

JSC Isbank Georgia

Financial Statements

For the year ended 31 December 2022

Together with Independent Auditor's Report

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INDEPENDENT AUDITOR'S REPORT

To the Shareholders and Supervisory Council of JSC Isbank Georgia:

Opinion

We have audited the financial statements of JSC Isbank Georgia (hereinafter the "Bank"), which comprise the statement of financial position as at 31 December 2022, and the statement of profit or loss and other comprehensive income, statement of changes in equity and statement of cash flows for the year then ended, and notes to the financial statements, including a summary of significant accounting policies.

In our opinion, the accompanying financial statements present fairly, in all material respects, the financial position of the Bank as at 31 December 2022, 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 (ISA). Our responsibilities under those standards are further described in the *Auditor's Responsibilities for the Audit of the Financial Statements* section of our report.

We are independent of the Bank in accordance with the International Ethics Standards Board for Accountants' Code of Ethics for Professional Accountants (the "IESBA Code") together with the ethical requirements that are relevant to our audit of the financial statements in Georgia, and we have fulfilled our other ethical responsibilities in accordance with these requirements and the IESBA Code.

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

Other Information included in the Bank's Management Report

Management is responsible for the other information. Other information consists of the information included in the Bank's 2022 Management Report, other than the financial statements and our auditor's report thereon. The Bank's 2022 Management Report is expected to be made available to us after the date of this auditor's report.

Our opinion on the financial statements does not cover the other information and we do not express any form of assurance conclusion thereon in our report on the audit of the financial statements.

In connection with our audit of the financial statements, our responsibility is to read the other information identified above when it becomes available and, in doing so, consider whether the other information is materially inconsistent with the financial statements or is materially non-compliant with the requirements of the respective regulatory acts, or otherwise appears to be materially misstated based on our knowledge obtained in the audit. If we conclude that there is a material misstatement of this other information, we are required to report that fact.

Responsibilities of Management and the Audit Committee for the Financial Statement

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 Bank's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless management either intends to liquidate the Bank or to cease operations or has no realistic alternative but to do so.

The Audit Committee is responsible for overseeing the Bank's financial reporting process.

Auditor's 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 auditor's 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 ISA will always detect a material misstatement when it exists.

Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

As part of an audit in accordance with ISA, we exercise professional judgment and maintain professional scepticism 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 Bank's internal control.
- ▶ Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management.
- ▶ Conclude on the appropriateness of management's use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Bank's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's 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 auditor's report. However, future events or conditions may cause the Bank 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 Audit Committee 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.

Sophiko Ghudushauri, Engagement Partner (SARAS-A-835962)

Nexia TA LLC (SARAS-F-550338)

31 March 2023

Tbilisi, Georgia



Member of Nexia International

Auditor's 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 auditor's 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 ISA will always detect a material misstatement when it exists.

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As part of an audit in accordance with ISA, 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 Bank's internal control.
- ▶ Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management.
- ▶ Conclude on the appropriateness of management's use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Bank's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's 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 auditor's report. However, future events or conditions may cause the Bank 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.

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Sophiko Ghudushauri, Engagement Partner (SARAS-A-835962)

Nexia TA LLC (SARAS-F-550338)

31 March 2023

Tbilisi, Georgia

JSC Isbank Georgia
Statement of profit or loss and other comprehensive income
For the year ended 31 December 2022
(In thousands of GEL)

	Notes	2022	2021	2020
Interest income calculated using effective interest rate		29,780	22,365	19,388
Interest expense		(7,185)	(4,652)	(4,203)
Net interest income	5	22,595	17,713	15,185
Fee and commission income		3,238	3,414	2,846
Fee and commission expense		(1,395)	(1,694)	(1,055)
Net fee and commission income	6	1,843	1,720	1,791
Dealing		2,956	3,408	752
Translation differences		(1,057)	(1,885)	75
Net foreign exchange gain		1,899	1,523	827
Operating income		26,337	20,956	17,803
Net gains/(losses) from disposal of investment securities measured at fair value through other comprehensive income		(118)	-	-
Credit loss	7	(1,379)	(56)	(254)
Operating income after credit loss		24,840	20,900	17,549
Personnel expenses	8	(4,821)	(4,867)	(4,850)
Other income		-	70	-
Other expenses	9	(4,242)	(3,896)	(2,646)
Profit before income tax		15,777	12,207	10,053
Income tax expense	10	(3,264)	(1,626)	(378)
Profit for the year		12,513	10,581	9,675
Net change in fair value and expected credit losses for debt securities as fair value through other comprehensive income		485	(427)	608
Income tax effect on other comprehensive income	10	(82)	64	(91)
Net other comprehensive income/(loss) to be reclassified subsequently to profit or when specific conditions are met		403	(363)	517
Total comprehensive income for the year		12,916	10,218	10,192

The financial statements as set out on pages 5 to 66 were approved for issue and signed on behalf of the Management on 31 March 2023 by:

Hüseyin Emre Yılmaz
Chief Executive Officer

Ucha Saralidze
Chief Financial Officer

JSC Isbank Georgia
Statement of profit or loss and other comprehensive income
For the year ended 31 December 2022
(In thousands of GEL)

	Notes	2022	2021	2020
Interest income calculated using effective interest rate		29,780	22,365	19,388
Interest expense		(7,185)	(4,652)	(4,203)
Net interest income	5	<u>22,595</u>	<u>17,713</u>	<u>15,185</u>
Fee and commission income		3,238	3,414	2,848
Fee and commission expense		(1,395)	(1,694)	(1,058)
Net fee and commission income	6	<u>1,843</u>	<u>1,720</u>	<u>1,791</u>
Dealing		2,956	3,408	752
Translation differences		(1,057)	(1,685)	75
Net foreign exchange gain		<u>1,899</u>	<u>1,723</u>	<u>827</u>
Operating income		<u>26,337</u>	<u>20,956</u>	<u>17,803</u>
Net gains/(losses) from disposal of investment securities measured at fair value through other comprehensive income		(118)	-	-
Credit loss	7	(1,379)	(96)	(254)
Operating income after credit loss		<u>24,840</u>	<u>20,900</u>	<u>17,549</u>
Personnel expenses	8	(4,821)	(4,667)	(4,800)
Other income		-	70	-
Other expenses	9	(4,242)	(3,696)	(2,646)
Profit before income tax		<u>15,777</u>	<u>12,207</u>	<u>10,053</u>
Income tax expense	10	(3,284)	(1,628)	(378)
Profit for the year		<u>12,513</u>	<u>10,581</u>	<u>9,675</u>
Net change in fair value and expected credit losses for debt securities as fair value through other comprehensive income		485	(427)	608
Income tax effect on other comprehensive income	10	(82)	64	(91)
Net other comprehensive income(loss) to be reclassified subsequently to profit or when specific conditions are met		<u>403</u>	<u>(363)</u>	<u>517</u>
Total comprehensive income for the year		<u>12,916</u>	<u>10,218</u>	<u>10,192</u>

The financial statements as set out on pages 5 to 66 were approved for issue and signed on behalf of the Management on 31 March 2023 by:

Hüseyin Emre Yılmaz
Chief Executive Officer



Ucha Saralidze
Chief Financial Officer



The accompanying notes on pages 9 to 66 are an integral part of these Financial Statements.

JSC Isbank Georgia
Statement of Financial Position
As at 31 December 2022
(In thousands of GEL)

	Notes	2022	2021	2020
ASSETS				
Cash and cash equivalents	11	57,785	52,038	32,485
Amounts due from banks	12	-	8,745	9,190
Mandatory reserves at the National Bank of Georgia	13	39,030	38,427	36,217
Loans to customers	14	307,154	260,026	236,955
Investment securities	15	2,353	14,459	18,038
Property, equipment, intangible and Right-of-use assets	16	6,988	8,073	2,354
Other assets	17	3,342	4,250	4,749
Total assets		416,652	386,018	339,988
Liabilities				
Amounts due to banks	18	83,628	90,982	136,521
Amounts due to customers	19	147,975	105,234	75,820
Other borrowed funds	20	57,596	73,782	29,188
Deferred tax liabilities	10	764	1,002	1,264
Other liabilities	17	9,342	10,587	2,982
Total liabilities		299,305	281,587	245,775
Equity				
Share capital	21	69,162	69,162	69,162
Fair value reserve for investment securities		(87)	(490)	(127)
Retained earnings		48,272	35,759	25,178
Total equity		117,347	104,431	94,213
Total liabilities and equity		416,652	386,018	339,988

JSC Isbank Georgia
Statement of changes in equity
For the year ended 31 December 2022
(In thousands of GEL)

	Share capital	Fair value reserve for investment securities	Retained earnings	Total equity
Balances as at 31 December 2020	69,162	(127)	25,178	94,213
Profit for the year	-	-	10,581	10,581
Other comprehensive income for the year	-	(363)	-	(363)
Total comprehensive income for the year	-	(363)	10,581	10,218
Balances as at 31 December 2021	69,162	(490)	35,759	104,431
Profit for the year	-	-	12,513	12,513
Other comprehensive loss for the year	-	403	-	403
Total comprehensive income for the year	-	403	12,513	12,916
Balances as at 31 December 2022	69,162	(87)	48,272	117,347

JSC Isbank Georgia
Statement of cash flows
For the year ended 31 December 2022
(In thousands of GEL)

	Notes	2022	2021	2020
Cash flows from operating activities				
Profit before income tax		15,777	12,207	10,053
<i>Adjustment for:</i>				
Depreciation and amortization	16	1,234	1,281	1,269
Interest income calculated using effective interest rate	5	(29,780)	(22,365)	(19,388)
Interest expense	5	7,185	4,652	4,203
Impairment loss	7	1,379	56	254
Loss from disposal of PPE	16	(85)	360	-
Net foreign exchange gain		(1,899)	(1,523)	(827)
Cash flows used from operating activities before changes in operating assets and liabilities				
		(6,189)	(5,332)	(4,436)
Decrease/(increase) in mandatory reserves at the National Bank of Georgia		(7,950)	(6,062)	(3,554)
Decrease/(increase) in amounts due from banks		286	(3,884)	(1,886)
Decrease/ (increase) in loans to customers		(77,084)	(38,887)	(57,999)
Decrease/ (increase) in other assets		1,426	2,342	(3,846)
Increase/(decrease) in deposits and balances from banks		11,427	(31,726)	(26,919)
(Decrease)/ Increase in current accounts and deposits from customers		58,605	36,553	33,612
(Decrease)/ increase in other liabilities		(2,915)	225	77
Cash flows (used in)/from operations before interest and tax				
		(22,394)	(46,771)	(64,951)
Interest receipts		29,279	23,108	18,497
Interest payments		(6,847)	(4,431)	(4,210)
Income tax paid		-	(96)	(981)
Cash flows (used in) / from operations				
		38	(28,190)	(51,645)
Cash flows from investing activities				
Purchases of investment securities		(3,210)	(19,610)	(6,501)
Receipts from investment securities		14,753	22,088	23,997
Purchases of property, equipment and intangible assets	16	(64)	(464)	(1,082)
Cash flows from / (used in) investing activities				
		11,479	2,014	16,414
Cash flows from financing activities				
Receipts from other borrowed funds	20	8,653	51,831	16,219
Repayments of other borrowed funds	20	(13,287)	(4,771)	(4,875)
Repayments of principal portion of lease liabilities		(801)	(955)	(1,003)
Cash flows from / (used in) financing activities				
		(5,435)	46,105	10,341
Net increase/(decrease) in cash and cash equivalents				
		6,082	19,929	(24,890)
Effect of changes in exchange rates and expected credit losses on cash and cash equivalents		(335)	(376)	362
Cash and cash equivalents as at the beginning of the year	11	52,038	32,485	57,013
Cash and cash equivalents as at the end of the year	11	57,785	52,038	32,485

1 Principal Activities

(a) Organization and operations

JSC Isbank Georgia (hereinafter the “Bank”) is a joint stock company, incorporated on 29 June 2015 in accordance with legislation of Georgia. The Bank operates under a general banking license (N: 368) issued by the National Bank of Georgia (“NBG”) on 1 August 2015. The Bank is registered by the LEPL National Agency of Public Registry and the registration number is 404496611.

Before reorganization (1 August 2015) the Bank was presented as Batumi Branch of JSC Isbank Turkey (the “Branch”) registered on 13 July 2012 by the National Bank of Georgia (License N: 908) as a branch of a foreign bank Türkiye İş Bankası Anonim Şirketi (the “Parent” or the “Shareholder”) which was incorporated in Turkey in 1924.

The Bank’s principal activities include the following: accepts deposits from the public and provide credit, transfers payments in Georgia as well as abroad, exchanges currencies and provides other banking services to its commercial and retail customers. Main office of the Bank is in Tbilisi, Georgia and as at 31 December 2022, 31 December 2021 and 31 December 2020 it has two branches located in Tbilisi and Batumi.

The Bank’s registered legal address is 72a Ilia Chavchavadze Avenue, Tbilisi, Georgia.

As at 31 December 2022, 2021 and 2020 the Bank’s 100% shareholder was JSC Isbank Turkey.

As of December 31, 2022, 37.31% of the JSC Isbank Turkey shares are owned by T. İş Bankası A.Ş. Supplementary Pension Fund (Fund), 28.09% are owned by the Republican People’s Party- CHP (Atatürk’s shares) and 34.60% are on free float (December 31, 2021: Fund 37.26%, CHP 28.09%, Free float 34.65%, December 31, 2020: Fund 37.08%, CHP 28.09%, Free float 34.83%).

The Bank is ultimately controlled by Is bank Turkey member’s Supplementary Pension Fund. Related party transactions are disclosed in Note 25.

(b) 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.

2022 was a challenging year. As the region was recovering from the impact of the Covid-19 pandemic, it was hit by another major shock – Russia’s war in Ukraine. However the Georgian economy has demonstrated resilience thanks to a safe and business-friendly environment and its convenient geographical location.

According to the preliminary data of 2022, the volume of gross domestic product at current prices is GEL 71,754.2 million or USD 24,610.2 mln (2021 – GEL 60,003.3 or USD 18,629.20) which is 19.6 percent higher than the corresponding indicator of the previous year, and the growth of the real gross domestic product in 2022, compared to the previous year, amounted to 10.1 percent. The percentage change in the GDP Deflator in 2022 was set at 8.6 percent. The GDP per Capita Amounted USD 6,671.9 (2021 – USD 5,023.2)

According to preliminary data, the volume of direct foreign investments(FDI) made in Georgia in 2022 amounted to 2 billion US dollars, which is 61.1 percent higher than the adjusted data of 2021 – USD 1.2 bln. The growth is due to the increase of two components of direct foreign investments - share capital (USD 686 mln) and reinvestment (USD 1,289 mln).

In 2022, the external trade turnover was 19,042.9 million. USD, which is 32.8 percent more than the previous year. Out of mentioned volume USD 5 592.8 mln. is export (increased by 31.8 percent) and imports amount to 13,450.1 million. USD (increased by 33.2 percent). The negative trade balance of Georgia in 2022 amounted USD 7,857.2 mln. which is 41.3 percent of foreign trade turnover.

In 2022, the share of the ten largest export partner countries in the total export of Georgia amounted to 78.6 percent. The top three exporters were formed as follows: China (US\$ 736.8 million), Azerbaijan (US\$ 672.6 million) and Russia (US\$ 651.6 million).

1. Principal Activities (continued)

In 2022, the share of the ten largest import partner countries in the total import of Georgia amounted to 67.5 percent. The top three countries include: Turkiye (2,370.9 million US dollars), Russia (1,835.4 million US dollars) and China (1,126.0 million US dollars).

In 2022 Net money transfers amounted USD 4bln having growth by 98% compared to 2021 – USD 2bln.

In 2022 International tourism revenue amounted USD 3.5 bln having growth by 182% compared to 2021 – USD 1.2bln.

Inflation amounted 9.80% in December 2022 and averaging at 11.90% for the full year 2022.

In response to persistent price pressures, the National Bank of Georgia (NBG) maintained tight monetary policy with the refinancing rate at 11.0% since March 2022, having gradually increased the rate by 300 bps since March 2021. Given the tight monetary policy and strong external inflows, GEL strengthened against the US dollar by 12.5% in 2022. The strong external sector also enabled the NBG to accumulate international reserves, which amounted to US\$ 4.9 billion at 31 December 2022.

The strong economic activity recorded in 2021-2022 is expected to be sustained in 2023, however, the growth momentum is likely to slow due to the base effect. According to the IMF 2023 Projected Real GDP growth is 4.0%, Expected change in Consumer Prices is 5.90%.

War in Ukraine and related developments and consequent sanctions imposed on Russia is expected to have an adverse impact on the Georgian economy. On the upside, the lasting impact of migration, stronger tourism inflows and higher investment spending could deliver higher-than-expected growth.

2 Basis of preparation

(c) 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 two preceding periods – years ended 31 December 2021 and 2020. The Bank's management considers such disclosure more useful and informative for the stakeholders of the Bank.

These financial statements have not yet been approved by the Parent on the general meeting of shareholders of the Bank. The shareholders have the power and authority to amend the financial statements after the issuance.

(d) Basic measurement

The financial statements are prepared on the historical cost convention, except for investment securities, that are measured at fair value, or otherwise stated.

(e) Presentation of financial statements

The Bank presents its statement of financial position in order of liquidity based on the Bank's intention and perceived ability to recover/settle the majority of assets /liabilities of the corresponding financial statement line items. Analysis regarding recovery or settlement within 12 months after the reporting date (current) and more 12 months after the reporting date (non-current) is presented in Note 22.

(f) Functional and presentation currency

The national currency of Georgia is the Georgian Lari ("GEL" or "ლ"), which is the Bank's functional and presentation currency. These financial statements are presented in thousands of Georgian Lari ("ლ") except where otherwise stated.

(g) Going Concern

The Management of JSC Isbank Georgia has prepared these financial statements on a going concern basis. In making this judgment the management considered the Bank's strong financial position, current intentions, profitability of operations and access to financial resources. The management is not aware of any material uncertainty that may cast significant doubt on the Bank's ability to continue as going concern.

3 Summary of Significant Accounting Policies

Functional and Presentation currency, Foreign Currency Translation

The financial statements are presented in Georgian Lari (ლ), which is the Bank's functional currency and presentation currency. Transactions in foreign currencies are initially recorded in the functional currency, converted at the rate of exchange ruling at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies at the reporting date are retranslated into the functional currency at the official exchange rate set by the National Bank of Georgia at the reporting date. Gains or losses resulting from the translation of foreign currency transactions are recognized in the statement of profit or loss as gains less losses from foreign currencies – translation differences. 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.

The exchange rates used by the Bank in the preparation of the financial statements as at 31 December 2022, 31 December 2021 and 31 December 2020 are as follows:

	2022	2021	2020
1 US Dollar / ლ	2.7020	3.0976	3.2766
1 Euro / ლ	2.8844	3.5040	4.0233
1 TRY / ლ	0.1443	0.2379	0.4462
1 GBP / ლ	3.2581	4.1737	4.4529

Determination of fair value

The Bank measures financial instruments carried at Fair value through profit or loss (FVPL) and Fair value through other comprehensive income (FVOCI) at fair value at each balance sheet date.

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

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

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

In order to show how fair values have been derived, financial instruments are classified based on a fair value hierarchy, as summarised below:

- ▶ Level 1 financial instruments - those where the inputs used in the valuation are unadjusted quoted prices from active markets for identical assets or liabilities that the bank has access to the measurement date. The bank considers markets as active only if there are sufficient trading activities with regards to the volume and liquidity of the identical assets or liabilities and when there are binding and exercisable price quotes available on the balance sheet date;
- ▶ Level 2 financial instruments - those where the inputs that are used for valuation and are significant, are derived from directly or indirectly observable market data available over the entire period of the instrument's life. Such inputs include quoted prices for similar assets or liabilities in active market, quoted prices such as interest rates yield curves, implied volatilities, and credit spreads. In addition, adjustments may be required for the condition or location of the asset or the extent to which it relates to items that are comparable to the valued instrument. However, if such adjustments are based on unobservable inputs which are significant to the entire measurement, the Bank will classify the instruments as level 3.
- ▶ Level 3 financial instruments - those that include one or more unobservable inputs that is significant to the measurement as whole.

3. Summary of Significant Accounting Policies (continued)

The Bank periodically reviews its valuation techniques including the adopted methodologies and model calibrations. However, the base models may not fully capture all factors relevant to the valuation of the Bank's financial instruments such as credit risk (CVA), own credit (DVA) and /or funding costs (FVA). Therefore, the Bank applies various techniques to estimate the credit risk associated with its financial instruments measured at fair value, which include a portfolio-based approach that estimates the expected net exposure per counterparty over the full lifetime of the individual assets, in order to reflect the credit risk of the individual counterparties for non-collateralised financial instruments.

The Bank evaluates the levelling at each reporting period on an instrument-by-instrument basis and reclassifies instruments when necessary, based on the facts at the end of reporting period.

Income and expense recognition

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

Interest and similar income and expense

Under IFRS 9, interest income is recorded using the EIR method for all financial assets measured at amortised cost. Interest income on interest bearing financial assets measured at FVOCI under IFRS 9 is also recorded using the EIR method. Interest expense is also calculated using the EIR method for all financial liabilities held at amortised cost. The EIR is the rate that exactly discounts estimated future cash receipts through the expected life of the financial assets or liabilities, or, when appropriate, a shorter period, to the gross carrying amount of the financial asset. The EIR (and therefore, the amortised cost of the financial asset) is calculated by taking into account transaction costs

Income and expense recognition (continued)

and any discount or premium on the acquisition of the financial assets, as well as fees and costs are an integral part of the EIR. The Bank recognises interest income using a rate of return that represents the best estimate of a constant rate of return over the expected life of the loan. Hence, the EIR calculation also takes into account the effect of potentially different interest rates that may be charged at various stages of the financial asset's expected life, and other characteristics of the product life cycle (including prepayments, penalty interest and charges).

If expectations of fixed rate financial assets or liabilities cash flows are revised for reasons other than credit risk, than changes to future contractual cash flows are discounted at the original EIR with a consequential adjustment to the carrying amount. The difference from the previous carrying amount is booked as a positive or negative adjustment to the carrying amount of the financial asset or liability on the balance sheet with a corresponding increase or decrease in interest revenue/ expense calculated using the effective interest method.

When a financial asset becomes credit-impaired, the Bank calculates interest revenue by applying the effective interest rate to the net amortised cost of the financial asset. If the financial asset cures and is no longer credit impaired, the Bank reverts to calculating interest revenue on a gross basis.

For purchased or originated credit-impaired (POCI) financial assets, the Bank calculates interest revenue by calculating the credit-adjusted EIR and applying that rate to the amortised cost of the asset. The credit-adjusted EIR is the interest rate that, at original recognition, discounts the estimated future cash flows (including credit losses) to the amortised cost of the POCI assets.

Fee and commission income

The Bank earns fee and commission income from a diverse range of financial services it provides to its customers. Fee and commission income is recognised at an amount that reflects the considerations to which the Bank expects to be entitled in exchange for providing services.

- *Fee income earned from services provided over a certain period of time*

Fees earned for the provision of services over a period of time are accrued over that period as respective performance obligations are satisfied. 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 revenue over the estimated life of the financial instrument using the effective interest method.

- *Fee income earned at a point in time*

Other fees, commissions and other income and expense items are recognized in profit or loss when the

3. Summary of Significant Accounting Policies (continued)

corresponding service is provided. Each operation is treated as a separate performance obligation.

Retirement and other benefit obligations

The Bank does not have any pension arrangements separate from the state pension system of Georgia. In addition, the Bank has no post-retirement benefits.

Financial instruments

Initial recognition

The classification of financial instruments at initial recognition depends on their contractual terms and the business model for managing the instruments. Financial instruments are initially measured at their fair value and, except in the case of financial assets and financial liabilities recorded at FVPL, transaction costs are added to, or subtracted from this amount. The Bank determines the classification of its financial assets upon initial recognition and subsequently can reclassify financial assets in certain cases as described below.

Classification and measurement

Measurement categories of financial assets and liabilities.

The Bank classifies all of its financial assets based on the business model for managing the assets and the asset's contractual terms, measured at either:

Financial instruments (continued)

- ▶ Amortised cost;
- ▶ FVOCI;
- ▶ FVPL.

The Bank classifies and measures its derivative and trading portfolio at FVPL. The Bank may designate financial instruments at FVPL, if so doing eliminates or significantly reduces measurement or recognition inconsistencies.

Financial liabilities, other than loan commitments and financial guarantees, are measured at amortised cost or at FVPL when they are held for trading, are derivative instruments or the fair value designation is applied.

The Bank only measures amounts due from banks, loans to customers and other financial investments at amortized cost if both of the following conditions are met:

- ▶ The financial asset is held within a business model with the objective to hold financial assets in order to collect contractual cash flows;
- ▶ The contractual terms of the financial asset give rise on specified dates to cash flows that are solely payments of principal and interest on the principal amount outstanding (SPPI).

The corporate bonds represent debt securities issued by the legal entities, which the Bank intends to hold until maturity. They are measured at amortised cost and recognized within loans to customers section in the statement of financial position.

Business model assessment

The Bank determines its business model at the level that best reflects how it manages groups of financial assets to achieve its business objective.

The Bank's business model is not assessed on an instrument-by-instrument basis, but at a higher level of aggregated portfolios and is based on observable factors such as:

- ▶ How the performance of the business model and the financial assets held within that business model are evaluated and reported to the entity's key management personnel;
- ▶ The risks that affect the performance of the business model (and the financial assets held within that business model) and, in particular, the way those risks are managed;
- ▶ How managers of the business are compensated (for example, whether the compensation is based on the fair value of the assets managed or on the contractual cash flows collected);

3 Summary of Significant Accounting Policies (continued)

- ▶ The expected frequency, value and timing of sales are also important aspects of the Bank's assessment.

The business model assessment is based on reasonably expected scenarios without taking 'worst case' or 'stress case' scenarios into account. If cash flows after initial recognition are realized in a way that is different from the Bank's original expectations, the Bank does not change the classification of the remaining financial assets held in that business model, but incorporates such information when assessing newly originated or newly purchased financial assets going forward.

The SPPI test

As a second step of its classification process the Bank assesses the contractual terms of financial asset to identify whether they meet the SPPI test.

'Principal' for the purpose of this test is defined as the fair value of the financial asset at initial recognition and may change over the life of the financial asset (for example, if there are repayments of principal or amortization premium/discount).

The most significant elements of interest within a lending arrangement are typically the consideration for the time value of money and credit risk. To make the SPPI assessment, the Bank applies judgement and considers relevant factors such as the currency in which the financial asset is denominated, and the period for which the interest rate is set. In contrast, contractual terms that introduce a more than de Minimis exposure to risks or volatility in the contractual cash flows that are unrelated to a basic lending arrangement do not give rise to contractual cash flows that are solely

Financial instruments (continued)

payments of principal and interest on the amount outstanding. In such cases, the financial asset is required to be measured at FVPL.

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.

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 Debt instruments at FVOCI.

The Bank applies the new category under IFRS 9 of debt instruments measured at FVOCI when both of the following conditions are met:

- ▶ The instrument is held within a business model, the objective of which is achieved by both collecting contractual cash flows and selling financial assets;
- ▶ The contractual terms of the financial asset meet the SPPI test.

FVOCI debt instruments are subsequently measured at fair value with gains and losses arising due to changes in fair value recognised in OCI. Interest revenue and foreign exchange gains and losses are recognised in profit or loss in the same manner as for financial assets measured at amortised cost. On derecognition, cumulative gains or losses previously recognised in OCI are reclassified from OCI to profit or loss.

The ECLs for debt instruments measured at FVOCI do not reduce the carrying amount of these financial assets in the statement of financial position, which remains at fair value. Instead, an amount equal to the allowance that would arise if the assets were measured at amortised cost is recognised in OCI as an accumulated impairment amount, with a corresponding charge to profit or loss. The accumulated loss recognised in OCI is recycled to the profit and loss upon derecognition of the asset.

Financial guarantees, letters of credit and undrawn loan commitments

The Bank issues financial guarantees, letter of credit and loan commitments.

Financial guarantees are initially recognised in the financial statements at fair value, being the premium received. Subsequent to initial recognition, the Bank's liability under each guarantee is measured at the higher of the amount initially recognised less cumulative amortisation recognised in the consolidated statement of profit or loss, and an ECL provision.

3 Summary of Significant Accounting Policies (continued)

Undrawn loan commitments and letters of credits are commitments under which, over the duration of the commitment, the Bank is required to provide a loan with pre-specified terms to the customer. Similar to financial guarantee contracts these contracts are in the scope of the ECL requirements.

Reclassification of financial assets and liabilities

The Bank does not reclassify its financial assets subsequent to their initial recognition, apart from the exceptional circumstances in which the Bank changes the business model for managing financial assets. Financial liabilities are never reclassified.

Staged approach to the determination of expected credit losses

IFRS 9 introduced a three-stage approach to impairment for financial instruments that are performing at the date of origination or purchase. This approach is summarised as follows:

- ▶ Stage 1: The Bank recognises a credit loss allowance at an amount equal to 12-month expected credit losses. This represents the portion of lifetime expected credit losses from default events that are expected within 12 months of the reporting date, assuming that credit risk has not increased significantly after initial recognition. For those financial assets with a remaining maturity of less than 12 months, a PD is used that corresponds to the remaining maturity;

Financial instruments (continued)

- ▶ Stage 2: The Bank recognises a credit loss allowance at an amount equal to lifetime expected credit losses (LTECL) for those financial instruments which are considered to have experienced a significant increase in credit risk since initial recognition. This requires the computation of ECL based on lifetime probability of default (LTPD) that represents the probability of default occurring over the remaining lifetime of financial instrument. Allowance for credit losses are higher in this stage because of an increase in credit risk and the impact of a longer time horizon being considered compared to 12 months in Stage 1. Financial instruments in stage 2 are not yet deemed to be credit-impaired;
- ▶ Stage 3: If the financial instrument is credit-impaired, it is then moved to stage 3. The Bank recognise a loss allowance at an amount equal to lifetime expected credit losses, reflecting a Probability of Defaults (PD) of 100% for financial instruments that are credit-impaired.

Financial instruments within the scope of the impairment requirement of IFRS 9 are classified into one of the above three stages.

Key judgment and estimates used under IFRS 9 are disclosed in NOTE 4.

Cash and cash equivalents

Cash and cash equivalents are items which are readily convertible to known amounts of cash and are subject to an insignificant risk of changes in value. Cash and cash equivalents include notes and coins on hand, amounts due from National Bank of Georgia (NBG), excluding mandatory reserves, and other highly liquid financial assets with original maturities of less than three month. Cash and cash equivalent are carried at amortised cost.

Amounts due from banks

Amounts due from banks are recorded when the Bank advances money to counterparty banks. Amounts due from banks are initially recognized at fair value and are subsequently measured at amortized cost (AC) using the effective interest method when: they are held for the purposes of collecting contractual cash flows and cash flows represent SPPI, and they are not designated at FVTPL. Otherwise they are carried at Fair value (FV). Amounts due from banks are carried net of any allowances for impairment losses.

Mandatory reserve with National Bank of Georgia (NBG)

Mandatory reserves with NBG, as financial assets are carried at amortised cost and represent mandatory reserve deposits that are not available to finance the Bank's day-to-day operations.

Investments securities

Investment securities include Government bonds. The Bank classifies investment securities as carried at AC or FVOCI. Securities are carried at AC if they are held for collection of contractual cash flows and where those cash flows represent

3 Summary of Significant Accounting Policies (continued)

SPPI. Securities are carried at FVOCI if they are held for collection of contractual cash flows and for selling, where those cash flows represent SPPI, and if they are not designated at FVTPL. Interest income from these assets is calculated using the effective interest method and recognised in profit or loss for the year. All other changes in the carrying value are recognised in OCI. When the security are derecognised, the cumulative gain or loss previously recognised in OCI is classified from OCI to profit or loss.

Derivative financial instruments

In the normal course of business, the Bank enters into various derivative financial instruments including, forwards, swaps and options in the foreign exchange and capital markets. Such financial instruments are held for trading and are recorded at fair value. The fair values are estimated based on quoted market prices or pricing models that take into account the current market and contractual prices of the underlying instruments and other factors. Derivatives are carried as assets when their fair value is positive and as liabilities when it is negative. Gains and losses resulting from these instruments are included in the statement of profit or loss as net gains/ (losses) from financial instruments at fair value through profit or loss or net gains/ (losses) from foreign currencies dealing, depending on the nature of the instrument.

Financial instruments (continued)

Borrowings

Issued financial instruments or their components are classified as liabilities, where the substance of the contractual arrangement results in the Bank having an obligation either to deliver cash or another financial asset to the holder, or to satisfy the obligation other than by the exchange of a fixed amount of cash or another financial asset for a fixed number of own equity instruments. Such instruments include amounts due to credit institutions, amounts due to customers, debt securities issued. After initial recognition, borrowings are subsequently measured at amortised cost using the effective interest method. Gains and losses are recognised in the statement of profit or loss when the borrowings are derecognised as well as through the amortisation process. If the Bank purchases its own debt, it is removed from the statement of financial position and the difference between the carrying amount of the liability and the consideration paid is recognised in the statement of profit or loss.

Amounts due to customers

Amounts due to customers are non-derivative liabilities to individuals or corporate customers and are carried at AC.

Derecognition of financial assets and liabilities

Financial assets

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.

Write-off

Financial assets are written off either partially or in their entirety only when the Bank has stopped pursuing the recovery. If the amount to be written off is greater than the accumulated loss allowance, the difference is first treated as an addition to the allowance that is then applied against the gross carrying amount. Any subsequent recoveries are credited to credit loss expense. A write-off constitutes a derecognition event.

Once the loan is in overdue, the problematic debt collection process is started. The loan is transferred to problem asset manager, who is trying to contact the borrower and find a solution for covering the loan. If there is no any result within the 90 days, court actions are undertaken, which may last for 3 or 4 years, including all steps of the process.

The management believes that around 4 years are needed to conclude that there is no reasonable expectation of recovery and the asset should be written off.

Financial liabilities

A financial liability is derocognised when the obligation under the liability is discharged or cancelled or expires. Where an existing financial liability is replaced by another from the same lender on substantially different terms, or the terms of an existing liability are substantially modified, such an exchange or modification is treated as a derecognition

3 Summary of Significant Accounting Policies (continued)

of the original liability and the recognition of a new liability, and the difference in the respective carrying amounts is recognized in profit or loss.

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. The right of set-off must not be contingent on a future event and must be legally enforceable in all of the following circumstances:

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

Financial instruments (continued)

Impairment of financial assets.

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

The bank applies a three stage model for impairment, based on changes in credit quality since initial recognition:

- ▶ Stage 1: A financial instrument that is not credit-impaired on initial recognition is classified in Stage 1. Financial assets in Stage 1 have their ECL measured at an amount equal to the portion of lifetime ECL that results from default events possible within the next 12 months or until contractual maturity, if shorter ("12 Months ECL").
- ▶ Stage 2: If the bank identifies a significant increase in credit risk ("SICR") since initial recognition, the asset is transferred to Stage 2 and its ECL is measured based on ECL on a lifetime basis ("Lifetime ECL"). If a SICR is no longer observed, instrument will move back to Stage 1.
- ▶ Stage 3: Credit impaired assets are transferred to Stage 3 and allowance for Lifetime ECL is recognized. The bank's definition of credit impaired assets and definition of default is based on the occurrence of one or more loss events. Change in ECL is recognized in statement of profit or loss with a corresponding allowance reported as a decrease in carrying value of the financial asset on the statement of financial position. described further in Note 22.

Property and equipment

Property and equipment is stated at cost excluding the costs of day-to-day servicing, less accumulated depreciation and accumulated impairment in value. Changes in the expected useful life are accounted for by changing the amortisation period or methodology, as appropriate, and treated as changes in estimates. Right-of-use assets are presented together with property and equipment in the statement of financial position-refer to the accounting policy in below. Right-of-use assets are depreciated on a straight-line basis over the lease term.

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
Right-of-use assets	lease term

An item of property, plant and equipment is derecognised upon disposal or when no future economic benefits are expected its use of disposal. Any gain or loss arising on derecognition of the assets is included in the statement of profit or loss when the asset is derecognised.

3 Summary of Significant Accounting Policies (continued)

The residual values, useful lives and methods of depreciation of property, plant and equipment are reviewed at each financial year end and adjusted prospectively, if appropriate.

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.

Share capital

Share capital

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.

Dividends

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

Leases

The bank assesses at contract inception whether a contract is or contains, a lease. That is, if the contract conveys the right to control the use of an identified asset for a period of time in exchange for consideration. The bank applies a single recognition and measurement approach for all leases, except for short-term leases and leases of low-value assets. The bank recognise lease liabilities to make lease payments and right-of-use assets representing the right to use the underlying assets.

Right-of-use assets

The Bank recognises right-of-use assets at the commencement date of the lease. Right-of-use assets are measured at cost, less any accumulated depreciation and impairment losses, and adjusted for any re-measurement of lease liabilities. The cost of right-of-use assets includes the amount of lease liabilities recognised, initial direct costs incurred, and lease payments made at or before the commencement date less any lease incentives received. Right-of-use assets are depreciated on a straight-line basis over the shorter of the lease term and the estimated useful lives of the assets. Right-of-use assets are also subject to impairment.

Lease liabilities

At the Commencement date of the lease, the Bank recognises lease liabilities measured at the present value of lease payments to be made over the lease term. The lease payments include fixed payments less any lease incentives receivable, variable lease payments that depend on an index or a rate, and amounts expected to be paid under residual value guarantees. The lease payments also include the exercise price of a purchase option reasonably certain to be exercised by the bank and payments of penalties for terminating the lease, if the lease term reflects the Bank exercising the option to terminate.

In calculating the present value of lease payments, the Bank uses its incremental borrowing rate at the lease commencement date because the interest rate implicit in the lease is not readily determinable. The carrying amount of lease liabilities is re-measured if there is a modification, a change in the lease term, a change in the lease payments or a change in the assessment of an option to purchase the underlying asset.

Short-term leases and leases of low-value assets

The Bank applies the lease of low-value assets recognition exemption to leases of placement of ATM that are considered to be low value. Lease payments on leases of low-value assets are recognised as expense on a straight-line basis over the lease term.

3 Summary of Significant Accounting Policies (continued)

Impairment of 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.

Impairment of non-financial assets (continued)

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.

Credit enhancements

The Bank seeks to use collateral to mitigate its credit risks on financial assets. The collateral comes in various forms, such as cash, securities, letters of credit/guarantees, real estate, receivables. Collateral, unless repossessed, is not recorded on the Bank's statement of financial position. Cash flows expected from credit enhancements which are not required to be recognised separately by IFRS standards and which are considered integral to the contractual terms of a debt instrument which is subject to ECL, are included in the measurement of those ECL. On this basis, the fair value of collateral affects the calculation of ECL. Collateral is generally assessed, at a minimum, at inception and re-assessed on a quarterly basis. Details of the Bank's credit enhancements are disclosed in Note 21.

Repossessed assets

The Bank's policy is to determine whether a repossessed asset can be best used for its internal operations or should be sold. Assets determined to be useful for the internal operations are transferred to their relevant asset category at the lower of their repossessed value or the carrying value of the original secured asset. Assets for which selling is determined to be a better option are transferred to assets held for sale at their fair value (if financial assets) and fair value less cost to sell for non-financial assets at the repossession date in, line with the Bank's policy.

Contingencies

Contingent liabilities are not recognised in the statements of financial position but are disclosed unless the possibility of any outflow in settlement is remote. A contingent asset is not recognised in the statement of financial position but disclosed when an inflow of economic benefits is probable.

Taxation

Income taxes are provided in the financial statements in accordance with the legislation enacted or substantively enacted by the end of reporting period in the respective territories that the Bank operates. The income tax comprises of current tax and deferred tax and is recognised in profit or loss except if it is recognised directly in the other comprehensive income because it is related to transactions that are also recognised, in the same or a different period, directly in other comprehensive income.

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

Deferred income tax is provided using the balance sheet liability method for tax loss carry forwards and temporary differences arising between the tax bases of assets and liabilities and their carrying amounts for financial reporting purposes. In accordance with initial recognition exemption, deferred taxes are not recorded for temporary differences on initial recognition of an asset or a liability in a transaction other than a business combination if the transaction, when initially recorded, affects neither accounting nor taxable profit. Deferred tax liabilities are not recorded for temporary differences on initial recognition of goodwill and subsequently for goodwill that is not deductible for tax purposes. Deferred tax balances are measured at tax rates enacted or substantively enacted at the end of the reporting period that are expected to apply to the extent of time when the temporary differences will reverse or the tax loss carry forwards will be utilised.

3. Summary of Significant Accounting Policies (continued)

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

Application of new standards, interpretations and amendments

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

IFRS 9 Financial Instruments – Fees in the '10 per cent' test for derecognition of financial liabilities

As part of its 2019-2020 Annual Improvements to IFRS standards process, the IASB issued an amendment to IFRS 9. The amendment clarifies the fees that an entity includes when assessing whether the terms of a new or modified financial liability are substantially different from the terms of the original financial liability. These fees include only those paid or received between the borrower and the lender, including fees paid or received by either the borrower or lender on the other's behalf. An entity applies the amendment to financial liabilities that are modified or exchanged on or after the beginning of the annual reporting period in which the entity first applies the amendment.

The amendment is effective for annual reporting periods beginning on or after 1 January 2022 with earlier adoption permitted. The Bank will apply the amendments to financial liabilities that are modified or exchanged on or after the beginning of the annual period in which it will first apply the amendment and does not expect this will result in a material impact on its financial statements.

4 Critical Accounting Estimates and Judgements

The preparation of the Bank's financial statements requires management to make judgments, estimates and assumptions that affect the reported amount or revenues, expenses, assets and liabilities, and the accompanying disclosures, as well as the disclosure of contingent liabilities. Uncertainty about these assumptions and estimates could result in outcomes that require a material adjustment to the carrying amount of assets and liabilities affected in future periods. In the process of applying the Bank's accounting policies, management has made the following judgements and assumptions concerning the future and other key sources of estimation uncertainty at the reporting date, that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year.

Significant Increase in Credit Risk (SIRC)

A significant increase in credit risk is not a defined term per IFRS 9, and is determined by management, based on their experience and judgment. In assessing whether the credit risk has significantly increased the Bank has identified a series of qualitative and quantitative criteria based on undertaking the holistic analysis of various factors including those which specific to a particular financial instrument or to a borrower as well as those applicable to particular sub-portfolios. The Bank has established general trigger events for individually significant and collectively assessed loans.

For further details on significant increase in credit risk see NOTE 22.

Measurement of expected credit losses (ECL)

ECL reflects an unbiased, probability-weighted estimate based on a combination of the following principal factors: probability of defaults (PD), loss given defaults (LGD), exposure of default (EAD) and loss given liquidation of collateralized exposure (LGL) which are further explained below:

Probability of Defaults (PD): The bank estimates PD based on a combination of rating model calibration results and a migration matrices approach which is further adjusted for macroeconomic expectations for all portfolios, to represent the forward-looking estimators of the PD parameters. With the forecasted conditional PD's migration matrices are constructed, from which unconditional marginal PD's are calculated that are further adjusted by age of the instrument in the portfolio. Since stage 3 financial instruments are defaulted, the probability of default in this case is equal to 100%.

Exposure of Defaults (EAD): The EAD represents an estimate of the exposure to credit risk at the time of a potential default occurring during the life of a financial asset. It represents the cash flows outstanding at the time of default, considering expected repayments, interest payments and accruals discounted at the EIR. For Stage 1, the EAD are calculated as outstanding amount of loans and off balance commitments that are expected to be impaired in the period of 12 month after reporting period. For Stage 2 financial instruments, the EAD is calculated for each contractual remaining year. EAD for each year is estimated as an outstanding amount by the reporting period minus the cumulative yearly principal repayments. The outstanding amount by the reporting period is calculated taking into account CCF and cash cover

4 Critical Accounting Estimates and Judgments (continued)

amounts. For Stage 3, the EAD is calculated as the outstanding amount of the instrument by the reporting date taking into account CCF and cash cover amounts.

Loss Given Default (LGD): LGD is defined as the likely loss in case of a counterparty default. It provides an estimation of the exposure that cannot be recovered in default event and therefore captures the severity of a loss. LGD rate are calculated for corporate and retail portfolios. LGD is statistically calculated based on historical loan recovery data and takes into account historical losses incurred on unsecured exposures. While calculation LGD outlier recoveries are excluded from the calculation. LGD is expressed as a percentage of the EAD.

Loss Given Liquidation of collateralized exposures (LGL): LGL represents the percentage of the exposure that cannot be recovered from collateral liquidation if the exposure is defaulted. Loss Given Liquidation calculation takes into account LTV, adjusted by time to sale of movable and immovable collateral, real estate price index, EIR, and expected sales ratio of collaterals. For uncollateralized exposures LGL is taken at 100%.

Details of ECL measurement methodology are disclosed in Note 22.

Macro-economic scenarios

Under IFRS 9, the allowance for credit losses is based on reasonable and supportable forward-looking information obtainable without undue costs of effort, which takes into considerations past events, current conditions and forecasts of future economic conditions.

To incorporate forward-looking information into the Bank's allowance for credit losses, the Bank uses the macroeconomic forecasts provided By National Bank of Georgia. Macroeconomic variables covered by these forecasts and which the Bank incorporated in its ECL assessment model include GDP growth, foreign exchange rate and unemployment rate. The determination of the probability weighted ECL requires evaluating a range of diverse and relevant future economic conditions. To accommodate this requirement, the Bank uses three different economic scenarios in the ECL calculation: an upside (weight 0.25), a baseline (weight 0.50) and downside (weight 0.25) scenario relevant for each respective portfolio. A weight is computed for each scenario by using a probabilistic economic model that considers recent information as well as historical data provided by National Bank of Georgia.

Income tax

The Bank is subject to income tax and significant judgment is required in determining the provision for income taxes. During the ordinary course of business, there are transactions and calculations for which the ultimate tax determination is uncertain. As a result, the Bank recognizes tax liabilities based on estimates of whether additional taxes and interest will be due. These tax liabilities are recognized when, despite the Bank's belief that its tax return positions are supportable, the Bank believes that certain positions are likely to be challenged and may not be fully sustained upon review by tax authorities.

5 Net interest income

The interest income and expenses of the Bank are as follows:

	2022	2021	2020
Interest income			
Financial assets measured as amortized cost			
Loans to customers	28,119	20,421	17,230
Cash and cash equivalent and due from banks	954	967	503
Financial assets measured at fair value through other comprehensive income			
Investment securities	707	977	1,655
Interest income calculated using effective interest rate	29,780	22,365	19,388
Interest expense			
Amounts due to banks	(3,032)	(1,952)	(2,663)
Other borrowed funds	(2,699)	(1,643)	(910)
Amounts due to customers	(1,454)	(1,057)	(630)
Interest expenses	(7,185)	(4,652)	(4,203)
Net interest income	22,595	17,713	15,185

6 Net Fee and commission income

The interest income and expenses of the Bank are as follows:

	2022	2021	2020
Fee and commission income			
Commission from guarantees	2,503	2,494	2,189
Settlement operations	418	415	366
Card operations	257	484	270
Other operations	60	21	21
Total fee and commission income	3,238	3,414	2,846
Fee and commission expense			
Card operations	(959)	(1,070)	(685)
Settlement operations	(436)	(453)	(294)
Other operations	-	(171)	(76)
Total fee and commission expense	(1,395)	(1,694)	(1,055)
Total net fee and commission income	1,843	1,720	1,791

The Bank applies the practical expedient in paragraph 121 of IFRS 15 and does not disclose information about remaining performance obligations that have original expected durations of one year or less.

7 Credit loss expense on financial assets

The table below shows the net ECL charges (reversal) on financial instruments recorded in the statement of profit or loss for the year ended 31 December 2022:

		Stage 1	Stage 2	Stage 3	Total
	Notes				
Amounts due from banks	12	2	-	-	2
Loans to customers	14	1,266	(13)	65	1,318
Investment securities	15	(28)	-	-	(28)
Financial guarantees		87	-	-	87
Total credit loss		1,327	(13)	65	1,379

7 Credit loss expense on financial assets (continued)

The table below shows the net ECL charges (reversal) on financial instruments recorded in the statement of profit or loss for the year ended 31 December 2021:

		Stage 1	Stage 2	Stage 3	Total
	Notes				
Amounts due from banks	12	3	-	-	3
Loans to customers	14	(154)	3	249	98
Investment securities	15	(71)	-	-	(71)
Financial guarantees		26	-	-	26
Total credit loss		(196)	3	249	56

The table below shows the net ECL charges (reversal) on financial instruments recorded in the statement of profit or loss for the year ended 31 December 2020:

		Stage 1	Stage 2	Stage 3	Total
	Notes				
Loans to customers	14	366	9	(137)	238
Investment securities	15	(82)	-	-	(82)
Financial guarantees		98	-	-	98
Total credit loss		382	9	(137)	254

8 Personnel expenses

Personnel expenses of the Bank are as follows:

	2022	2021	2020
Salaries and bonuses	4,304	4,578	4,558
Other compensation cost	517	289	292
	4,821	4,867	4,850

In 2022 the average number of employees by the Bank was 63 (2021: 65; 2020: 64).

9 Other expense

Other expenses of the Bank are as follows:

	2022	2021	2020
Depreciation and amortization	1,234	1,281	1,269
Royalty	826	695	549
Communication and information services	781	662	53
Interest expense on lease liability	212	90	94
Entertainment expenses	196	110	32
Professional services	175	119	114
Travel expenses	114	60	30
Operating Lease	95	17	14
Repairs and maintenance	81	130	81
Insurance expense	58	110	112
Utilities	36	54	46
Taxes other than on income	31	21	7
Office supplies	26	17	10
Advertising and marketing	10	3	5
Penalty fee	-	22	-
Disposal of LHI	-	127	-
Other	367	378	230
	4,242	3,896	2,646

9 Other expenses (continued)

Remuneration of the Bank's auditor for the audit of the Bank's annual financial statements for the year ended 31 December 2022 comprised GEL 79 thousand (2021: GEL 61 thousand, 2020: GEL 63 thousand) (net of VAT).

10 Taxation

On 12 June 2018, an amendment to the current corporate taxation model applicable to financial institutions, including banks and insurance businesses, became effective. The change implied a zero corporate tax rate on retained earnings and a 15% corporate tax rate on distributed earnings starting from 1 January 2023. On 16 December 2022, an amendment to the corporate tax code was passed into law abolishing the expected transition to taxation on distributed earnings from 1 January 2023. According to the amendment, effective from 1 January 2023, existing taxation rules for financial institutions, including banks, will be maintained. At the same time, the existing corporate tax rate for banks will be increased from 15% to 20% from 2023 going forward. In addition, with effect from 2023, taxable interest income and deductible ECLs on loans to customers will be defined as per IFRS, instead of local NBG regulations. Transition differences in ECLs will be taxed one-off at 15%. The amended law lacks clarification in treatment of transition differences in interest income. Management considers it reasonable that an approach similar to ECL on transition is applicable on interest income and calculates deferred tax respectively.

The change had an immediate impact on deferred tax asset and deferred tax liability balances attributable to previously recognised temporary differences arising from prior periods. As at 31 December 2022, deferred tax assets and liabilities balances have been remeasured, in line with the updated legislation. The change resulted in a material one-off deferred tax charge as previously the Bank recognised deferred taxes only to the extent they were expected to realise before 1 January 2023.

Following the enactment of the latest amendment, the Bank recalculated its deferred tax assets at 31 December 2022 and made the relevant recognition of deferred tax expense in the profit and loss statement for 2022.

The corporate income tax expense comprises:

	<u>2022</u>	2021	2020
Current year tax expense	(3,106)	(1,824)	(218)
Deferred tax benefit/(expense)			
Movement in deferred tax assets and liabilities due to origination and reversal of temporary differences	320	198	(160)
One-off expense	(478)	-	-
	(158)	198	(160)
Total income tax expense	(3,264)	(1,626)	(378)

In 2022, the applicable tax rate for current and deferred tax is 15% (2021: 15%; 2020: 15%)

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

	<u>2022</u>	2021	2020
Profit before tax	15,777	12,207	10,053
Income tax at the applicable			
Tax rate (15%)	(2,367)	(1,831)	(1,508)
Non-taxable differences	(419)	143	1,130
One-off expense	(478)	-	-
	(3,264)	198	(378)

Deferred tax assets and liabilities

Movements in temporary differences during the years ended 31 December 2022, 2021 and 2020 are presented as follows.

10 Taxation (continued)

	Balance 1 January 2022	Recognized in profit or loss	Recognized in other comprehensive income	Balance 31 December 2022
Property, equipment, Intangible and ROU assets	(352)	67	-	(285)
Loans to customers	(548)	197	-	(351)
Investment securities	(42)	23	(82)	(101)
Other liabilities	(60)	33	-	(27)
Net tax (liabilities)/assets	(1,002)	320	(82)	(764)

	Balance 1 January 2021	Recognized in profit or loss	Recognized in other comprehensive income	Balance 31 December 2021
Property, equipment, Intangible and ROU assets	(299)	(53)	-	(352)
Loans to customers	(807)	259	-	(548)
Investment securities	(87)	(19)	64	(42)
Other liabilities	(71)	11	-	(60)
Net tax (liabilities)/assets	(1,264)	198	64	(1,002)

	Balance 1 January 2020	Recognized in profit or loss	Recognized in other comprehensive income	Balance 31 December 2020
Property, equipment, Intangible and ROU assets	(323)	24	-	(299)
Loans to customers	(654)	(153)	-	(807)
Investment securities	49	(45)	(91)	(87)
Other liabilities	(85)	14	-	(71)
Net tax (liabilities)/assets	(1,013)	(160)	(91)	(1,264)

11 Cash and cash equivalents

Cash and cash equivalents as at 31 December 2022, 31 December 2021 and December 2020 comprise of following:

	2022	2021	2020
Cash on hand	3,279	2,974	3,167
Cash equivalents			
Correspondent accounts with the NBG	799	19,477	16,181
Nostro accounts with other banks	47,714	7,180	5,676
Term deposits with NBG	4,102	18,204	3,203
Term deposits with other banks	1,891	4,204	4,260
Less-allowance for impairment	-	(1)	(2)
Total cash equivalents	54,506	49,064	29,318
Total cash on hand and cash equivalents	57,785	52,038	32,485

All balances of cash equivalents are allocated to Stage 1; there were no significant movements in ECL during the year.

11 Cash and cash equivalents (continued)

As at 31 December 2022 the Bank has a placement with two bank (2021: one bank; 2020: one bank) with carrying value that individually exceeds 10% of equity. The gross value of that balance as at 31 December 2022 is GEL 47,625 thousand (2021: GEL 37,677 thousand; 2020: GEL 19,381 thousand).

Credit rating of correspondent accounts and placements with other banks with original maturities of less than three month stands as follow:

	2022	2021	2020
BB+	1,892	-	-
BB	4,901	37,681	19,381
BB-	47,625	5,995	5,462
B+	-	4,261	40
B	34	-	-
Not Rated	54	1,127	4,435
Total	54,506	49,064	29,318

The table illustrates the ratings by international agency Fitch Ratings.

12 Amounts due from credit institutions

Amounts due from credit institutions as at 31 December 2022, 31 December 2021 and 31 December 2020 comprise of following:

	2022	2021	2020
With less than 1 year contractual maturity	-	8,751	9,193
Expected credit loss	-	(6)	(3)
Total amount due from banks	-	8,745	9,190

For the purpose of ECL measurement due from CI are included in stage 1. The ECL recognised for the amounts due from banks as at 31 December 2022 was GEL 0 thousand and there were no significant movements in ECL during the year (NOTE 7).

Credit rating of Amounts due from banks stands as follow:

	2022	2021	2020
BB	-	-	8,645
B+	-	5,286	545
B-	-	3,459	-
	-	8,745	9,190

The table illustrates the ratings by international agency Fitch Ratings.

Amounts due to banks portfolio has changed completely as for 31 December 2022. All items that were on balance at 31 December 2021 was repaid to bank and as 31 December 2022 bank has only new items on balance sheet. In previous years bank have entered into agreements only in case of excess of cash and cash equivalents funds, but in 2022 the new items has increased interest rates, which do not significantly differ from the interest rates of loans issued to customers. In 2022 the profitability of interbank loans are same or even higher than in case of loans to customers, respectively bank changed their approach to interbank loans and in 2022 bank looked at interbank loans as loan portfolio.

13 Mandatory reserves at the National Bank of Georgia

Mandatory reserves at the National Bank of Georgia (NBG) represents amounts deposits with the NBG. 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 Bank's ability to withdraw these deposits is restricted by regulations.

	2022	2021	2020
Mandatory reserves at the NBG	39,030	38,427	36,217
	39,030	38,427	36,217

14 Loans to customers

Loans to customers as at 31 December 2022, 31 December 2021 and 31 December 2020 comprise of following:

	2022	2021	2020
Loans to legal entities			
Corporate lending	255,255	234,548	207,908
Small and medium business lending	25,124	19,849	22,627
Interbank loans	21,513	-	-
Total loans to legal entities	301,892	254,397	230,535
Loans to individuals			
Residential mortgage	3,785	2,946	4,186
Consumer lending	3,926	3,833	3,286
Total loans to individuals	7,711	6,779	7,472
Gross loans to customers	309,603	261,176	238,007
Less-allowance for impairment	(2,449)	(1,150)	(1,052)
Loans to customers	307,154	260,026	236,955

(a) Allowance for impairment of loans to customers at amortised cost

The following tables disclose the changes in the credit loss allowance and gross carrying amount for loans to customers carried at amortised cost between the beginning and the end of the reporting period. Below main movements in the table are described:

- ▶ Transfers between Stage 1, 2 and 3 due to balances experiencing significant increases (or decreases) of credit risk or becoming credit-impaired in the period, and the consequent "step up" (or "step down") between 12-month and Lifetime ECL;
- ▶ New originated or purchased gives us information regarding gross loans and corresponding credit impairment losses issued during the period (however, exposures which were issued and repaid during the period and issued to refinance existing loans are excluded);
- ▶ The line, derecognised during the period refers to starting balance of loans which were repaid or during the period;
- ▶ Foreign exchange translations of assets denominated in foreign currencies;
- ▶ Net remeasurement due to stage transfers and risk parameters changes refers to the movements in ECL as a result of transfer of exposure between stages or changes in risk parameters and forward looking expectations.

An analysis of changes in the gross carrying value and corresponding ECL in relation to corporate lending during the year ended 31 December 2022 is as follows:

Corporate lending	Stage 1	Stage 2	Stage 3	Total
Gross carrying values as at 1 January 2022	232,789	-	1,763	234,552
New assets originated or purchased	175,795	-	-	175,795
Assets repaid	(143,202)	-	(1,348)	(144,550)
Foreign exchange adjustments	(10,489)	-	(53)	(10,542)
At 31 December 2022	254,893	-	362	255,255

Corporate lending	Stage 1	Stage 2	Stage 3	Total
ECL as 1 January 2022	(405)	-	-	(405)
New assets originated or purchased	(1232)	-	-	(1232)
Assets repaid	197	-	-	197
Net remeasurement of ECL	48	-	-	48
At 31 December 2022	(1,392)	-	-	(1,392)

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14 Loans to customers (continued)

An analysis of changes in the gross carrying value and corresponding ECL in relation to corporate lending during the year ended 31 December 2021 is as follows:

Corporate lending	Stage 1	Stage 2	Stage 3	Total
Gross carrying values as at 1 January 2021	206,043	-	1,865	207,908
New assets originated or purchased	165,181	-	-	165,181
Assets repaid	(133,637)	-	-	(133,637)
Foreign exchange adjustments	(4,802)	-	(102)	(4,904)
At 31 December 2021	232,785	-	1,763	234,548

Corporate lending	Stage 1	Stage 2	Stage 3	Total
ECL as 1 January 2021	(571)	-	(37)	(608)
New assets originated or purchased	(274)	-	-	(274)
Assets repaid	256	-	37	293
Net remeasurement of ECL	184	-	-	184
At 31 December 2021	(405)	-	-	(405)

An analysis of changes in the gross carrying value and corresponding ECL in relation to corporate lending during the year ended 31 December 2020 is as follows:

Corporate lending	Stage 1	Stage 2	Stage 3	Total
Gross carrying values as at 1 January 2020	126,883	-	1,632	128,515
New assets originated or purchased	162,268	-	-	162,268
Assets repaid	(88,200)	-	-	(88,200)
Foreign exchange adjustments	5,092	-	233	5,325
At 31 December 2020	206,043	-	1,865	207,908

Corporate lending	Stage 1	Stage 2	Stage 3	Total
ECL as 1 January 2020	(212)	-	-	(212)
New assets originated or purchased	(516)	-	-	(516)
Assets repaid	223	-	-	223
Net remeasurement of ECL	(66)	-	(37)	(103)
At 31 December 2020	(571)	-	(37)	(608)

An analysis of changes in the gross carrying value and corresponding ECL in relation to small and medium business lending during the year ended 31 December 2022 is as follows:

Small and medium business	Stage 1	Stage 2	Stage 3	Total
Gross carrying values as at 1 January 2022	18,263	492	1,094	19,849
New assets originated or purchased	19,332	-	238	19,570
Assets repaid	(12,656)	(108)	(450)	(13,214)
Foreign exchange adjustments	(1,026)	(49)	(6)	(1,081)
At 31 December 2022	23,913	335	876	25,124

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14 Loans to customers (continued)

Small and medium business	Stage 1	Stage 2	Stage 3	Total
ECL as 1 January 2022	(33)	(15)	(204)	(252)
New assets originated or purchased	(137)	-	(238)	(375)
Assets repaid	18	1	142	161
Net remeasurement of ECL	8	10	3	21
At 31 December 2022	(144)	(4)	(297)	(445)

An analysis of changes in the gross carrying value and corresponding ECL in relation to small and medium business lending during the year ended 31 December 2021 is as follows:

Small and medium business	Stage 1	Stage 2	Stage 3	Total
Gross carrying values as at 1 January 2021	20,422	39	2,166	22,627
New assets originated or purchased	10,441	-	268	10,709
Assets repaid	(12,521)	(39)	(818)	(13,378)
Transfers to Stage 2	-	520	(520)	-
Foreign exchange adjustments	(78)	(28)	(3)	(109)
At 31 December 2021	18,264	492	1,093	19,849

Small and medium business	Stage 1	Stage 2	Stage 3	Total
ECL as 1 January 2021	(21)	(15)	(103)	(139)
New assets originated or purchased	(30)	-	(141)	(171)
Assets repaid	15	-	71	86
Transfers to Stage 2	-	15	(15)	-
Net remeasurement of ECL	3	(15)	(16)	(28)
At 31 December 2021	(33)	(15)	(204)	(252)

An analysis of changes in the gross carrying value and corresponding ECL in relation to small and medium business lending during the year ended 31 December 2020 is as follows:

Small and medium business	Stage 1	Stage 2	Stage 3	Total
Gross carrying values as at 1 January 2020	15,236	-	3,358	18,594
New assets originated or purchased	17,340	39	1,710	19,089
Assets repaid	(12,565)	-	(2,915)	(15,480)
Foreign exchange adjustments	411	-	13	424
At 31 December 2020	20,422	39	2,166	22,627

Small and medium business	Stage 1	Stage 2	Stage 3	Total
ECL as 1 January 2020	(26)	-	(230)	(256)
New assets originated or purchased	(19)	(15)	(56)	(90)
Assets repaid	22	-	182	204
Net remeasurement of ECL	2	-	1	3
At 31 December 2020	(21)	(15)	(103)	(139)

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14 Loans to customers (continued)

An analysis of changes in the gross carrying value and corresponding ECL in relation to Interbank loans during the year ended 31 December 2022 is as follows:

Interbank Loans	Stage 1	Stage 2	Stage 3	Total
Gross carrying values as at 1 January 2022	-	-	-	-
New assets originated or purchased	21,513	-	-	21,513
Assets repaid	-	-	-	-
Foreign exchange adjustments	-	-	-	-
At 31 December 2022	21,513	-	-	21,513

Interbank Loans	Stage 1	Stage 2	Stage 3	Total
ECL as 1 January 2022	-	-	-	-
New assets originated or purchased	(47)	-	-	(47)
Assets repaid	-	-	-	-
Net remeasurement of ECL	-	-	-	-
At 31 December 2022	(47)	-	-	(47)

An analysis of changes in the gross carrying value and corresponding ECL in relation to Residential mortgages during the year ended 31 December 2022 is as follows:

Residential mortgages	Stage 1	Stage 2	Stage 3	Total
Gross carrying values as at 1 January 2022	2,577	-	369	2,946
New assets originated or purchased	2,268	-	84	2,352
Assets repaid	(1,358)	-	(74)	(1,432)
Foreign exchange adjustments	(58)	-	(23)	(81)
At 31 December 2022	3,429	-	356	3,785

Residential mortgages	Stage 1	Stage 2	Stage 3	Total
ECL as 1 January 2022	(8)	-	(124)	(132)
New assets originated or purchased	(51)	-	(94)	(145)
Assets repaid	(6)	-	141	135
Net remeasurement of ECL	13	-	(72)	(59)
At 31 December 2022	(52)	-	(149)	(201)

14 Loans to customers (continued)

An analysis of changes in the gross carrying value and corresponding ECL in relation to Residential mortgages during the year ended 31 December 2021 is as follows:

Residential mortgages	Stage 1	Stage 2	Stage 3	Total
Gross carrying values as at 1 January 2021	2,773	144	1,269	4,186
New assets originated or purchased	775	-	133	908
Assets repaid	(1,626)	(100)	(373)	(2,099)
Transfers to stage 1	810	(44)	(766)	-
Transfers to stage 3	(114)	-	114	-
Foreign exchange adjustments	(41)	-	(8)	(49)
At 31 December 2021	2,577	-	369	2,946

Residential mortgages	Stage 1	Stage 2	Stage 3	Total
ECL as 1 January 2021	(27)	-	(13)	(40)
New assets originated or purchased	(19)	-	-	(19)
Assets repaid	26	-	-	26
Transfers to stage 1	1	-	(1)	-
Transfers to stage 3	(7)	-	7	-
Net remeasurement of ECL	18	-	(117)	(99)
At 31 December 2021	(8)	-	(124)	(132)

An analysis of changes in the gross carrying value and corresponding ECL in relation to Residential mortgages during the year ended 31 December 2020 is as follows:

Residential mortgages	Stage 1	Stage 2	Stage 3	Total
Gross carrying values as at 1 January 2020	5,175	156	288	5,619
New assets originated or purchased	555	65	731	1,351
Assets repaid	(2,901)	(27)	(33)	(2,961)
Transfers to stage 1	93	(93)	-	-
Transfers to stage 2	(38)	38	-	-
Transfers to stage 3	(246)	(5)	251	-
Foreign exchange adjustments	135	10	32	177
At 31 December 2020	2,773	144	1,269	4,186

Residential mortgages	Stage 1	Stage 2	Stage 3	Total
ECL as 1 January 2020	(14)	(1)	(8)	(23)
New assets originated or purchased	(28)	-	(6)	(34)
Assets repaid	12	-	2	14
Net remeasurement of ECL	3	-	-	3
At 31 December 2020	(27)	(1)	(12)	(40)

An analysis of changes in the gross carrying value and corresponding ECL in relation to consumer lending during the year ended 31 December 2022 is as follows:

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14 Loans to customers (continued)

Consumer lending	Stage 1	Stage 2	Stage 3	Total
Gross carrying values as at 1 January 2022	3,390	6	437	3,833
New assets originated or purchased	2,771	-	15	2,786
Assets repaid	(2,529)	-	(154)	(2,683)
Foreign exchange adjustments	(7)	-	(3)	(10)
At 31 December 2022	3,625	6	295	3,926

Consumer lending	Stage 1	Stage 2	Stage 3	Total
ECL as at 1 January 2022	(36)	(3)	(322)	(361)
New assets originated or purchased	(74)	-	(24)	(98)
Assets repaid	26	1	72	99
Net remeasurement of ECL	(11)	-	7	(4)
At 31 December 2022	(95)	(2)	(267)	(364)

An analysis of changes in the gross carrying value and corresponding ECL in relation to consumer lending during the year ended 31 December 2021 is as follows:

Consumer lending	Stage 1	Stage 2	Stage 3	Total
Gross carrying values as at 1 January 2021	2,628	64	594	3,286
New assets originated or purchased	2,185	6	20	2,211
Assets repaid	(1,411)	(13)	(148)	(1,572)
Transfers to stage 1	82	(51)	(31)	-
Transfers to stage 3	(3)	-	3	-
Foreign exchange adjustments	(91)	-	(1)	(92)
At 31 December 2021	3,390	6	437	3,833

Consumer lending	Stage 1	Stage 2	Stage 3	Total
ECL as at 1 January 2021	(22)	-	(243)	(265)
New assets originated or purchased	(50)	(3)	-	(53)
Assets repaid	29	-	24	53
Net remeasurement of ECL	7	-	(103)	(96)
At 31 December 2021	(36)	(3)	(322)	(361)

An analysis of changes in the gross carrying value and corresponding ECL in relation to consumer lending during the year ended 31 December 2020 is as follows:

Consumer lending	Stage 1	Stage 2	Stage 3	Total
Gross carrying values as at 1 January 2020	2,705	77	723	3,505
New assets originated or purchased	1,319	64	147	1,530
Assets repaid	(1,485)	(69)	(363)	(1,917)
Transfers to stage 3	(77)	(8)	85	-
Foreign exchange adjustments	166	-	2	168
At 31 December 2020	2,628	64	594	3,286

14 Loans to customers (continued)

Consumer lending	Stage 1	Stage 2	Stage 3	Total
ECL as at 1 January 2020	(21)	(10)	(293)	(324)
New assets originated or purchased	(24)	-	(39)	(63)
Assets repaid	31	13	60	104
Transfers to stage 3	(14)	(3)	17	-
Net remeasurement of ECL	6	-	12	18
At 31 December 2020	(22)	-	(243)	(265)

The credit loss allowance for loans and advances to customers recognised in the period is impacted by a variety of factors, details of ECL measurement are provided in Note 7.

(b) Credit quality of loans to customers

The bank is working on implementation its own internal grading system, which will define credit risk category based on the several factors, which has impact on the quality of the loans to customers by business segment. Before implementation the mentioned internal grading system, the Bank is controlling its loan portfolio by four overdue buckets on daily basis and relevant actions are planned according to the information, retrieved after such analysis.

The following table provides information on the credit quality of loans to customers as at 31 December 2022:

	Stage 1	Stage 2	Stage 3	Total
Loans to legal entities				
Corporate lending	254,893	-	362	255,255
not overdue	254,893	-	-	254,893
overdue more than 90 days	-	-	362	362
Small and medium business lending	23,913	335	876	25,124
not overdue	23,799	335	279	24,413
overdue less than 30 days	114	-	-	114
overdue more than 90 days	-	-	597	597
Interbank loans	21,513	-	-	21,513
not overdue	21,513	-	-	21,513
Total loans to legal entities	300,319	335	- 1,238	301,892
Loans to individuals	Stage 1	Stage 2	Stage 3	Total
Residential mortgages	3,429	-	356	3,785
not overdue	3,429	-	160	3,589
overdue more than 30 days and less than 90 days	-	-	162	162
overdue more than 90 days	-	-	34	34
Consumer lending	3,593	-	333	3,926
not overdue	3,593	-	183	3,776
overdue more than 90 days	-	-	150	150
Total loans to individuals	7,022	-	689	7,711
Total gross loans to customers	307,341	335	1,927	309,603

The following table provides information on the credit quality of loans to customers as at 31 December 2021:

	Stage 1	Stage 2	Stage 3	Total
Loans to legal entities				
Corporate lending	232,785	-	1,763	234,548
not overdue	232,785	-	-	232,785
overdue more than 90 days	-	-	1,763	1,763
Small and medium business lending	18,264	492	1,093	19,849
not overdue	18,264	492	320	19,076
overdue more than 30 days and less than 90 days	-	-	670	670
overdue more than 90 days	-	-	103	103
Total loans to legal entities	251,049	492	2,856	254,397

14 Loans to customers (continued)

Loans to individuals	Stage 1	Stage 2	Stage 3	Total
Residential mortgages	2,577	-	369	2,946
not overdue	2,565	-	255	2,820
overdue less than 30 days	12	-	85	97
overdue more than 90 days	-	-	29	29
Consumer lending	3,390	6	437	3,833
not overdue	3,390	-	167	3,557
overdue more than 30 days and less than 90 days	-	6	11	17
overdue more than 90 days	-	-	259	259
Total loans to individuals	5,967	6	806	6,779
Total gross loans to customers	257,016	498	3,662	261,176

The following table provides information on the credit quality of loans to customers as at 31 December 2020:

Loans to legal entities	Stage 1	Stage 2	Stage 3	Total
Corporate lending	206,043	-	1,865	207,908
not overdue	206,043	-	-	206,043
overdue more than 90 days	-	-	1,865	1,865
Small and medium business lending	20,422	39	2,166	22,627
not overdue	20,377	39	1,711	22,127
overdue less than 30 days	45	-	-	45
overdue more than 90 days	-	-	455	455
Total loans to legal entities	226,465	39	4,031	230,535
Loans to individuals	Stage 1	Stage 2	Stage 3	Total
Residential mortgages	2,773	144	1,269	4,186
not overdue	2,345	34	1,104	3,483
overdue less than 30 days	428	-	-	428
overdue more than 30 days and less than 90 days	-	110	-	110
overdue more than 90 days	-	-	165	165
Consumer lending	2,628	64	594	3,286
not overdue	2,505	64	271	2,841
overdue less than 30 days	123	-	28	151
overdue more than 30 days and less than 90 days	-	-	17	17
overdue more than 90 days	-	-	277	277
Total loans to individuals	5,401	208	1,863	7,472
Total gross loans to customers	231,866	247	5,894	238,007

(c) Analysis of collateral and other credit enhancements

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

The main types of collateral obtained are as follows:

- ▶ For commercial lending, charges over real estate properties, inventory, trade receivables, movable properties, sureties;
- ▶ For retail lending, mortgages over residential properties, movable properties and sureties.

The below table provides an analysis of the current fair values of collateral held and credit enhancements for credit-impaired (stage 3) assets. Dependent on the level of collateral, some Stage 3 exposures may not have individual ECLs when the expected value of the collateral is greater than the LGD, even in if the future value of collateral is forecast using multiple economic scenarios. However, the Stage 3 ECL can be higher than net exposure show below when the future value of collateral, measured using multiple economic scenarios, is expected to decline.

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14 Loans to customers (continued)

	<i>Maximum Fair value of collateral held under the base scenario</i>						<i>Associated ECL</i>
	<i>exposure to credit risk</i>	<i>Real estate property</i>	<i>Other*</i>	<i>Surplus collateral</i>	<i>Total collateral</i>	<i>Net exposure</i>	
31 December 2022	1,927	7,815	1,079	(7,581)	1,313	614	281
Corporate lending	362	2,648	362	(2,648)	362	-	-
Small and medium business lending	876	4,534	570	(4,534)	570	306	273
Residential mortgages	356	564	81	(330)	315	41	(6)
Consumer lending	333	69	66	(69)	66	267	14

* Vehicles, sureties, machinery, other fixed assets, inventory and trade receivables.

	<i>Maximum Fair value of collateral held under the base scenario</i>						<i>Associated ECL</i>
	<i>exposure to credit risk</i>	<i>Real estate property</i>	<i>Other*</i>	<i>Surplus collateral</i>	<i>Total collateral</i>	<i>Net exposure</i>	
31 December 2021	3,662	10,087	3,021	(9,751)	3,357	305	650
Corporate lending	1,763	3,943	1,763	(3,943)	1,763	-	-
Small and medium business lending	1,093	4,708	1,083	(4,722)	1,069	24	204
Residential mortgages	369	850	-	(488)	362	7	124
Consumer lending	437	586	175	(598)	163	274	322

* Vehicles, sureties, machinery, other fixed assets, inventory and trade receivables.

	<i>Maximum Fair value of collateral held under the base scenario</i>						<i>Associated ECL</i>
	<i>exposure to credit risk</i>	<i>Real estate property</i>	<i>Other*</i>	<i>Surplus collateral</i>	<i>Total collateral</i>	<i>Net exposure</i>	
31 December 2020	5,894	16,168	3,979	(14,635)	5,512	382	395
Corporate lending	1,865	5,902	1,865	(5,902)	1,865	-	37
Small and medium business lending	2,166	6,615	1,876	(6,398)	2,093	73	103
Residential mortgages	1,269	2,361	-	(1,110)	1,251	18	12
Consumer lending	594	1,290	238	(1,225)	303	291	243

* Vehicles, sureties, machinery, other fixed assets, inventory and trade receivables.

The following table shows carrying value of loans on which no ECL was recognized because of existence of collateral as at 31 December 2022:

Loans to legal entities	2022
Corporate lending	33,136
Small and medium business lending	2,289
Total loans to legal entities	35,425
Loans to individuals	
Residential mortgages	621
Consumer lending	841
Total loans to individuals	1,462
Gross loans to customers	36,887

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14 Loans to customers (continued)

The following table shows carrying value of loans on which no ECL was recognized because of existence of collateral as at 31 December 2021:

Loans to legal entities	2021
Corporate lending	46,287
Small and medium business lending	8,121
Total loans to legal entities	54,408
Loans to individuals	
Residential mortgages	666
Consumer lending	1,928
Total loans to individuals	2,594
Gross loans to customers	57,002

The following table shows carrying value of loans on which no ECL was recognized because of existence of collateral as at 31 December 2020:

Loans to legal entities	2020
Corporate lending	6,810
Small and medium business lending	5,856
Total loans to legal entities	12,666
Loans to individuals	
Residential mortgages	2,229
Consumer lending	1,803
Total loans to individuals	4,032
Gross loans to customers	16,698

(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:

	2022		2021		2020	
Financial institutions	89,306	29%	40,425	15%	33,183	14%
Other sectors	54,757	18%	21,718	8%	19,459	8%
Consumer goods	31,625	10%	27,161	10%	27,756	12%
Construction and land development	28,667	9%	42,521	16%	40,220	17%
Energy	24,341	8%	47,300	18%	31,074	13%
"Production and trade of clothes, shoes and textiles"	19,685	6%	13,168	5%	10,600	4%
Real estate management	15,361	5%	13,130	5%	18,453	8%
Hotels, restaurants and tourism	13,602	4%	19,005	7%	20,472	9%
Healthcare	13,041	4%	8,052	3%	5,043	2%
Service	11,507	4%	20,748	8%	23,105	10%
Loans to individuals	7,711	2%	6,779	3%	7,472	3%
Telecommunication	-	0%	1,169	0%	1,151	0%
Agriculture	-	0%	-	0%	19	0%
Total loan to customers	309,603	100%	261,176	100%	238,007	100%
Less -allowance for impairment	(2,449)		(1,150)		(1,052)	
Total net loans to customers	307,154		260,026		236,955	

14 Loans to customers (continued)

(e) Significant credit exposures

As at 31 December 2022 the Bank has loans issued to four borrowers or groups of connected borrowers (2021: seven; 2020: ten) with carrying values that individually exceed 10% of equity. The gross value of these loans as at 31 December 2022 is GEL 71,855 thousand (2021: GEL 85,630 thousand; 2020: GEL 116,435 thousand).

(f) Loan maturities

The maturity of the loan portfolio is presented in Note 22 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.

(g) Modified and restructured loans

The Bank derecognises a financial asset, such as a loan to a customer, when the terms and conditions have been renegotiated to the extent that, substantially, it becomes a new loan, with the difference recognised as a derecognition gain or loss, to the extent that an impairment loss has not already been recorded. The newly recognised loans are classified as Stage 1 for ECL measurement purposes.

If the modification does not result in cash flows that are substantially different, the modification does not result in derecognition. Based on the change in cash flows discounted at the original EIR, the Bank records a modification gain or loss, to the extent that an impairment loss has not already been recorded.

During 2021, the Bank has modified the terms and conditions of certain corporate and commercial loans, including introduction of payment holidays, as part of the measures introduced by the Government related to consequences of COVID-19 pandemic. The Bank considered these modifications to be non-substantial.

15 Investment securities

Investment securities as at 31 December are as follows:

	<u>2022</u>	<u>2021</u>	<u>2020</u>
Debt securities at FVOCI			
Treasury bonds of Ministry of Finance Georgia	996	8,296	7,485
Treasury bonds of Republic of Turkey	<u>1,357</u>	<u>6,163</u>	<u>10,553</u>
Total investment securities	<u>2,353</u>	<u>14,459</u>	<u>18,038</u>

All Investment securities are allocated to Stage 1. The ECL recognized for investment securities as at 31 December 2022 was GEL 28 thousand and there were no significant movements in ECL during the year (Note 7).

Credit rating of Investment securities as at 31 December 2022, 2021 and 2020 stands as follow:

	<u>2022</u>	<u>2021</u>	<u>2020</u>
BB	996	8,296	7,485
BB-	-	6,163	10,553
B	<u>1,357</u>		
	<u>2,353</u>	<u>14,459</u>	<u>18,038</u>

Country rating for Republic of Georgia stands at BB with stable outlook as assigned by international rating Country rating for Republic of turkey stands at B With stable outlook as assigned by international rating agency.

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16 Property, equipment, intangible and right-of-use assets

Property, equipment, intangible and right-of-use assets as of December 31 2022, 2021 and 2020 comprise:

	Right-of-use assets					Total
	Leasehold improvements	Computers and office equipment	Furniture and fixtures	Motor vehicles	Intangible assets	
Cost						
Balance at 1 January 2020	2,056	893	396	369	729	7,180
Additions	7	561	3	208	303	1,082
Balance at 31 December 2020	2,063	1,454	399	577	1,032	8,262
Additions	194	171	99	-	-	6,896
Write off	(1,675)	(26)	-	-	-	(2,107)
Balance at 31 December 2021	582	1,599	498	577	1,032	7,526
Additions	-	36	28	-	-	64
Write off	-	(39)	-	-	(729)	(630)
Balance at 31 December 2022	582	1,596	526	577	303	6,896
Depreciation and Amortization						
Balance at 1 January 2020	(1,851)	(752)	(365)	(186)	(604)	(4,638)
Depreciation and Amortization For the year	(47)	(134)	(33)	(61)	(80)	(915)
Balance at 1 January 2021	(1,898)	(886)	(398)	(247)	(684)	(5,908)
Depreciation and Amortization For the year	(46)	(170)	(16)	(92)	(83)	(874)
Write off	1,549	26	-	-	-	1,873
Balance at 31 December 2021	(395)	(1,030)	(414)	(339)	(767)	(3,741)
Depreciation and Amortization For the year	(29)	(225)	(26)	(105)	(56)	(793)
Write off	-	38	-	-	815	630
Balance at 31 December 2022	(424)	(1,217)	(440)	(444)	(8)	(959)
Carrying amount at 31 December 2020	165	568	1	330	348	2,354
Carrying amount at 31 December 2021	187	569	84	238	265	8,073
Carrying amount at 31 December 2022	158	379	86	133	295	6,988

The intangible assets comprised computer software and licenses.

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16 Property, equipment, Intangible assets and Right-of-use assets (continued)

Set out below are the carrying amounts of lease liabilities and the movements during the years:

	2022	2021
As at 1 January	6,751	1,084
Addition	-	6,828
Accrual of interest	207	90
Foreign exchange adjustments	(801)	22
Payments	(889)	(955)
Disposal of LL	-	(318)
As at 31 December	5,268	6,751

17 Other assets and liabilities

Other assets and liabilities as at December 2022, 31 December 2021 and 31 December 2020 comprise the following:

	2022	2021	2020
Other assets			
Settlement operations	729	1,167	650
Income tax asset	-	-	821
Repossessed assets	1,349	1,618	2,355
Receivables from problematic borrowers	366	394	443
Prepaid expenses	-	764	445
Other	898	307	35
Total other assets	3,342	4,250	4,749
Other liabilities			
Settlement operations	181	353	203
Finance Lease	5,275	6,751	1,084
Cash Cover	1,318	1,513	997
Other	2,044	1,569	698
Income tax liability	524	401	-
Total other liabilities	9,342	10,587	2,982

18 Amounts due to credit institutions

Amounts due to credit institutions as at December 2022, 31 December 2021 and 31 December 2020 comprise the following:

	2022	2021	2020
Vostro accounts	5,127	25,272	16,014
Term deposits	63,487	65,710	115,506
Short-term loan from NBG	15,014	-	5,001
	83,628	90,982	136,521

As at 31 December 2022 the Bank has placements from three banks (2021: four banks; 2020: four banks) with carrying values that individually exceed 10% of equity. The gross value of these balances as at 31 December 2022 is GEL 44,129 thousand (2021: GEL 81,610 thousand; 2020: GEL 126,272 thousand).

Loans from the National Bank of Georgia represent short-term GEL refinancing facilities used by the Bank to uphold its liquidity needs in GEL.

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19 Amounts due to customers

Amounts due to customers as at December 2022, 31 December 2021 and 31 December 2020 comprise the following:

	<u>2022</u>	<u>2021</u>	<u>2020</u>
Current accounts and demand deposits			
Retail	5,763	5,567	11,503
SME	11,729	6,905	6,230
Corporate	76,348	41,592	20,086
	<u>93,840</u>	<u>54,064</u>	<u>37,819</u>
Term deposits			
Retail	16,183	17,682	17,393
SME	1,367	1,498	695
Corporate	36,585	31,990	19,913
	<u>54,135</u>	<u>51,170</u>	<u>38,001</u>
Total amounts due to customers	<u>147,975</u>	<u>105,234</u>	<u>75,820</u>

As at 31 December 2022 the bank has customer's deposits balances with the amount of 30,963 thousand GEL (2021: 6,173; 2020: None) that serve as collateral for loans granted by the Bank. As at 31 December 2022 the Bank has placements from two customers (2021: two; 2020: none;) with carrying value that individually exceed 10% of equity.

20 Other borrowed funds

Other borrowed funds as at December 2022, 31 December 2021 and 31 December 2020 comprise the following:

	<u>2022</u>	<u>2021</u>	<u>2020</u>
Borrowings from financial institutions	57,596	73,782	29,188
Total other borrowed fund	<u>57,596</u>	<u>73,782</u>	<u>29,188</u>

Changes in liabilities arising from financing activities are as follows:

	<u>Other borrowed funds</u>
Carrying amounts at 31 December 2020	29,188
Proceed from issue	51,831
Redemption	(4,166)
Foreign currency translation	(3,071)
Other	-
Carrying amount at 31 December 2021	73,782
Proceed from issue	8,653
Redemption	(13,098)
Foreign currency translation	(11,741)
Other	-
Carrying amount at 31 December 2022	57,596

21 Capital management

The Bank maintains an activity managed capital base to cover risks inherent in the business and is meeting the capital adequacy requirements of the local banking supervisor, National Bank of Georgia. The adequacy of the Bank's capital is monitored using, among other measures, the rules and ratios established by Basel Committee on Banking Supervision (BIS rules/ratios) and adopted by the National Bank of Georgia in supervising the bank.

21 Capital management (continued)

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 exposures (statutory capital ratio) above the prescribed minimum level. The primary objectives of the Bank's capital management are to ensure that the Bank complies with externally imposed capital requirements set by the NBG and to safeguard the Bank's ability to continue as a going concern. The compliance with the capital adequacy ratios set by the NBG is monitored monthly with the reports outlining their calculation and are reviewed and signed by the Bank's CEO and CFO.

Basel III

In December 2017, the NBG has introduced approved amendments to the "Regulation on Capital Adequacy Requirements for Commercial Banks". Under the updated capital framework, capital requirements are divided into Pillar 1 Requirements for Common Equity Tier 1, Tier 1 and Regulatory Capital and additional buffers under Pillar 1 and Pillar 2.

Pillar 1

- ▶ The capital conservation buffer (which was incorporated in minimum capital requirements) is separated and set at 2.5%;
- ▶ A countercyclical capital buffer is currently set at 0%;
- ▶ A systemic risk buffer will be introduced for systematically important banks over the 4 years period.

Pillar 2

- ▶ A currency induced credit risk (CICR) buffer replaced conservative weighting for un-hedged FX loans denominated in foreign currencies;
- ▶ Concentration buffer for sectoral and single borrower exposure will be introduced;
- ▶ A net stress buffer will be introduced based on stress testing results provided by the Group;
- ▶ A General Risk-assessment Programme (GRAPE) buffer defined by the regulator, based on the Bank's specific risks.

In addition, specific PTI (payment to income) and LTV (loan to value) thresholds were introduced based on the new methodology. Exposures that do not meet pre-defined PTI and LTV limits are subject to weighting at higher rates.

Supervisory plan of the National Bank of Georgia with regard to COVID-19

With the intention to reduce the negative effects caused by coronavirus (COVID-19) pandemic and promote Georgian economy, the National Bank of Georgia has developed a temporary supervisory plan, which is in full compliance with the recommendations of the International Monetary Fund, European Central Bank and other leading financial authorities.

Immediate measures:

- 1). Postponement of growth (Phase-in) of Credit Risk Concentration Buffer (HHI) and Net GRAPE Buffer on Tier 1 capital (CET 1) and Tier 1 (Tier 1) in March, 2020;
- 2). Elimination of capital conservation buffer requirement (2.5%);
- 3). Decreasing the foreign currency induced credit risk buffer by 2/3.
- 4). Postponement of growth (Phase-in) of deduction of the provisions of foreign currency assets, created according to the rule of "Asset classification and possible loan losses" for the open currency position limit of the commercial banks.

NBG has also put in place a moratorium on any regulatory breaches of commercial banks caused by external factors such as additional credit losses, foreign exchange rate fluctuations and so on.

The NBG requires the Bank to maintain a minimum total capital adequacy ratio of 17.32%, Tier 1 Capital ratio of 11.79% and Core Tier 1 Capital ratio of 8.84% of risk-weighted assets, computed based on Basel III requirements.

21 Capital management (continued)

The Bank's capital adequacy ratios for the year ended 31 December calculated in accordance with NBG Basel II/III requirements were as follows:

	2022	2021	2020
Share capital	69,162	69,162	69,162
Retained earnings	42,176	25,441	14,154
Deductions	(242)	(211)	(318)
Total common equity and Tier 1 Capital	111,096	94,392	82,998
General loans loss provision (up to 1.25% of risk-weighted exposures)	5,077	4,932	4,423
Total regulatory capital	116,173	99,324	87,421
Risk-weighted exposures			
Credit risk-weighted exposure (balance and off-balance items)	406,191	394,563	353,850
Market risk-weighted exposures	602	1,580	1,464
Operational risk-weighted exposures	40,759	33,655	26,884
Total risk-weighted exposures	447,552	429,798	382,198
Common equity Tier 1 ratio	25%	22%	22%
Trial 1 capital ratio	25%	22%	22%
Total regulatory capital ratio	26%	23%	23%
Common equity Tier 1 ratio minimum requirements	9%	7%	6%
Trial 1 capital ratio minimum requirement	12%	9%	8%
Total regulatory capital minimum requirement	17%	16%	17%

The risk-weighted exposures 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.

22 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.;

22 Risk management, corporate governance and internal control (continued)

- ▶ 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 Bank's strong risk governance reflects the importance placed by Bank's Risks, Ethics and Compliance Committee on shaping the risk strategy and managing credit, financial and non-financial risks. All components necessary for comprehensive risk governance are embedded into risk organization structure: enterprise risk management; credit, financial and non-financial risks management; risk reporting and supporting IT infrastructure; cross-risk analytical tools and techniques such as capital adequacy management and stress-testing. The bank is exposed to credit risk, liquidity risk and market risk. It is also subject to various operating and business risks.

The risk management policies aim to identify, analyse 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. CRO 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 Risk Committee of Supervisory Council.

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 and ALCO. Such control arrangements guarantee that the Bank takes informed risk-taking decisions that are adequately priced, avoiding taking risks that are beyond the Bank's established threshold.

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 financial instruments will fluctuate due to changes in market variables such as interest rates, foreign exchange rates and equity prices. Market risk arises from open positions in interest rate 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.

22 Risk management, corporate governance and internal control (continued)

(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. Interest rate risk arises from potential changes in the market interest rates that can adversely affect the fair value or future cash flows of the financial instruments. This risk can arise from maturity mismatches of assets and liabilities, as well as from the re-pricing characteristics of such assets and liabilities. 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:

	Less than 3 months	3-6 months	6-12 months	1-5 years	More than 5 years	Carrying amount
31 December 2022 Assets						
Cash and cash equivalents	57,785	-	-	-	-	57,785
Amounts due from banks	-	-	-	-	-	-
Mandatory reserves at the NBG	39,030	-	-	-	-	39,030
Investment securities	996	-	-	1,357	-	2,353
Loans to customers	90,393	50,074	52,602	82,042	32,043	307,154
	188,204	50,074	52,602	83,399	32,043	406,322
Liabilities						
Accounts and deposits from banks	54,513	29,115	-	-	-	83,628
Current accounts and deposits from customers	128,736	12,282	6,317	640	-	147,975
Other borrowed funds	2,185	6,620	6,413	42,378	-	57,596
	185,434	48,017	12,730	43,018	-	289,199
	2,770	2,057	39,872	40,381	32,043	117,123
	Less than 3 months	3-6 months	6-12 months	1-5 years	More than 5 years	Carrying amount
31 December 2021 Assets						
Cash and cash equivalents	52,038	-	-	-	-	52,038
Amounts due from banks	4,616	2,576	1,553	-	-	8,745
Mandatory reserves at the NBG	38,427	-	-	-	-	38,427
Investment securities	1,497	3,833	2,966	6,163	-	14,459
Loans to customers	68,280	25,829	30,254	103,332	32,331	260,026
	164,858	32,238	34,773	109,495	32,331	373,695
Liabilities						
Accounts and deposits from banks	34,644	35,292	21,046	-	-	90,982
Current accounts and deposits from customers	86,146	8,273	5,482	5,333	-	105,234
Other borrowed funds	62	6,912	9,215	54,089	3,504	73,782
	120,852	50,477	35,743	59,422	3,504	269,998
	44,006	(18,239)	(970)	50,073	28,827	103,697
	Less than 3 months	3-6 months	6-12 months	1-5 years	More than 5 years	Carrying amount
31 December 2020 Assets						
Cash and cash equivalents	32,485	-	-	-	-	32,485
Amounts due from banks	9,190	-	-	-	-	9,190
Mandatory reserves at the NBG	36,217	-	-	-	-	36,217
Investment securities	2,999	-	1,490	13,549	-	18,038
Loans to customers	67,177	21,392	36,442	74,848	37,096	236,955
	148,068	21,392	37,932	88,397	37,096	332,885

22 Risk management, corporate governance and internal control (continued)

Liabilities

Accounts and deposits from banks	90,599	40,674	5,248	-	-	136,521
Current accounts and deposits from customers	49,520	2,052	23,007	1,241	-	75,820
Other borrowed funds	-	2,613	2,548	24,027	-	29,188
	140,119	45,339	30,803	25,268	-	241,529
	7,949	(23,947)	7,129	63,129	37,096	91,356

Average nominal interest rates

The table below displays average nominal interest rates for interest-bearing assets and liabilities as at 31 December 2022, 2021 and 2020. These interest rates are an approximation of the yields to maturity of these assets and liabilities.

	2022			2021			2020		
	Average nominal interest rate %			Average nominal interest rate %			Average nominal interest rate %		
	GEL	USD	EUR	GEL	USD	EUR	GEL	USD	EUR
Interest bearing assets									
Cash and cash equivalents	9.7%	2.4%	0.7%	8.5%	0%	0.1%	7.15%	1.25%	0%
Amounts due from banks	0.0%	0.0%	0.0%	0%	4.4%	0%	0%	4.0%	0%
Investment securities	9.2%	6.8%	0.0%	8.9%	6.6%	0%	7.4%	6.5%	0%
Loans to customers	14.0%	8.3%	6.5%	13.2%	6.8%	5.5%	11.5%	6.7%	5.5%
Interest bearing liabilities									
Deposits and balances from banks	11.0%	0.92%	0.6%	0%	0.8%	1.58%	7.93%	1.36%	1.13%
Deposits from customers	10.9%	2.1%	1.4%	6%	1.54%	0.8%	5.14%	1.87%	0.56%
Other borrowed funds	0.0%	7.0%	5.3%	0%	3.7%	3.1%	0%	4%	0%

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, assuming that all other variables, such as foreign currency exchange rates remain constant) 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 2022, 2021 and 2020, is as follows:

	2022	2021	2020
100 bps parallel fall	(232)	(197)	(175)
100 bps parallel rise	232	197	175

Sensitivity of equity (net of taxes) to a 100 bps shift of yield curve as at 31 December was as follows:

	2022	2021	2020
100 bps parallel fall	(188)	(167)	(149)
100 bps parallel rise	188	167	149

22 Risk management, corporate governance and internal control (continued)

(ii) Currency risk

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 Bank has assets and liabilities denominated in several foreign currencies.

The following table shows the foreign currency exposure structure of financial assets and liabilities as at 31 December 2022:

	<i>EUR</i>	<i>USD</i>	<i>TRY</i>	<i>GBP</i>	<i>Total</i>
Assets					
Cash and cash equivalents	11,702	36,627	17	1,252	49,598
Mandatory reserve at the NBG	12,555	26,475	-	-	39,030
Investment securities	-	1,357	-	-	1,357
Loans to customers	69,130	69,899	-	-	139,029
Other financial assets	138	113	-	-	251
Total assets	93,525	134,471	17	1,252	229,265
Liabilities					
Deposits and balances form banks	41,021	10,301	-	1,243	52,565
Current accounts and deposits from customers	16,589	98,280	10	2	114,881
Other borrowed funds	36,126	21,470	-	-	57,596
Other liabilities	8	1,441	-	-	1,449
Total liabilities	93,744	131,492	10	1,245	226,491
Net position	(219)	2,979	7	7	2,774

The following table shows the foreign currency exposure structure of financial assets and liabilities as at 31 December 2021:

	<i>EUR</i>	<i>USD</i>	<i>TRY</i>	<i>GBP</i>	<i>Total</i>
Assets					
Cash and cash equivalents	27,231	4,736	58	900	32,925
Amounts due from banks	-	8,745	-	-	8,745
Mandatory reserve at the NBG	22,938	15,489	-	-	38,427
Investment securities	-	6,163	-	-	6,163
Loans to customers	77,064	91,821	-	-	168,885
Other financial assets	169	157	1	-	327
Total assets	127,402	127,111	59	900	255,472
Liabilities					
Deposits and balances form banks	57,674	32,410	-	898	90,982
Current accounts and deposits from customers	34,411	48,494	79	2	82,986
Other borrowed funds	35,504	38,278	-	-	73,782
Other liabilities	394	1,282	75	-	1,751
Total liabilities	127,983	120,464	154	900	249,501
Net position	(581)	6,647	(95)	-	5,971

22 Risk management, corporate governance and internal control (continued)

The following table shows the foreign currency exposure structure of financial assets and liabilities as at 31 December 2020:

	<i>EUR</i>	<i>USD</i>	<i>TRY</i>	<i>GBP</i>	<i>Total</i>
Assets					
Cash and cash equivalents	2,469	24,489	24	710	27,692
Amounts due from banks	-	9,121	-	-	9,121
Mandatory reserve at the NBG	18,688	17,530	-	-	36,218
Investment securities	-	10,553	-	-	10,553
Loans to customers	73,938	68,670	-	-	142,608
Other financial assets	217	72	3	-	292
Total assets	95,312	130,435	27	710	226,484
Liabilities					
Deposits and balances form banks	90,584	40,226	-	711	131,521
Current accounts and deposits from customers	4,812	60,585	7	2	65,406
Other borrowed funds	-	29,188	-	-	29,188
Other liabilities	6	1,054	-	-	1,060
Total liabilities	95,402	131,053	7	713	227,175
Net position	(90)	(618)	20	(3)	(691)

A weakening of the Gel, as indicated below, against the following currencies at 31 December 2021, 2020 and 2019, 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.

	2022	2021	2020
20% appreciation of USD against GEL	506	1,130	(105)
20% appreciation of EUR against GEL	(37)	(99)	(15)
20% appreciation of TRY against GEL	1	(16)	3
20% appreciation of GBP against GEL	1	-	(1)

A strengthening of the GEL against the above currencies at 31 December 2021, 2020 and 2019 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.

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

22 Risk management, corporate governance and internal control (continued)

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.

Credit-related commitments risks

The Bank makes available to its customers guarantees which may require that the Bank make payments on their behalf.

They expose the Bank to similar risks to loans and these are mitigated by the same control processes and policies.

The maximum exposure to credit risk for the components of the statement of financial position, including derivatives, before the effect of mitigation through the use of master netting and collateral agreements, is best represented by their carrying amounts.

Where financial instruments are recorded at fair value, the carrying value represents the current credit risk exposure but not the maximum risk exposure that could arise in the future as a result of changes in values.

Impairment assessment

The Bank calculates ECL based on several probability-weighted scenarios to measure the expected cash shortfalls, discounted at an approximation to the EIR. A cash shortfall is the difference between the cash flows that are due to an entity in accordance with the contract and the cash flows that the entity expects to receive. The mechanics of the ECL calculations are outlined below and the key elements are as follows:

PD	The Probability of Default is an estimate of the likelihood of default over a given time horizon. A default may only happen at a certain time over the assessed period, if the facility has not been previously derecognised and is still in the portfolio.
EAD	The Exposure at Default is an estimate of the exposure at a future default date, taking into account expected changes in the exposure after the reporting date, including repayments of principal and interest, whether scheduled by contract or otherwise, expected drawdowns on committed facilities, and accrued interest from missed payments.
LGD	The Loss Given Default is an estimate of the loss arising in the case where a default occurs at a given time. It is based on the difference between the contractual cash flows due and those that the lender would expect to receive, excluding the realisation of any collateral. It is usually expressed as a percentage of the EAD.
LGL	The Loss Given Liquidation represents the percentage of the exposure that cannot be recovered from collateral liquidation if the exposure is defaulted.

The ECL allowance is based on the credit losses expected to arise over the life of the asset (the lifetime expected credit loss or LTECL), unless there has been no significant increase in credit risk since origination, in which case, the allowance is based on the 12 months' expected credit loss (12m ECL). The 12m ECL is the portion of LTECL that represent the ECLs that result from default events on a financial instrument that are possible within the 12 months after the reporting date. Both LTECL and 12mECL are calculated on an individual basis.

The Bank has established a policy to perform an assessment, at the end of each reporting period, of whether a financial instrument's credit risk has increased significantly since initial recognition, by considering the change in the risk of default occurring over the remaining life of the financial instrument. Based on the above process, the Bank groups its loans into Stage 1, Stage 2 and Stage 3, as described below:

Stage 1: When loans are first recognised, the Bank recognises an allowance based on 12m ECL. Stage 1 loans also include facilities where the credit risk has improved and the loan has been reclassified from Stage 2.

Stage 2: When a loan has shown a significant increase in credit risk since origination, the Bank classifies the loan as Stage 2 loan and records an allowance for the LTECL. Stage 2 loans also include facilities, where the credit risk has improved and the loan has been reclassified from Stage 3.

Retail clients are assigned Stage 2 category when following cases are met:

22 Risk management, corporate governance and internal control (continued)

GEL	INCOME	Latest available PTI	PTI increase =potential SICR
	< 1500	>25%	>=10 p.p.
	>=1000	>50%	>=10 p.p.
USD	INCOME	Latest available PTI	PTI increase =potential SICR
	< 1500	>20%	>=10 p.p.
	>=1500	>30%	>=10 p.p.

Corporate clients are assigned Stage 2 category when following cases are met:

DSCR Latest Updated	DSCR Delta vs Origination
< 1.2	<=-10%

Stage 3: Loans considered credit-impaired. The Bank records an allowance for the LTECL.

POCI: Purchased or originated credit impaired (POCI) assets are financial assets that are credit impaired on initial recognition. POCI assets are recorded at fair value at original recognition and interest revenue is subsequently recognised based on a credit-adjusted EIR. ECL are only recognised or released to the extent that there is a subsequent change in the lifetime expected credit losses.

POCI status is assigned to a financial instrument in following cases:

- In the event of termination of a financial instrument as a result of restructuring and the emergence of a new financial instrument in its place, the new financial instrument will be granted POCI status.
- Besides restructuring, a newly originated financial instrument bears signs of credit impairment such as violation of Real PTI requirements (for retail borrowers) or DSCR < 1.0 (for legal entities).
- The Bank has initiated repossession process of a borrower's collateral or part of claim has been decreased by a write-off, as a result of which the existing financial instrument is replaced by a newly emerged financial instrument, the remaining claim is assigned POCI status. Exceptions from this rule should be documented.

POCI is assigned to the instrument level. Financial instruments which are assigned POCI status are will be classified in Stage 3, which will lead to all financial instruments of the borrower to be classified in Stage 3, according to the contagious principle. However, POCI status will remain at the financial instrument level.

Definition of default and cure

The Bank's definition of default is based on quantitative and qualitative criteria. An instrument is classified as credit impaired if:

- ▶ Payments of interest, principal or fees by obligor are overdue for more than 90 days; or
- ▶ If a problematic restructuring of a loan took place, which otherwise would become defaulted; or
- ▶ There is an event which have a detrimental impact on the estimated future cash flows of the borrower endangering its ability to repay liabilities in full, when bankruptcy or insolvency proceedings of enforced liquidation have commenced or there is other evidence that payment obligations will not be fully met.

In terms of measurable indicators, following criteria are monitored as following:

For legal entities	Indicator
For Sectors: Hotels, Energy, Real Estate Management	DSCR < 1.0 (recalculated on 15 years)
For Other Sectors	DSCR < 1.0 (recalculated on 10 years)

22 Risk management, corporate governance and internal control (continued)

For retail clients	Indicator
Monthly net income (in GEL or FCY in GEL equivalent)	
< 1,500	PTI > 55%
>= 1,500	PTI > 70%

In case, above measurable indicators are met, the borrower is considered as defaulted and transferred into Stage 3.

Once financial instrument is classified to Stage 2 it remains so until following two conditions are met:

1. The financial instrument should fulfil requirements for standard loan category as defined by NBG;
2. Overdue days and probation period conditions should be met.

If these two conditions are met, then the instrument is classified as Stage 1.

A loan is classified as standard if:

- ▶ The payments are done on time or overdue days do not exceed 30 days;
- ▶ The borrower's liquidity, capital and loan repayment capacity is stable;
- ▶ The borrower is financially sufficiently strong to absorb medium level stress outcomes, and has enough liquidity to service all liabilities.

As for overdue days and probation period, for non-restructured Stage 2 instruments, probation period is 6 months, during which the instrument must not fall in more than 30 days overdue.

For restructured performing Stage 2 financial instrument the probation period is 1 year (during which it should not fall in more than 30 days overdue and fulfil standard loan category requirements) after which the instrument is reclassified to Stage 1.

Cure period for non-restructured Stage 3 financial instruments is 6 months, after which the instrument is classified at Stage 1 if during the probation period the financial instrument was not more than 30 days overdue and fulfils standard loan category requirements, and is classified at Stage 2 if the instrument was 30-90 days overdue during the cure period.

For restructured Stage 3 financial instrument the cure period is 6 months, after which the instrument is classified as Stage 2 (Performing Restructured) if the instrument was not more than 90 days overdue during the cure period. As soon as the financial instrument is classified as Performing Restructured, starts 1 year probation period, after which the instrument is classified as Stage 1 if the instrument was not more than 30 days overdue during the probation period and fulfils standard loan category requirements. If the instrument falls in 30-90 days overdue it remains in Stage 2. One year probation period starts from the last month when the instrument last recovered from 30-90 days overdue.

PD estimation process

For retail and corporate portfolios PD is estimated through macro model, which describes relationship between historical PDs for retail and corporate portfolios and macroeconomic variables such as real GDP growth and USD/GEL exchange rate. Based on estimation results and predicted macro variables provided by the NBG conditional retail and corporate PDs are forecasted. The model will be re-estimated annually and other macroeconomic variables will be incorporated if they improve explanatory power of the model. With the forecasted conditional PD's migration matrices are constructed, from which unconditional marginal PD's are calculated that are further adjusted by age of the instrument in the portfolio.

PD for stage 3 financial instruments is considered as 100%.

For the loans, on which the Bank has surety from parent companies of the borrower, the Bank uses PDs of their parents.

Exposure at default

The exposure at default (EAD) is calculated differently for Stage 1, Stage 2 and Stage 3 financial instruments. EAD are reduced by cash cover amounts. Off-balance commitments are considered through Cash Conversion Factor (CCF), specifically by 100% for corporate commitments and 50% for retail commitments.

22 Risk management, corporate governance and internal control (continued)

For Stage 1, the EAD are calculated as an outstanding amount of loans and off balance commitments taking into account CCF and cash cover amounts as of reporting date.

For Stage 2 and Stage 3, the EAD is calculated as the outstanding amount of the instrument by the reporting date taking into account CCF and cash cover amounts.

Loss given default

For corporate and retail lending assets, LGD values are assessed annually. LGD is defined as the likely loss arising in case of a counterparty defaults for unsecured exposures. It provides an estimation of the exposure that cannot be recovered in a default event and therefore captures the severity of a loss. LGD rate are calculated for corporate and retail portfolios. LGD is statistically calculated based on historical loan recovery data and takes into account historical losses incurred on unsecured exposures. While calculation LGD outlier recoveries are excluded from the calculation. LGD is expressed as a percentage of the EAD.

Loss Given Liquidation of collateralized exposures (LGL):

LGL represents the percentage of the exposure that cannot be recovered from collateral liquidation if the exposure is defaulted. Loss Given Liquidation calculation takes into account LTV, adjusted by time to sale of movable and immovable collateral, real estate price index, EIR, and expected sales ratio of collaterals. For uncollateralized exposures LGL is taken at 100%.

Average LGL ratios are calculated for five LTV bands separately for retail and non-retail borrowers, which then are assigned to each exposure depending on the LTV band the exposure falls.

Sales costs calculation:

The Bank considers following sales costs associated with sale of received collateral. In case the Bank's claim is over GEL 15,000, the Bank goes to Arbitration. For claims below GEL 15,000 the Bank goes to a Court.

Costs associated with Arbitration cases

VAT	18%	When demand x 1.18 is less than collateral value, in such case VAT is calculated from demand and vice versa. Including VAT, NOTE: min prices is GEL 236 (Without oral Hearing) /GEL 590 (Based on oral hearing)/GEL 708 Oral hearing when composed of 3 arbitrators), max prices is GEL 15,000.
Arbitration fee	3%	The Bank has the following approach in contracts: when the claim is ≤ GEL 50,000 the Bank goes without oral Hearing (i.e. minimal price GEL 236) / When the claim is > GEL 50,000 the Bank goes with an oral hearing consisting of 3 arbitrators (i.e. minimal price GEL 708).
Court of appeal fee	GEL150	
Fee paid to Enforcement	2%	From the total request (principal + arbitration fee + court of appeal fee)
Commission taken by the enforcement beraue	5%	From the selling price in auction

Costs associated with Court cases

VAT	18%	When demand x 1.18 is less than collateral value, in such case VAT is calculated from demand and vice versa.
Court fee	3%	Min price: GEL 100, max price: GEL 5,000
Fee paid to Enforcement	2%	From the total request (principal)
Commission taken by the enforcement beraue	5%	From the selling price in auction

22 Risk management, corporate governance and internal control (continued)

Significant increase in credit risk (SICR)

The Bank continuously monitors all assets subject to ECLs. When assessing significance of increase in credit risk and whether the instrument is subject to 12m ECL or LTECL, the Bank compares the risk of default at the reporting date and risk of default occurring at the date of initial recognition. To identify significant increase in credit risk since initial recognition of the financial asset at individual financial instrument level, the Bank is undertaking the holistic analysis of various factors, including those which are specific to a particular financial instrument or to a borrower.

The analysis includes considering of quantitative and qualitative information based on the Bank's historical experience, credit risk assessment and forward looking information.

For individually significant exposures the Bank evaluates individually whether an objective evidence of significant increase in credit risk or impairment exists to recognise lifetime expected credit losses. Individually significant exposures are considered exposures to the group exceeding 1% of the tier I capital of the bank. The Bank collectively assesses loans that are not individually significant and loans that are individually significant but for which there is no objective evidence of significant increase in credit risk.

Individually significant loans

SICR identification process for individually significant exposures includes performing a qualitative test. To assess SICR for individually significant loans the Bank has established general trigger events for all types of exposures, specific trigger events for non-retail borrowers and specific trigger events for retail borrowers. General trigger events include but are not limited to:

- ▶ Deterioration of macroeconomic, regulatory, political or technological outlook relevant to particular or group of borrowers;
- ▶ Adverse changes in the sector or industry conditions in which borrower operates.

Specific trigger events for non-retail borrowers include:

- ▶ Deterioration of borrowers' financial performance that is quantified by adverse changes in financial coefficients;
- ▶ Being overdue more than 30 days but less than 90 days;
- ▶ Those restructurings which if had not been done would not lead to the instrument falling in more than 90 days overdue;
- ▶ Breaching the contract;
- ▶ Sale of crucial part of the business or property which is necessary for the borrower's profit making operations;
- ▶ Fraud in borrower's business, etc.

If significant increase in credit risk is identified, for lifetime ECL calculation it is assessed whether future cash inflows of the borrower are enough to cover the cash outflows for different scenarios. Analysis of cash flow of the borrower includes analysis of existing and forecasted trends of industry within which the borrower operates. 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.

Collectively assessed loans

Non-retail exposures that are not individually significant are assessed for SICR based on overdue days (between 30 and 90 days), whether they are restructured and if not restructured whether they would fall in more than 90 days overdue, and deterioration of various financial coefficients (Payment To Income (PTI), Debt/EBITDA, Equity/Assets, Interest Coverage Ratio (ICR) and Debt Service Coverage Ratio (DSCR)).

Specific trigger events for retail borrowers include but are not limited to loan being overdue more than 30 days but less than 90 days, restructuring of an exposure which if would not be done would lead to the instrument falling in more than 90 days overdue, deterioration of PTI ratio, etc.

For the purpose of a collective evaluation of impairment, financial instruments are grouped within homogeneous pools on the basis of asset types – whether the instrument is retail or non-retail, and based on Loan to Value (LTV) ratio. On the basis of LTV ratios financial instruments are grouped into five LTV bands.

Writing-off of facilities:

The Bank has elaborated the methodology for writing-off of exposures towards the borrowers, specifically as following:

22 Risk management, corporate governance and internal control (continued)

Written-off conditions:

Unsecured financial instrument is subject to be written off if overdue days exceed 360 days;

Secured financial instrument is subject to be written off if overdue days exceed 720 days.

Write-off is understood as creation of provisions on the facility that equal to EAD.

Treasury and interbank relationships

The Bank's treasury and interbank relationships and counterparties comprise financial services institutions, banks, corporates and Georgian and Turkish governments.

PDs are assigned to issuers or banks according to external rating default rates. The minimum PD is set to 0.05% according to Basel. LGD is taken at 41.90%, according to the foundation approach of the Basel document. For corporate securities LGD is taken at 56.89%. This figure represents the average historical recoveries of the Bank starting from 2014. EAD represents monthly average of outstanding exposures in the case of securities and sovereign bonds and monthly average outstanding amount of principal plus accrued interest for interbank exposures.

Forward-looking information and multiple economic scenarios

In its ECL models, the Bank relies on the following forward looking information as economic inputs, such as:

- ▶ GDP growth;
- ▶ Foreign exchange rates.

The Bank calculates ECL on an individual basis for all financial assets. ECL is calculated for three (Baseline 50%, Upside 25%, and Adverse 25%) scenarios and weighted ECL is computed as a weighted sum of all three scenario ECLs.

The Bank obtains the forward-looking information from the NBG. The tables below show the values of the forward looking economic variables/assumptions used in each of the economic scenarios for the ECL calculations:

The figures for "Subsequent years" represent a long-term average and so are the same for each scenario as at 31 December 2022:

Key drivers	ECL scenario	Assigned probabilities,				Subsequent years	
		%	2022	2023	2024		2025
GDP growth, %	Upside	25%	10%	6%	5%	5%	5%
	Base case	50%	10%	4%	5.5%	5%	5%
	Downside	25%	10%	2%	4%	5%	5%
GEL/USD exchange rate, % change	Upside	25%	0%	2%	0%	0%	0%
	Base case	50%	0%	0%	0%	0%	0%
	Downside	25%	0%	-15%	5%	5%	5%

22 Risk management, corporate governance and internal control (Continued)

The figures for “Subsequent years” represent a long-term average and so are the same for each scenario as at 31 December 2021:

Key drivers	ECL scenario	Assigned probabilities,	2022	2023	2024	Subsequent years
		%				
GDP growth, %						
	Upside	25%	6%	5%	5%	5%
	Base case	50%	5%	4.5%	4.5%	4.5%
	Downside	25%	1%	4%	4%	4%
USD/GEL exchange rate, % change						
	Upside	25%	-5%	-5%	0%	0%
	Base case	50%	0%	0%	0%	0%
	Downside	25%	0%	0%	0%	0%

The figures for “Subsequent years” represent a long-term average and so are the same for each scenario as at 31 December 2020:

Key drivers	ECL scenario	Assigned probabilities,	2021	2022	2023	Subsequent years
		%				
GDP growth, %						
	Upside	25%	6%	5%	5%	5%
	Base case	50%	5%	4.5%	4.5%	4.5%
	Downside	25%	1%	4%	4%	4%
USD/GEL exchange rate, % change						
	Upside	25%	-5%	-5%	0%	0%
	Base case	50%	0%	0%	0%	0%
	Downside	25%	10%	-5%	0%	0%

(f) Liquidity risk

Liquidity risk is defined as the risk that the Bank does not have sufficient liquid financial resources to meet obligations associated with financial liabilities that are settled by delivering cash or another financial asset. Liquidity risk arises because of the possibility that the Bank might be unable to meet its payment obligations when they fall due as a result of mismatches in the timing of the cash flows under both normal and stress circumstances. The Bank maintains liquidity management with the objective of ensuring that funds will be available at all times to honour 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.

22 Risk management, corporate governance and internal control (Continued)

The liquidity position is monitored by the Finance Management Division 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 ALCO and implemented by the Treasury Division. In addition, the Bank monitors on a regular basis the liquidity ratio calculated in accordance with the NBG requirements.

22 Risk management, corporate governance and internal control (Continued)

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 2022 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
Non-derivative liabilities								
Deposits and balances from banks	(39,837)	(14,928)	(29,439)	-	-	-	(84,204)	(83,628)
Current accounts and deposits from customers	(122,225)	(6,569)	(12,557)	(6,660)	(661)	-	(148,672)	(147,975)
Other borrowed funds	-	-	(2,194)	-	(65,790)	-	(67,984)	(57,596)
Other liabilities	(4,857)	(88)	(132)	(268)	(2,334)	(2,427)	(10,106)	(10,106)
Total financial liabilities	(166,919)	(21,585)	(44,322)	(6,928)	(68,785)	(2,427)	(310,966)	(299,305)
Credit related commitments	(95,990)	-	-	-	-	-	-	(95,990)

The maturity analysis for financial liabilities as at 31 December 2021 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
Non-derivative liabilities								
Deposits and balances from banks	(25,272)	(9,426)	(35,552)	(21,280)	-	-	(91,530)	(90,982)
Current accounts and deposits from customers	(57,384)	(28,941)	(8,336)	(5,592)	(5,508)	-	(105,761)	(105,234)
Other borrowed funds	-	-	-	-	(83,594)	-	(83,594)	(73,782)
Other liabilities	(4,959)	(147)	(232)	(232)	(3,285)	(2,734)	(11,589)	(11,589)
Total financial liabilities	(87,615)	(38,514)	(44,120)	(27,104)	(92,387)	(2,734)	(292,474)	(281,587)
Credit related commitments	(110,543)	-	-	-	-	-	-	(110,543)

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22 Risk management, corporate governance and internal control (Continued)

The maturity analysis for financial liabilities as at 31 December 2020 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	gross amount inflow (outflow)	Carrying amount
Non-derivative liabilities								
Deposits and balances from banks	(80,686)	(9,989)	(40,949)	(5,299)	-	-	(136,923)	(136,521)
Current accounts and deposits from customers	(40,687)	(8,873)	(2,074)	(23,314)	(1,297)	-	(76,245)	(75,820)
Other borrowed funds	-	-	-	-	(33,156)	-	(33,156)	(29,188)
Other liabilities	(3,241)	(159)	(721)	(125)	-	-	(4,246)	(4,246)
Total financial liabilities	(124,614)	(19,021)	(43,744)	(28,738)	(34,453)	-	(250,570)	(245,775)
Credit related commitments	(74,830)	-	-	-	-	-	-	(74,830)

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 stated maturity dates is presented below:

	2022	2021	2020
Demand and less than 1 month	7,723	7,873	13,675
From 1 to 3 month	6,591	4,037	7,828
From 3 to 12 month	7,543	6,006	6,153
From 1 to 5 years	88	5,333	1,240
More than 5 years	-	-	-
	21,945	23,249	28,896

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22 Risk management, corporate governance and internal control (Continued)

The table below shows an analysis, by expected maturities, of amounts recognized in the statement of financial position as at 31 December 2022:

	Demand and less than 1 month	From 1 to 3 month	From 3 to 12 month	From 1 to 5 years	More than 5 years	No maturity	Total
Assets							
Cash and cash equivalents	57,785	-	-	-	-	-	57,785
Mandatory reserves at the NBG	39,030	-	-	-	-	-	39,030
Investment securities	996	-	-	1,357	-	-	2,353
Loans to customers	51,171	44,519	122,188	70,233	19,043	-	307,154
Property, equipment and intangible assets And ROU	-	-	-	-	-	6,988	6,988
Other assets	3,342	-	-	-	-	-	3,342
Total assets	152,324	44,519	122,188	71,590	19,043	6,988	416,652
Liabilities							
Deposits and balance from banks	54,513	29,115	-	-	-	-	83,628
Current accounts and deposits from Customers	121,620	7,116	18,599	640	-	-	147,975
Other borrowed funds	-	2,184	6,620	6,413	42,379	-	57,596
Other liabilities	4,857	88	400	2,334	2,427	-	10,106
Total liabilities	180,990	38,503	25,619	9,387	44,806	-	299,305
Net position	(28,666)	6,016	96,569	62,203	(25,763)	6,988	117,347

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22 Risk management, corporate governance and internal control (Continued)

The table below shows an analysis, by expected maturities, of amounts recognized in the statement of financial position as at 31 December 2021:

	Demand and less than 1 month	From 1 to 3 month	From 3 to 12 month	From 1 to 5 years	More than 5 years	No maturity	Total
Assets							
Cash and cash equivalents	52,038	-	-	-	-	-	52,038
Amounts due from banks	1,832	2,784	4,129	-	-	-	8,745
Mandatory reserves at the NBG	38,427	-	-	-	-	-	38,427
Investment securities	1,497	-	6,799	6,163	-	-	14,459
Loans to customers	8,269	64,137	81,168	88,938	17,514	-	260,026
Property, equipment and intangible assets And ROU	-	-	-	-	-	8,073	8,073
Other assets	4,250	-	-	-	-	-	4,250
Total assets	106,313	66,921	92,096	95,101	17,514	8,073	386,018
Liabilities							
Deposits and balance from banks	25,272	9,372	56,338	-	-	-	90,982
Current accounts and deposits from customers	57,381	28,765	13,755	5,333	-	-	105,234
Other borrowed funds	-	-	16,189	54,089	3,504	-	73,782
Other liabilities	4,959	147	464	3,285	2,734	-	11,589
Total liabilities	87,612	38,284	86,746	62,707	6,238	-	281,587
Net position	18,701	28,637	5,350	32,394	11,276	8,073	104,431

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22 Risk management, corporate governance and internal control (Continued)

The table below shows an analysis, by expected maturities, of amounts recognized in the statement of financial position as at 31 December 2020:

	Demand and less than 1 month	From 1 to 3 month	From 3 to 12 month	From 1 to 5 years	More than 5 years	No maturity	Total
Assets							
Cash and cash equivalents	32,485	-	-	-	-	-	32,485
Amounts due from banks	-	9,190	-	-	-	-	9,190
Mandatory reserves at the NBG	36,217	-	-	-	-	-	36,217
Investment securities	2,999	-	1,490	13,549	-	-	18,038
Loans to customers	8,330	58,848	57,835	74,848	37,094	-	236,955
Property, equipment and intangible assets And ROU	-	-	-	-	-	2,354	2,354
Other assets	4,749	-	-	-	-	-	4,749
Total assets	84,780	68,038	59,325	88,397	37,094	2,354	339,988
Liabilities							
Deposits and balance from banks	80,672	9,928	45,921	-	-	-	136,521
Current accounts and deposits from customers	40,684	8,836	25,059	1,241	-	-	75,820
Other borrowed funds	-	-	5,161	24,027	-	-	29,188
Other liabilities	3,241	159	721	125	-	-	4,246
Total liabilities	124,597	18,923	76,862	25,393	-	-	245,775
Net position	(39,817)	49,115	(17,537)	63,004	37,094	2,354	94,213

22 Risk management, corporate governance and internal control (Continued)

(g) Operational and business risk

Operational risk is the risk of loss arising from system failure, human error, fraud and external events. When controls fail to operate effectively, operational risks can cause damage to reputation, have legal or regulatory implications, or lead to financial loss. The bank cannot expect to eliminate all operational risks, but it endeavours to manage these risks through a control framework and by monitoring and responding to potential risks. Controls include effective segregation of duties, access, authorisation and reconciliation procedures, staff education and assessment procedures, such as the use of internal audit.

23 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 and financial guarantees 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 represent the maximum accounting loss that would be recognised at the reporting date if the counterparties failed completely to perform as contracted.

	<u>2022</u>	<u>2021</u>	<u>2020</u>
Contracted amount			
Undrawn overdraft facilities	54	30	52
Letter of Credit	1,210	2,690	1,782
Guarantees	<u>94,726</u>	<u>107,823</u>	<u>72,996</u>
	<u>95,990</u>	<u>110,543</u>	<u>74,830</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 as at 31 December 2022 accounting GEL 67,218 thousand are to six banks (2021: GEL 76,980 thousand, 2020: GEL 46,501 thousand). This exposure represents a significant concentration of credit risk exposure to the Bank.

All credit related commitments are allocated to Stage 1. ECL recognized for credit related commitments as at 31 December 2022 was GEL 387 thousand and there were no significant movements in ECL during the year (Note 7).

24 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.

(b) Litigations

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.

24 Contingencies (Continued)

(c) Operating environment

As an emerging market, Georgia does not possess a well-developed business and regulatory infrastructure that would generally exist in a more mature market economy. Operations in Georgia may involve risks that are not typically associated with those in developed markets. However, over the last few years the Georgian government has made a number of developments that positively affect the overall investment climate of the country, specifically implementing the reforms necessary to create banking, judicial, taxation and regulatory systems. This includes the adoption of a new body of legislation (including new Tax Code and procedural laws). In the view of the management, these steps contribute to mitigate the risks of doing business in Georgia.

The existing tendency aimed at the overall improvement of the business environment is expected to persist. The future stability of the Georgian economy is largely dependent upon these reforms and developments and the effectiveness of economic, financial and monetary measures undertaken by the Government. However, the Georgian economy is vulnerable to market downturns and economic slowdowns elsewhere in the world.

(d) 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.

25 Related party transaction

In accordance with IAS 24 "Related Party Disclosures", parties are considered to be related if one party has the ability to control the other party or exercise significant influence over the other party in making financial or operational decisions. In considering each possible related party relationship, attention is directed to the substance of the relationship, not merely the legal form.

Related parties may enter into transactions which unrelated parties might not, and transactions between related parties may not be effected on the same terms, conditions and amounts as transactions between unrelated parties. All transactions with related parties disclosed below have been conducted on an arm's length basis.

(a) Control relationships

The Bank 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 2022, 2021 and 2020 is as follows:

	2022	2021	2020
Short-term employee benefits	1,863	1,927	2,133

25 Related party transaction (Continued)

Loans to and deposits from the key management personnel and respective interest income and expenses were immaterial as at 31 December 2022, 2021 and 2020 and for the years then ended.

(c) Transactions with the related parties

The outstanding balances and related profit or loss amounts of transactions as at and for the year ended 31 December 2021, 2020 and 2019 are as follows:

	2022	2021	2020
Statement of financial position			
Assets			
Cash and cash equivalents			
- In TRY	17	36	13
- In EUR	45	1,135	19
- In USD	27	14	8
Amounts due from banks			
- In USD	-	912	-
Liabilities			
Deposits and balances from banks			
- In EUR	7,561	18,900	1,388
- In USD	2,092	23,038	13,915
- In GBP	1,243	898	711
- In TRY	-	-	-
Income/(expense)			
Interest income	13	28	7
Interest expense	(208)	(840)	(263)

The deposits from the Parent as at 31 December 2022 mature according to contractual maturity as follows: GEL 10,896 thousand matures in less than 12 months (2021:GEL 25,272 thousand matures in less than 12 months ; 2020:GEL 16,014 thousand matures in less than 12 months).

26 Fair Value measurement

(a) Fair values estimates and assumptions

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.

The following describes the methodologies and assumptions used to determine fair values for assets and liabilities recorded at fair value in the financial statements and those items that are not measured at fair value in the statement of financial position, but whose fair value is disclosed.

Assets for which fair value approximates carrying value

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

Derivatives

Derivatives valued using a valuation technique with market observable inputs are mainly interest rate swaps, currency swaps and forward foreign exchange contracts. The most frequently applied valuation techniques include forward pricing and swap models, using present value calculations. The models incorporate various inputs including the credit quality of counterparties, foreign exchange spot and forward rates and interest rate curves. Derivatives valued using a valuation technique with significant non-market observable inputs are primarily long dated option contracts. These derivatives are valued using the binomial models. The models incorporate various non-observable assumptions, which include market rate volatilities.

26 Fair Value measurement (Continued)

Trading securities and investment securities

Trading securities and investment securities valued using a valuation technique or pricing models primarily consist of unquoted equity and debt securities. These securities are valued using models which sometimes only incorporate data observable in the market and at other times use both observable and non-observable data. The non-observable inputs to the models include assumptions regarding the future financial performance of the investee, its risk profile, and economic assumptions regarding the industry and geographical jurisdiction in which the investee operates.

Financial assets and financial liabilities carried at amortised cost

Fair value of the quoted notes and bonds is based on price quotations at the reporting date. The fair value of unquoted instruments, loans to customers, customer deposits, amounts due from credit institutions and amounts due to the NBG and credit institutions and other financial assets and liabilities, obligations under finance leases is estimated by discounting future cash flows using rates currently available for debt on similar terms, credit risk and remaining maturities.

(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.

For the purpose of fair value disclosures, the Bank has determined classes of assets and liabilities on the basis of the nature, characteristics and risks of the asset or liability and the level of the fair value hierarchy as explained above.

Set out below is a comparison by class of the carrying amounts and fair values of the Bank's financial instruments. The table does not include the fair values of non-financial assets and non-financial liabilities.

31 December 2022	Level 1	Level 2	Level 3	Total fair Value	Carrying amount
Assets measured at fair value					
Debt securities measured at					
FVOCI	2,353	-	-	2,353	2,353
Assets for which fair values are disclosed					
Loans to customers	-	-	307,154	307,154	307,154
Liabilities for which fair values are disclosed					
Amounts due to customers	-	231,603	-	231,603	231,603

26 Fair value measurement (Continued)

31 December 2021	Level 1	Level 2	Level 3	Total fair Value	Carrying amount
Assets measured at fair value					
Debt securities measured at FVOCI					
FVOCI	14,459	-	-	14,459	14,459
Assets for which fair values are disclosed					
Loans to customers	-	-	260,026	260,026	260,026
Liabilities for which fair values are disclosed					
Amounts due to customers	-	196,216	-	196,216	196,216
31 December 2020	Level 1	Level 2	Level 3	Total fair Value	Carrying amount
Assets measured at fair value					
Debt securities measured at FVOCI					
FVOCI	18,038	-	-	18,038	18,038
Assets for which fair values are disclosed					
Loans to customers	-	-	236,955	236,955	236,955
Liabilities for which fair values are disclosed					
Amounts due to customers	-	212,341	-	212,341	212,341

27 Presentation of financial instruments by measurement category

For the measurement purposes, IFRS 9, classified financial assets into the categories discussed in Note 3. The following table provides a reconciliation of classes of financial assets with these measurement categories as of 31 December 2022:

	Amortized cost	FVOCI	FVPL	Total
Assets				
Cash and cash equivalents	57,785	-	-	57,785
Amounts due from banks	-	-	-	-
Mandatory reserves at NBG	39,030	-	-	39,030
Investment Securities	-	2,353	-	2,353
Loans to customers	307,154	-	-	307,154
Other assets	3,342	-	-	3,342
Total financial assets	407,311	2,353	-	409,664

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27 Presentation of financial instruments by measurement category (Continued)

The following table provides a reconciliation of classes of financial assets with these measurement categories as of 31 December 2021:

	<u>Amortized cost</u>	<u>FVOCI</u>	<u>FVPL</u>	<u>Total</u>
Assets				
Cash and cash equivalents	52,038	-	-	52,038
Amounts due from banks	8,745	-	-	8,745
Mandatory reserves at NBG	38,427	-	-	38,427
Investment Securities	-	14,459	-	14,459
Loans to customers	260,026	-	-	260,026
Other assets	4,250	-	-	4,250
Total financial assets	<u>363,486</u>	<u>14,459</u>	<u>-</u>	<u>377,945</u>

The following table provides a reconciliation of classes of financial assets with these measurement categories as of 31 December 2020:

	<u>Amortized cost</u>	<u>FVOCI</u>	<u>FVPL</u>	<u>Total</u>
Assets				
Cash and cash equivalents	32,485	-	-	32,485
Amounts due from banks	9,190	-	-	9,190
Mandatory reserves at NBG	36,217	-	-	36,217
Investment Securities	-	18,038	-	18,038
Loans to customers	236,955	-	-	236,955
Other assets	4,749	-	-	4,749
Total financial assets	<u>319,596</u>	<u>18,038</u>	<u>-</u>	<u>337,634</u>

28 Events after reporting date

There were no significant events after the reporting date that need to be presented in the financial statement.