingly, the effective maturity of the loan portfolio may be significantly longer than the contractually agreed term.

11 Property, equipment and intangible assets

000'GEL	Leasehold improvements	Computers and office equipment	Furniture and fixtures	Motor vehicles	Intangible assets	Total
Cost						
Balance at 1 January 2016	2,095	513	344	168	729	3,849
Additions	30	259	-	(1)	-	288
Balance at 31 December 2016	2,125	772	344	167	729	4,137
Depreciation and amortization						
Balance at 1 January 2016	(531)	(159)	(101)	(59)	(168)	(1,018)
Depreciation and amortization for the year	(481)	(138)	(69)	(39)	(109)	(836)
Balance at 31 December 2016	(1,012)	(297)	(170)	(98)	(277)	(1,854)
Carrying amount						
At 31 December 2016	1,113	475	174	69	452	2,283
000'GEL						
	Leasehold improvements	Computers and office equipment	Furniture and fixtures	Motor vehicles	Intangible assets	Total
Cost						
Balance at 1 January 2015	1,254	285	221	103	543	2,406
Additions	841	228	123	65	186	1,443
Balance at 31 December 2015	2,095	513	344	168	729	3,849
Depreciation and amortization						
Balance at 1 January 2015	(206)	(89)	(54)	(27)	(79)	(455)
Depreciation and amortization for the year	(325)	(70)	(47)	(32)	(89)	(563)
Balance at 31 December 2015	(531)	(159)	(101)	(59)	(168)	(1,018)
Carrying amount						
At 31 December 2015	1,564	354	243	109	561	2,831

000'GEL	Leasehold improvements	Computers and office equipment	Furniture and fixtures	Motor vehicles	Intangible assets	Total
Cost						
Balance at 1 January 2014	378	174	98	103	425	1,178
Additions	876	111	123	-	118	1,228
Balance at 31 December 2014	1,254	285	221	103	543	2,406
Depreciation and amortization						
Balance at 1 January 2014	(77)	(46)	(24)	(6)	(13)	(166)
Depreciation and amortization for the year	(129)	(43)	(30)	(21)	(66)	(289)
Balance at 31 December 2014	(206)	(89)	(54)	(27)	(79)	(455)
Carrying amount						
At 31 December 2014	1,048	196	167	76	464	1,951

12 Deposits and balances from banks

	2016 000'GEL	2015 000'GEL	2014 GEL
Vostro accounts	1,047	2,800	2,397
Term deposits	172,837	123,424	6,535
	173,884	126,224	8,932

As at 31 December 2016 the Bank has two banks (2015: two banks; 2014: one bank), whose balances exceed 10% of equity. The gross value of these balances as at 31 December 2016 is GEL 173,884 thousand (2015: GEL 126,224 thousand; 2014: GEL 8,932 thousand).

The major part of term deposits was obtained from the Parent to be in compliance with NBG requirement, see note 10 (e).

13 Current accounts and deposits from customers

	2016 000'GEL	2015 000'GEL	2014 000'GEL
Current accounts and demand deposits			
- Retail	4,065	6,054	1,126
- SME	3,532	1,872	867
- Corporate	2,588	1,404	5,910
Term deposits			
- Retail	50,897	40,551	19,086
- SME	4,018	103	691
- Corporate	-	5,032	5,163
	65,100	55,016	32,843

As at 31 December 2016 the Bank maintained customer deposit balances of GEL 43,761 thousand (2015: GEL 35,085 thousand; 2014: GEL 18,636 thousand) that serve as collateral for loans granted by the Bank. As at 31 December 2016 the Bank has four customers (2015: six customers; 2014: seven customers), whose balances exceed 10% of equity. These balances as at 31 December 2016 are GEL 43,717 thousand (2015: GEL 46,031 thousand; 2014: GEL 29,913 thousand).

14 Other borrowed funds

	2016 000'GEL	2015 000'GEL	2014 000'GEL
Türkiye İş Bankası Anonim Şirketi	-	-	36,709

As at 2015 borrowings from the parent company Türkiye İş Bankası Anonim Şirketi was transferred and reclassified into deposits and balances from banks due to the regulatory requirements for the reorganization from the Branch into the Bank.

15 Risk management, corporate governance and internal control

(a) Corporate governance framework

The Bank is established as a bank in accordance with Georgian law. The supreme governing body of the Bank is the Supervisory Council. The Supervisory Council makes strategic decisions on the Bank's operations.

The Supervisory Council elects the Board of Directors. The Board of Directors is responsible for overall governance of the Bank's activities.

(b) Internal control policies and procedures

Management has responsibility for the development, implementation and maintaining of internal controls in the Bank that are commensurate with the scale and nature of operations.

The purpose of internal controls is to ensure:

- proper and comprehensive risk assessment and management
- proper business and accounting and financial reporting functions, including proper authorization, processing and recording of transactions
- completeness, accuracy and timeliness of accounting records, managerial information, regulatory reports, etc.
- reliability of IT-systems, data and systems integrity and protection
- prevention of fraudulent or illegal activities, including misappropriation of assets
- compliance with laws and regulations

Management is responsible for identifying and assessing risks, designing controls and monitoring their effectiveness. Management monitors the effectiveness of the Bank's internal controls and periodically implements additional controls or modifies existing controls as considered necessary.

Management believes that the Bank complies with the NBG requirements related to risk management and internal control systems, including requirements related to the internal audit function, and that risk management and internal control systems are appropriate for the scale, nature and complexity of operations.

(c) Risk management policies and procedures

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

The risk management policies aim to identify, analyze and manage the risks faced by the Bank, to set appropriate risk limits and controls, and to continuously monitor risk levels and adherence to limits. Risk management policies and procedures are reviewed regularly to reflect changes in market conditions, products and services offered and emerging best practice.

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

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

Credit, market and liquidity risks, both at the portfolio and transactional levels, are managed and controlled through a system of Credit Committees and Risk Management Division.

Both external and internal risk factors are identified and managed throughout the organization. Particular attention is given to identifying the full range of risk factors and determining the level of assurance over current risk mitigation procedures.

(d) Market risk

Market risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in market prices. Market risk comprises currency risk, interest rate risk and other price risks. Market risk arises from open positions in interest rate and equity financial instruments, which are exposed to general and specific market movements and changes in the level of volatility of market prices and foreign currency rates.

The objective of market risk management is to manage and control market risk exposures within acceptable parameters, while optimizing the return on risk.

The Bank manages its market risk by setting open position limits in relation to financial instruments, interest rate maturity and currency positions. These are monitored on a regular basis and reviewed and approved by management.

(i) Interest rate risk

Interest rate risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in market interest rates. The Bank is exposed to the effects of fluctuations in the prevailing levels of market interest rates on its financial position and cash flows. Interest margins may increase as a result of such changes, but may also reduce or create losses in the event that unexpected movements occur.

Interest rate gap analysis

Interest rate risk is managed principally through monitoring interest rate gaps. A summary of the interest gap position for major financial instruments is as follows:

000'GEL	Less than 3 months	3-6 months	6-12 months	1-5 years	More than 5 years	Carrying amount
31 December 2016						
ASSETS						
Cash and cash equivalents	44,098	-	-	-	-	44,098
Mandatory reserves at NBG	46,607	-	-	-	-	46,607
Held-to-maturity investments	-	-	-	1,018	-	1,018
Loans to customers	20,119	8,792	16,915	109,430	24,530	179,786
	110,824	8,792	16,915	110,448	24,530	271,509
LIABILITIES						
Accounts and deposits from banks	12,092	2,648	82,530	44,972	31,642	173,884
Current accounts and deposits from customers	14,064	120	7,156	43,760	-	65,100
Other borrowed funds	-	-	-	-	-	-
	26,156	2,768	89,686	88,732	31,642	238,984
	84,668	6,024	(72,771)	21,716	(7,112)	32,525
	Less than 3 months	3-6 months	6-12 months	1-5 years	More than 5 years	Carrying amount
31 December 2015						
ASSETS						
Cash and cash equivalents	38,889	-	-	-	-	38,889
Mandatory reserves at NBG	25,819	-	-	-	-	25,819
Loans to customers	10,663	11,939	20,305	76,668	25,710	145,285
	75,371	11,939	20,305	76,668	25,710	209,993
LIABILITIES						
Accounts and deposits from banks	3,041	8,167	53,668	11,557	49,791	126,224
Current accounts and deposits from customers	18,787	12,049	5,994	18,186	-	55,016
	21,828	20,216	59,662	29,743	49,791	181,240
	53,543	(8,277)	(39,357)	46,925	(24,081)	28,753

000'GEL	Less than 3 months	3-6 months	6-12 months	1-5 years	More than 5 years	Carrying amount
31 December 2014						
ASSETS						
Cash and cash equivalents	14,034	-	-	-	-	14,034
Mandatory reserves at NBG	5,436	-	-	-	-	5,436
Loans to customers	3,232	2,152	5,460	54,511	3,736	69,091
	22,702	2,152	5,460	54,511	3,736	88,561
LIABILITIES						
Deposits and balances from banks	8,932	-	-	-	-	8,932
Current accounts and deposits from customers	14,098	1,506	-	-	17,239	32,843
Other borrowed funds	1,525	1,881	4,270	27,790	1,243	36,709
	24,555	3,387	4,270	27,790	18,482	78,484
	(1,853)	(1,235)	1,190	26,721	(14,746)	10,077

Average effective interest rates

The table below displays average effective interest rates for interest-bearing assets and liabilities as at 31 December 2016, 2015 and 2014. These interest rates are an approximation of the yields to maturity of these assets and liabilities.

	2016			2015			2014		
	Average effective interest rate, %			Average effective interest rate, %			Average effective interest rate, %		
	GEL	USD	EUR	GEL	USD	EUR	GEL	USD	EUR
Interest bearing assets									
Cash and cash equivalents	6.9%	0.7%	-	8.8%	-	-	3.4%	0.5%	-
Held-to-maturity investments	6.7%	-	-	-	-	-	-	-	-
Loans to customers	12.8%	8.2%	10.0%	11.9%	10.8%	10.5%	8.7%	9.0%	-
Interest bearing liabilities									
Deposits and balances from banks	-	4.1%	-	-	3.9%	-	-	2.3%	-
Deposits from Customers	5.0%	4.3%	-	4.0%	6.4%	2.5%	4.5%	6.7%	-
Other borrowed funds	-	-	-	-	-	-	-	4.7%	-

Interest rate sensitivity analysis

The management of interest rate risk, based on an interest rate gap analysis, is supplemented by monitoring the sensitivity of financial assets and liabilities. An analysis of the sensitivity of net profit or loss and equity (net of taxes) to changes in interest rates (repricing risk), based on a simplified scenario of a 100 basis point (bps) symmetrical fall or rise in all yield curves and positions of interest-bearing assets and liabilities existing as at 31 December 2016, 2015 and 2014, is as follows:

	2016	2015	2014
	000'GEL	000'GEL	000'GEL
100 bps parallel fall	2	211	104
100 bps parallel rise	(2)	(211)	(104)

(ii) Currency risk

The Bank has assets and liabilities denominated in several foreign currencies.

Currency risk is the risk that the fair value or the future cash flows of a financial instrument will fluctuate because of changes in foreign currency exchange rates. The Bank constantly monitors that the NBG limits of currency positions against regulatory capital are maintained.

The following table shows the foreign currency exposure structure of financial assets and liabilities as at 31 December 2016:

	EUR	USD	TRY	GBP	Total
	000'GEL	000'GEL	000'GEL	000'GEL	000'GEL
ASSETS					
Cash and cash equivalents	605	39,477	219	284	40,585
Mandatory reserves at NBG	394	46,213	-	-	46,607
Loans to customers	233	147,853	-	-	148,086
Other financial assets	1	1,120	-	-	1,121
Total assets	1,233	234,663	219	284	236,399
LIABILITIES					
Deposits and balances from banks	193	173,408	-	283	173,884
Current accounts and deposits from customers	222	61,701	30	-	61,953
Other financial liabilities	-	105	-	-	105
Total liabilities	415	235,214	30	283	235,942
Net position	818	(551)	189	1	457

The following table shows the foreign currency exposure structure of financial assets and liabilities as at 31 December 2015:

	EUR 000'GEL	USD 000'GEL	TRY 000'GEL	GBP 000'GEL	Total 000'GEL
ASSETS					
Cash and cash equivalents	868	17,208	302	917	19,295
Mandatory reserves at NBG	296	25,523	-	-	25,819
Loans to customers	159	135,464	-	-	135,623
Other financial assets	-	10	-	-	10
Total assets	1,323	178,205	302	917	180,747
LIABILITIES					
Deposits and balances from banks	1,185	124,438	-	601	126,224
Current accounts and deposits from customers	27	53,419	11	-	53,457
Other financial liabilities	-	24	-	-	24
Total liabilities	1,212	177,881	11	601	179,705
Net position	111	324	291	316	1,042

The following table shows the currency structure of financial assets and liabilities as at 31 December 2014:

	EUR 000'GEL	USD 000'GEL	TRY 000'GEL	GBP 000'GEL	Total 000'GEL
ASSETS					
Cash and cash equivalents	942	7,041	490	-	8,473
Mandatory reserves at NBG	162	5,274	-	-	5,436
Loans to customers	-	61,257	-	-	61,257
Other financial assets	-	689	-	-	689
Total assets	1,104	74,261	490	-	75,855
LIABILITIES					
Accounts and deposits from banks	702	8,230	-	-	8,932
Current accounts and deposits from customers	5	29,445	35	-	29,485
Loans and borrowings	-	36,709	-	-	36,709
Other financial Liabilities	-	689	-	-	689
Total liabilities	707	75,073	35	-	75,815
Net position	397	(812)	455	-	40

A weakening of the GEL, as indicated below, against the following currencies at 31 December 2016, 2015 and 2014, would have increased (decreased) equity and profit or loss by the amounts shown below. This analysis is on a net-of-tax basis, and is based on foreign currency exchange rate variances that the Bank considered to be reasonably possible at the end of the reporting period. The analysis assumes that all other variables, in particular interest rates, remain constant.

	<u>2016</u> <u>000'GEL</u>	<u>2015</u> <u>000'GEL</u>	<u>2014</u> <u>000'GEL</u>
20% appreciation of USD against GEL	(94)	55	(138)
20% appreciation of EUR against GEL	139	19	67
20% appreciation of TRY against GEL	32	49	77
20% appreciation of GBP against GEL	-	54	-

A strengthening of the GEL against the above currencies at 31 December 2016, 2015 and 2014 would have had the equal but opposite effect on the above currencies to the amounts shown above, on the basis that all other variables remained constant.

(e) Credit risk

Credit risk is the risk of financial loss to the Bank if a customer or counterparty to a financial instrument fails to meet its contractual obligations. The Bank has policies and procedures in place to manage credit exposures (both for recognized financial assets and unrecognized contractual commitments), including guidelines to limit portfolio concentration and the establishment of a Credit Committee to actively monitor credit risk. The credit policy is reviewed and approved by management.

The credit policy establishes:

- procedures for reviewing and approving loan credit applications
- methodology for the credit assessment of borrowers (legal entities and individuals)
- methodology for the evaluation of collateral
- credit documentation requirements
- procedures for the ongoing monitoring of loans and other credit exposures

The Bank Credit Committee is authorized to make the final decision regarding financing or rejecting loan applications. The loans presented for approval are based on limits established by the credit policy. All loans are authorized by the Credit Committee first. The final decision authority for loans below USD 500,000 is the Bank Board of Directors, the loans above USD 500,000 and below USD 1,500,000 are authorized by the Parent Credit Committee and loans over USD 1,500,000 are authorized by the Supervisory Council of the Bank.

For all loans to legal entities the Bank performs due diligence that focuses on the customer's business and financial performance.

Exposure to credit risk is also managed, in part, by obtaining collateral and personal guarantees. Valuation of collateral is performed by independent experts for loans mentioned above.

The maximum exposure to credit risk is generally reflected in the carrying amounts of financial assets in the statement of financial position and unrecognized contractual commitment amounts. The impact of the possible netting of assets and liabilities to reduce potential credit exposure is not significant.

For the analysis of collateral held against loans to customers and concentration of credit risk in respect of loans to customers, see note 10.

The maximum exposure to credit risk from unrecognized contractual commitments at the reporting date is presented in note 17.

(f) Liquidity risk

Liquidity risk is the risk that the Bank will encounter difficulty in meeting obligations associated with its financial liabilities that are settled by delivering cash or another financial asset. 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 liquidity management. It is unusual for financial institutions ever to be completely matched, since business transacted is often of an uncertain term and of different types. An unmatched position potentially enhances profitability, but can also increase the risk of losses.

The Bank maintains liquidity management with the objective of ensuring that funds will be available at all times to honor all cash flow obligations as they become due. The liquidity policy is reviewed and approved by management.

The Bank seeks to actively support a diversified and stable funding base in order to be able to respond quickly and efficiently to unforeseen liquidity requirements.

The liquidity management policy requires:

- maintaining a diverse range of funding sources
- managing the concentration and profile of debts
- maintaining debt financing plans
- monitoring liquidity ratios against regulatory requirements

The liquidity position is monitored by the Finance Department and the Risk Management Division. Under the normal market conditions, information on the liquidity position is presented to the management on a weekly basis. Decisions on liquidity management are made by the Risk management Division and the Management and implemented by the Finance Department.

In addition, the Bank monitors on a regular basis the liquidity ratio calculated in accordance with the NBG requirements.

The following tables show the undiscounted cash flows on financial assets, liabilities and credit-related commitments on the basis of their earliest possible contractual maturity. The total gross inflow and outflow disclosed in the tables is the contractual, undiscounted cash flow on the financial assets, liability or credit related commitment. For issued financial guarantee contracts, the maximum amount of the guarantee is allocated to the earliest period in which the guarantee can be called.

The maturity analysis for financial liabilities as at 31 December 2016 is as follows:

000'GEL	Demand and less than 1 month	From 1 to 3 months	From 3 to 6 months	From 6 to 12 months	From 1 to 5 years	More than 5 years	Total gross amount inflow (outflow)	Carrying amount
Non-derivative liabilities								
Deposits and balances from banks	(2,644)	(9,500)	(2,712)	(84,691)	(54,368)	(42,264)	(196,179)	(173,884)
Current accounts and deposits from customers	(21,542)	(291)	(449)	(907)	(44,150)	-	(67,339)	(65,100)
Other borrowed funds	-	-	-	-	-	-	-	-
Other financial liabilities	(1,213)	-	-	-	-	-	(1,213)	(1,203)
Total financial liabilities	(25,399)	(9,791)	(3,161)	(85,598)	(98,518)	(42,264)	(264,731)	(240,187)
Credit related commitments	(10,207)	-	-	-	-	-	(10,207)	(10,207)

The maturity analysis for financial liabilities as at 31 December 2015 is as follows:

	Demand and less than 1 month	From 1 to 3 months	From 3 to 6 months	From 6 to 12 months	From 1 to 5 years	More than 5 years	Total gross amount inflow (outflow)	Carrying amount
000'GEL								
Non-derivative liabilities								
Deposits and balances from banks	(3,042)	-	(8,257)	(55,054)	(13,309)	(66,460)	(146,122)	(126,224)
Current accounts and deposits from customers	(13,645)	(9,031)	(11,242)	(11,603)	(11,559)	-	(57,080)	(55,016)
Other financial liabilities	(256)	-	-	-	-	-	(256)	(256)
Total financial liabilities	(16,943)	(9,031)	(19,499)	(66,657)	(24,868)	(66,460)	(203,458)	(181,496)
Credit related commitments	(5,310)	-	-	-	-	-	(5,310)	(5,310)

The maturity analysis for financial liabilities as at 31 December 2014 is as follows:

	Demand and less than 1 month	From 1 to 3 months	From 3 to 6 months	From 6 to 12 months	From 1 to 5 years	More than 5 years	Total gross amount inflow (outflow)	Carrying amount
000'GEL								
Non-derivative liabilities								
Deposits and balances from banks	(8,934)	-	-	-	-	-	(8,934)	(8,932)
Current accounts and deposits from customers	(13,422)	(696)	(2,027)	(494)	(7,585)	(17,238)	(41,462)	(32,843)
Other borrowed funds	(804)	(999)	(2,309)	(5,039)	(30,981)	(1,385)	(41,517)	(36,709)
Other financial liabilities	(689)	-	-	-	-	-	(689)	(689)
Total financial liabilities	(23,849)	(1,695)	(4,336)	(5,533)	(38,566)	(18,623)	(92,602)	(79,173)
Credit related commitments	(2,267)	-	-	-	-	-	(2,267)	(2,267)

Under Georgian law, individuals can withdraw their term deposits at any time, forfeiting in most of the cases the accrued interest. Accordingly, these deposits are shown in the table below in accordance with their stated maturity. The classification of these deposits in accordance with their stated maturity dates is presented below:

Demand and less than 1 month	2016	2015	2014
From 1 to 3 months	000'GEL	000'GEL	000'GEL
From 3 to 12 months	-	-	5,501
From 1 to 5 years	919	426	695
More than 5 years	3,677	2,184	1,506
	6,489	36,432	-
	42,349	-	17,238
	53,434	39,042	24,940

The table below shows an analysis, by expected maturities, of amounts recognized in the statement of financial position as at 31 December 2016:

000'GEL	Demand and less than 1 month	From 1 to 3 months	From 3 to 12 months	From 1 to 5 years	More than 5 years	No maturity	Total
ASSETS							
Cash and cash equivalents	44,098	-	-	-	-	-	44,098
Mandatory reserves at the NBG	46,607	-	-	-	-	-	46,607
Held-to-maturity investments	-	-	-	1,018	-	-	1,018
Loans to customers	8,036	12,083	25,707	109,430	24,530	-	179,786
Property, equipment and intangible assets	-	-	-	-	-	2,283	2,283
Other assets	2,258	-	-	-	-	-	2,258
Total assets	100,999	12,083	25,707	110,448	24,530	2,283	276,050
LIABILITIES							
Deposits and balances from banks	2,640	9,452	85,178	44,972	31,642	-	173,884
Current accounts and deposits from customers	13,191	873	7,276	43,760	-	-	65,100
Other borrowed funds	-	-	-	-	-	-	-
Other liabilities	1,203	-	-	-	-	-	1,203
Total liabilities	17,034	10,325	92,454	88,732	31,642	-	240,187
Net position	83,965	1,758	(66,747)	21,716	(7,112)	2,283	35,863

The table below shows an analysis, by expected maturities, of amounts recognized in the statement of financial position as at 31 December 2015:

000'GEL	Demand and less than 1 month	From 1 to 3 months	From 3 to 12 months	From 1 to 5 years	More than 5 years	No maturity	Total
ASSETS							
Cash and cash equivalents	38,889	-	-	-	-	-	38,889
Mandatory reserves at the NBG	25,819	-	-	-	-	-	25,819
Loans to customers	7,118	3,545	32,244	76,668	25,710	-	145,285
Property, equipment and intangible assets	-	-	-	-	-	2,831	2,831
Other assets	233	-	-	-	-	-	233
Total assets	72,059	3,545	32,244	76,668	25,710	2,831	213,057
LIABILITIES							
Deposits and balances from banks	3,041	-	61,835	11,557	49,791	-	126,224
Current accounts and deposits from customers	9,519	9,267	18,043	18,187	-	-	55,016
Other liabilities	280	-	-	-	-	-	280
Total liabilities	12,840	9,267	79,878	29,744	49,791	-	181,520
Net position	59,219	(5,722)	(47,634)	46,924	(24,081)	2,831	31,537

The table below shows an analysis, by expected maturities, of amounts recognized in the statement of financial position as at 31 December 2014:

000*GEL	Demand and less than 1 month	From 1 to 3 months	From 3 to 12 months	From 1 to 5 years	More than 5 years	No maturity	Total
ASSETS							
Cash and cash equivalents	14,034	-	-	-	-	-	14,034
Mandatory reserves at the NBG	5,436	-	-	-	-	-	5,436
Loans to customers	2,320	912	7,612	54,511	3,736	-	69,091
Property, equipment and intangible assets	-	-	-	-	-	1,951	1,951
Other assets	758	-	-	-	-	-	758
Total assets	22,548	912	7,612	54,511	3,736	1,951	91,270
LIABILITIES							
Deposits and balances from banks	8,932	-	-	-	-	-	8,932
Current accounts and deposits from customers	13,404	695	1,506	-	17,238	-	32,843
Other borrowed funds	804	720	6,153	27,790	1,242	-	36,709
Other liabilities	722	-	-	-	-	-	722
Total liabilities	23,862	1,415	7,659	27,790	18,480	-	79,206
Net position	(1,314)	(503)	(47)	26,721	(14,744)	1,951	12,064

(g) Operational risk

Operational risk is the risk of direct or indirect loss arising from a wide variety of causes associated with the Bank’s processes, personnel, technology and infrastructure, and from external factors other than credit, market and liquidity risks, such as those arising from legal and regulatory requirements and generally accepted standards of corporate behavior. Operational risks arise from all of the Bank’s operations.

The Bank’s objective is to manage operational risk so as to balance the avoidance of financial losses and damage to the Bank’s reputation with overall cost effectiveness and innovation. In all cases, the Bank policy requires compliance with all applicable legal and regulatory requirements.

The Bank manages operational risk by establishing internal controls that management determines to be necessary in each area of its operations.

16 Capital management

The National Bank of Georgia sets and monitors capital requirements for the Bank.

The Bank defines as capital those items defined by statutory regulation as capital for credit institutions. Under the current capital requirements set by the NBG, banks have to maintain a ratio of capital to risk weighted assets (statutory capital ratio) above the prescribed minimum level. As at 31 December 2016, this minimum level is 10.5 % (2015: 10.5%; 2014: 12%). The Bank is in compliance with the statutory capital ratio as at 31 December 2016, 2015 and 2014.

After the reorganization of the Branch into a Bank on 1 August 2015 the Bank registered its share capital.

The calculation of capital adequacy based on requirements set by the NBG as at 31 December is as follows:

000’GEL	2016	2015	2014
Statutory reserve/share capital	30,000	30,000	13,013
Retained earnings/(accumulated losses)	5,284	1,497	(807)
Total capital	35,284	31,497	12,206
Risk-weighted assets (unaudited)	160,843	118,717	48,178
Capital adequacy ratio (%) (unaudited)	22%	27%	25%

The risk-weighted assets are measured by means of a hierarchy of risk weights classified according to the nature and reflecting an estimate of credit, market and other risks associated with each asset and counterparty, taking into account any eligible collateral or guarantees.

17 Credit related commitments

The Bank has outstanding credit related commitments to extend loans. These credit related commitments take the form of overdraft facilities.

The Bank provides financial guarantees to guarantee the performance of customers to third parties. These agreements have fixed limits and generally extend for a period of up to five years.

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

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

	2016 000'GEL	2015 000'GEL	2014 000'GEL
Contracted amount			
Undrawn overdraft facilities	483	25	14
Guarantees	9,724	5,285	2,253
	<u>10,207</u>	<u>5,310</u>	<u>2,267</u>

The total outstanding contractual credit related commitments above do not necessarily represent future cash requirements, as these credit related commitments may expire or terminate without being funded.

Of these credit related commitments GEL 5,717 thousand are to four counterparties (2015: GEL 3,685 thousand to two counterparties; 2014: GEL 1,483 thousand to one counterparty). This exposure represents a significant credit risk exposure to the Bank.

18 Operating leases

(a) Leases as lessee

Non-cancellable operating lease rentals as at 31 December are payable as follows:

	2016 000'GEL	2015 000'GEL	2014 000'GEL
Less than 1 year	1,023	998	447
Between 1 and 5 years	2,361	2,823	1,267
	<u>3,384</u>	<u>3,821</u>	<u>1,714</u>

The Bank leases a number of premises and equipment under operating leases. The leases typically run for an initial period of five years, with an option to then renew the lease. Lease payments are usually increased annually to reflect market rentals. None of the leases includes contingent rentals.

19 Other assets

Other assets as at 31 December are as follows:

	2016 000'GEL	2015 000'GEL	2014 000'GEL
Receivables under litigation	1,072	-	-
Transit accounts for settlement systems	942	112	694
Other	244	121	64
	<u>2,258</u>	<u>233</u>	<u>758</u>

20 Other liabilities

Other liabilities as at 31 December are as follows:

	2016 000'GEL	2015 000'GEL	2014 000'GEL
Transit accounts for settlement systems	832	66	689
Provisions	194	106	-
Other	177	108	33
	1,203	280	722

21 Contingencies

(a) Insurance

The insurance industry in Georgia is in a developing state and many forms of insurance protection common in other parts of the world are not yet generally available.

The Bank has insured against business interruption and third-party liability in respect of damage arising from managerial decisions related to operations.

(b) Litigation

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

(c) Taxation contingencies

The taxation system in Georgia continues to evolve and is characterized by frequent changes in legislation, official pronouncements and court decisions, which are sometimes contradictory and subject to varying interpretation by different tax authorities. Taxes are subject to review and investigation by a number of authorities which have the authority to impose severe fines, penalties and interest charges. In the event of a breach of tax legislation, no liabilities for additional taxes, fines or penalties may be imposed by the tax authorities after three years have passed since the end of the year in which the breach occurred.

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

22 Related party transactions

(a) Control relationships

JSC Isbank Georgia is ultimately controlled by Isbank Members' Supplementary Pension Fund.

No publicly available financial statements are produced by the Bank's ultimate controlling party. However, such financial statements are produced by Türkiye İş Bankası Anonim Şirketi, which is an intermediate controlling party of the Bank.

(b) Transactions with the key management personnel

Total remuneration included in personnel expenses for the years ended 31 December 2016, 2015 and 2014 is as follows:

	2016 000'GEL	2015 000'GEL	2014 000'GEL
Short-term employee benefits	<u>1,217</u>	<u>725</u>	<u>812</u>

(c) Transactions with other related parties

Other related parties include the parent company.

The outstanding balances and related profit or loss amounts of transactions are as below:

000'GEL	The Parent 2016	The Parent 2015	The Parent 2014
Statement of financial position			
Assets			
Cash and cash equivalents			
- In TRY	142	158	478
- In EUR	9	-	-
- In USD	11	-	5,591
Liabilities			
Deposits and balances from banks			
- In EUR	192	1,187	702
- In USD	93,087	76,460	8,230
- In GBP	282	601	-
Other borrowed funds			
- In USD	-	-	36,709
Income/(expense)			
Interest expense	<u>(4,486)</u>	<u>(1,895)</u>	<u>(1,170)</u>

The deposits and balances from related parties mature according to contractual maturity as follows: GEL 14,739 thousand matures in less than 12 months, GEL 24,716 thousand during 1 to 5 years and GEL 54,679 thousand in more than 5 years.

Transactions with related parties are not secured.

The average effective interest rate on above deposit is 5.08 %.

23 Financial assets and liabilities: fair values and accounting classifications

(a) Accounting classifications and fair values

The estimates of fair value are intended to approximate the price that would be received to sell an asset, or paid to transfer a liability in an orderly transaction between market participants at the measurement date. However, given the uncertainties and the use of subjective judgment, the fair value should not be interpreted as being realizable in an immediate sale of the assets or transfer of liabilities.

Management believes that the fair value of financial assets and liabilities approximates their carrying amounts. The principles for determining fair values is disclosed in note 3c(v).

The estimated fair values of all financial assets and liabilities are calculated using discounted cash flow techniques based on estimated future cash flows and discount rates for similar instruments at the reporting date.

The objective of valuation techniques is to arrive at a fair value determination that reflects the price that would be received to sell the asset, or paid to transfer the liability in an orderly transaction between market participants at the measurement date.

The following assumptions are used by management to estimate the fair values of financial instruments:

- discount rates of 9.4 % to 16.9% are used for discounting future cash flows from loans to customers.
- a discount rate of 4.7% is used for discounting future cash flows from liabilities.

(b) Fair value hierarchy

The Bank measures fair values using the following fair value hierarchy, which reflects the significance of the inputs used in making the measurements:

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

24 Subsequent events

On 13 January 2017 the Company obtained the subordinated debt of GEL 42,348 thousand (USD 16,000 thousand) from the Parent. This loan for the purpose of the NBG regulation and reporting is included in the regulatory capital of the Bank. This will enable the Company to increase its lending limits.

25 New standards and interpretations not yet adopted

A number of new Standards, amendments to Standards and Interpretations are not yet effective as at 31 December 2016, and have not been applied in preparing these financial statements. Of these pronouncements, potentially the following will have an impact on the Company's operations. The Company plans to adopt these pronouncements when they become effective.

New or amended standard	Summary of the requirements	Possible impact on financial statements
IFRS 9 Financial Instruments	<p>IFRS 9, published in July 2014, replaces the existing guidance in IAS 39 Financial Instruments: Recognition and Measurement. IFRS 9 includes revised guidance on the classification and measurement of financial instruments, including a new expected credit loss model for calculating impairment on financial assets, and the new general hedge accounting requirements. It also carries forward the guidance on recognition and derecognition of financial instruments from IAS 39.</p> <p>IFRS 9 is effective for annual reporting periods beginning on or after 1 January 2018, with early adoption permitted.</p>	<p>The Company has not yet assessed the impact on financial statements resulting from the application of IFRS 9.</p>
IFRS 15 Revenue from Contracts with Customers	<p>IFRS 15 establishes a comprehensive framework for determining whether, how much and when revenue is recognised. It replaces existing revenue recognition guidance, including IAS 18 Revenue, IAS 11 Construction Contracts and IFRIC 13 Customer Loyalty Programmes.</p> <p>The core principle of the new standard is that an entity recognises revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. The new standard results in enhanced disclosures about revenue, provides guidance for transactions that were not previously addressed comprehensively and improves guidance for multiple-element arrangements.</p> <p>IFRS 15 is effective for annual reporting periods beginning on or after 1 January 2017, with early adoption permitted.</p>	<p>The Company has assessed that there is no significant impact on financial statements resulting from the application of IFRS 15.</p>
IFRS 16 Leases	<p>IFRS 16 replaces the existing lease accounting guidance in IAS 17 Leases, IFRIC 4 Determining whether an Arrangement contains a lease, SIC-15 Operating Leases – Incentives and SIC-27 Evaluating the Substance of Transactions Involving the Legal Form of a Lease. It eliminates the current dual accounting model for lessees, which distinguishes between on-balance sheet finance leases and off-balance sheet operating leases. Instead, there is a single, on-balance sheet accounting model that is similar to current finance lease accounting.</p> <p>Lessor accounting remains similar to current practice – i.e. lessors continue to classify leases as finance and operating leases.</p> <p>IFRS 16 is effective for annual reporting periods beginning on or after 1 January 2019, early adoption is permitted if IFRS 15 Revenue from Contracts with Customers is also adopted.</p>	<p>The Company has assessed that there is no significant impact on financial statements resulting from the application of IFRS 16.</p>
IAS 7 Statement of Cash Flows	<p>Disclosure Initiative (Amendments to IAS 7) requires disclosures that enable users of financial statements to evaluate changes in liabilities arising from financing activities, including both changes arising from cash flow and non-cash changes. The amendments are effective for annual periods beginning on or after 1 January 2017, with early adoption permitted.</p>	<p>The Company has assessed that there is no significant impact on financial statements resulting from the application of IAS 7.</p>