“Yapi Kredi Bank Azerbaijan” CJSC

International Financial Reporting Standards Financial Statements and Independent Auditor’s Report

31 December 2019

Contents

Independent auditor's report

To the Shareholders and Board of Directors of the "Yapi Kredi Bank Azerbaijan" CJSC:

Our opinion

In our opinion, the financial statements present fairly, in all material respects, the financial position of "Yapi Kredi Bank Azerbaijan" CJSC (the "Bank") as at 31 December 2019, and its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards.

What we have audited

The Bank's financial statements comprise:

- the statement of financial position as at 31 December 2019;
- the statement of profit or loss and other comprehensive income for the year then ended;
- the statement of changes in equity for the year then ended;
- the statement of cash flows for the year then ended; and
- the notes to the financial statements, which include significant accounting policies and other explanatory information.

Basis for opinion

We conducted our audit in accordance with International Standards on Auditing (ISAs). Our responsibilities under those standards are further described in the Auditor's responsibilities for the audit of the financial statements section of our report.

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

Independence

We are independent of the Bank in accordance with the International Ethics Standards Board for Accountants' Code of Ethics for Professional Accountants (IESBA Code). We have fulfilled our other ethical responsibilities in accordance with the IESBA Code.

Responsibilities of management and those charged with governance for the financial statements

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

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

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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 ISAs will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

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

- Identify and assess the risks of material misstatement of the 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 those charged with governance regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

PricewaterhouseCoopers Audit Azerbaijan LLC

January 31, 2020

Baku, the Republic of Azerbaijan

Yapi Kredi Bank Azerbaijan CJSC
Statement of Financial Position
(Amounts expressed in thousands of Azerbaijani Manats)

	Notes	31 December 2019	31 December 2018
ASSETS			
Cash and cash equivalents	7	202,396	163,432
Notes issued by Central Bank of Azerbaijan Republic and other bonds	10	36,536	45,226
Amounts due from credit institutions	8	20,986	62,030
Loans to customers	9	160,678	144,831
Property and equipment	11	3,874	4,573
Intangible assets	12	7,890	7,940
Right of Use Assets	13	5,751	-
Other assets	15	8,936	7,793
TOTAL ASSETS		**447,047**	**435,825**
LIABILITIES			
Amounts due to credit institutions	16	10,051	7,270
Amounts due to customers	17	330,609	335,050
Current income tax liabilities		-	113
Deferred income tax liabilities	14	2,116	2,145
Other liabilities	15	12,922	6,093
TOTAL LIABILITIES		**355,698**	**350,671**
EQUITY			
Share capital	18	55,381	55,381
Retained earnings		35,968	29,773
TOTAL EQUITY		**91,349**	**85,154**
TOTAL LIABILITIES AND EQUITY		**447,047**	**435,825**

Signed and authorized for release on behalf of the Management Board of the Bank on 31 January 2020:

Cenk Yüksel
Chief Executive Officer / General Director

Matanat Gasimova
Chief Accountant

Ramin Saftarov
Chief of Financial Reporting Department

YAPI KREDI BANK AZƏRBAYCAN

(Amounts expressed in thousands of Azerbaijani Manats)

	Notes	2019	2018
Interest income			
Loans to customers		19,776	25,689
Amounts due from credit institutions		3,979	5,245
Investment securities		2,633	3,775
Interest expense			
Amounts due to customers		(2,887)	(4,767)
Amounts due to lease liability		(360)	-
Amounts due to credit institutions		(169)	(126)
Net interest income		**22,972**	**29,816**
Credit loss allowance		(637)	(7,738)
Net interest income after credit loss allowance		**22,335**	**22,078**
Net fee and commission income	20	4,957	5,241
Gains less losses from trading in foreign currencies		3,645	4,984
Net losses from currency translation differences		(14)	(62)
Other income		48	52
Non-interest income		**8,636**	**10,215**
Personnel expenses	21	(9,919)	(9,787)
General and administrative expenses	22	(7,336)	(10,317)
Depreciation and amortization	11 ,12	(3,820)	(4,068)
Depreciation charge on right of use assets	13	(2,328)	-
Other impairment and provisions		37	(46)
Non-interest expenses		**(23,366)**	**(24,218)**
Profit before tax		**7,605**	**8,075**
Income tax expense	14	(1,410)	(2,121)
PROFIT FOR THE YEAR		**6,195**	**5,954**
Other comprehensive income for the year		**6,195**	**5,954**
TOTAL COMPREHENSIVE INCOME FOR THE YEAR		**6,195**	**5,954**

(Amounts expressed in thousands of Azerbaijani Manats)

	Share Capital	Retained earnings	Total
Balance at 1 January 2018	**55,381**	**23,819**	**79,200**
Profit for the year	-	5,954	5,954
Total comprehensive income for the year	**-**	**5,954**	**5,954**
Balance at 31 December 2018	**55,381**	**29,773**	**85,154**
Profit for the year	-	6,195	6,195
Total comprehensive income for the year	**-**	**6,195**	**6,195**
Balance at 31 December 2019	**55,381**	**35,968**	**91,349**

The accompanying notes on pages 5 to 58 are an integral part of these financial statements.

Yapi Kredi Bank Azerbaijan CJSC
Statement of Cash Flows
(Amounts expressed in thousands of Azerbaijani Manats)

	Notes	2019	2018
Cash flows from operating activities			
Interest received		29,547	27,887
Interest paid		(3,716)	(5,822)
Fees and commissions received		10,585	10,931
Fees and commissions paid		(5,572)	(5,653)
Realized gains less losses from dealing in foreign currencies		3,645	4,984
Other income received		48	52
Personnel expenses paid		(9,340)	(10,339)
Other operating expenses paid		(7,558)	(10,296)
Cash flows from operating activities before changes in operating assets and liabilities		**17,639**	**11,744**
Net (increase)/decrease in operating assets			
Amounts due from credit institutions		40,001	(58,318)
Loans to customers		(17,357)	(30,840)
Other assets		(1,019)	200
Net increase/(decrease) in operating liabilities			
Amounts due to credit institutions		2,781	2,953
Amounts due to customers		(4,141)	(7,158)
Other liabilities		393	644
Net cash (used)/from in operating activities before income tax		**38,297**	**(80,775)**
Income tax paid		(2,012)	(3,916)
Net cash (used)/from in operating activities		**36,285**	**(84,691)**
Cash flows from investing activities			
(Purchase)/Disposal of bonds		7,460	(10,210)
Purchase of property and equipment	11	(1,036)	(1,066)
Purchase of intangible assets	12	(2,205)	(2,366)
Net cash used in investing activities		**4,219**	**(13,642)**
Cash flows from financing activities			
Repayment of principal of lease liabilities		(2,320)	–
Net cash from in financing activities		**(2,320)**	**-**
Effect of exchange rates changes on cash and cash equivalents		(14)	(62)
Net (decrease)/increase in cash and cash equivalents		**38,170**	**(98,395)**
Cash and cash equivalents, beginning		**197,918**	**296,313**
Cash and cash equivalents, ending	7 ,10	**236,088**	**197,918**

As per Company policy cash and cash equivalents includes notes issued by Central Bank of Azerbaijan Republic amounted AZN 33,692 (2018: AZN 34,486)

(Amounts expressed in thousands of Azerbaijani Manats)

1 Introduction

These financial statements have been prepared in accordance with International Financial Reporting Standards for the year ended 31 December 2019 for Yapi Kredi Bank (the "Bank").

Yapi Kredi Bank Azerbaijan (the "Yapi Kredi Bank") was incorporated and is domiciled in the Republic of Azerbaijan. Yapi Kredi Bank Azerbaijan is a closed joint-stock company limited by shares and was set up in accordance with Azerbaijani regulations.

Principal activity. The Yapi Kredi Bank's principal business activity is commercial and retail banking operations within the Republic of Azerbaijan. The Yapi Kredi Bank has operated under a full banking licence issued by the Central Bank of the Republic of Azerbaijan (the "CBAR") since 11 January 2000 under registration number 243. The Yapi Kredi Bank participates in the state deposit insurance scheme, which was introduced by the Azeri Law, "Insurance of individual deposits in the Republic of Azerbaijan" dated 29 December 2006. The State Deposit Insurance Fund guarantees full repayment of deposits of individuals, annual interest rate not exceeding 10% for AZN, 2.5% for foreign currencies.

Registered address and place of business. The Bank's registered address and principal place of business is 73G Jalil Mammadguluzadeh street Baku, AZ1078, Azerbaijan.

The Bank has 8 branches (2018: 7 branches), 1 customer services unit (2018: 1 unit) within the Republic of Azerbaijan. The Bank had 245 employees at 31 December 2019 (2018: 257).

As at 31 December 2019 and 2018 the following shareholders owned the outstanding shares of the Bank:

Shareholder	%
Yapı ve Kredi Bankası A.Ş.	99.8
YK Yatirim Menkul Degerler A.Ş.	0.1
YK Lease A.Ş.	0.1
Total	100.0

Yapı ve Kredi Bankası A.Ş. ("YKB"), an entity established in Turkey, is the ultimate parent of the Bank. YKB's shares have been traded on the Istanbul Stock Exchange ("ISE") since 1987. As at 31 December 2019, 18.20% of the shares of YKB are publicly traded (31 December 2018: 18.20%). The remaining 81.80% is owned by Koç Finansal Hizmetler A.Ş. ("KFS"). The ultimate shareholders of KFS are UniCredito Italiano SPA and Koç Holding, with 50% ownership each.

2 Operating Environment of the Bank

The Republic of Azerbaijan displays certain characteristics of an emerging market. Current and future growth and stability of the economy is largely dependent upon the effective implementation of economic, fiscal and monetary measures undertaken by government as well as crude oil prices and stability of Azerbaijani manats.

Following the sharp economic contraction in 2016 due to negative impact of the decline in oil prices and devaluations of national currency against major international currencies, the government accelerated reforms in support of long-term economic stability and sustainability. Based on the economic reforms involving institutional changes, inflation was stable at a low single-digit rate, the economic growth remained positively zoned, the exchange rate of the national currency was sustainable and positive trends emerged in the foreign sector.

Despite a number of ongoing fragilities in the systemic risks, the banking sector stability was safeguarded in parallel with lending recovery. The implementation of the Presidential Decree on "Additional measures on resolving problem loans of individuals" has led to compensation of individuals and restructuring of defaulted loans of individuals helped to improve bad loan problem in the banking sector.

The international rating agencies have maintained credit ratings of Azerbaijan during 2019 with stable outlook. In July, Moody's has upgraded the outlook of Azerbaijan's banking system from stable to positive and the agency affirms that Azerbaijan's growing economy and the high level of state support contributed the most to the positive forecast on the country's banking system. According to World Bank's Doing Business report 2020, Azerbaijan improved its position in the Ease of doing business rank to 34.

2 Operating Environment of the Bank (Continued)

The Bank's Management is monitoring these developments in the current environment and taking precautionary measures as it considers necessary in order to ensure the sustainability and development of the Bank's business in the foreseeable future. However, the future effects of the current economic situation are difficult to predict and management's current expectations and estimates could differ from actual results.

3 Significant Accounting Policies

Basis of preparation. These financial statements have been prepared in accordance with International Financial Reporting Standards ("IFRS") under the historical cost convention, as modified by the initial recognition of financial instruments based on fair value and by the revaluation of premises and equipment, financial instruments categorised at fair value through profit or loss ("FVTPL") and at fair value through other comprehensive income ("FVOCI"). The principal accounting policies applied in the preparation of these financial statements are set out below. Apart from the accounting policy changes resulting from the adoption of IFRS 16 effective from 1 January 2019, these policies have been consistently applied to all the periods presented, unless otherwise stated. Refer to Note 5.

Financial instruments – key measurement terms. *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 best evidence of fair value is price in an active market. An active market is one in which transactions for the asset or liability take place with sufficient frequency and volume to provide pricing information on an ongoing basis. Fair value of financial instruments traded in an active market is measured as the product of the quoted price for the individual asset or liability and the quantity held by the entity. This is the case even if a market's normal daily trading volume is not sufficient to absorb the quantity held and placing orders to sell the position in a single transaction might affect the quoted price.

Valuation techniques such as discounted cash flow models or models based on recent arm's length transactions or consideration of financial data of the investees, are used to measure fair value of certain financial instruments for which external market pricing information is not available. Fair value measurements are analysed by level in the fair value hierarchy as follows: (i) level one are measurements at quoted prices (unadjusted) in active markets for identical assets or liabilities, (ii) level two measurements are valuations techniques with all material inputs observable for the asset or liability, either directly (that is, as prices) or indirectly (that is, derived from prices), and (iii) level three measurements are valuations not based on solely observable market data (that is, the measurement requires significant unobservable inputs). Transfers between levels of the fair value hierarchy are deemed to have occurred at the end of the reporting period.

Transaction costs are incremental costs that are directly attributable to the acquisition, issue or disposal of a financial instrument. An incremental cost is one that would not have been incurred if the transaction had not taken place. Transaction costs include fees and commissions paid to agents (including employees acting as selling agents), advisors, brokers and dealers, levies by regulatory agencies and securities exchanges, and transfer taxes and duties. Transaction costs do not include debt premiums or discounts, financing costs or internal administrative or holding costs.

Amortised cost ("AC") is the amount at which the financial instrument was recognised at initial recognition less any principal repayments, plus accrued interest, and for financial assets less any allowance for expected credit losses. Accrued interest includes amortisation of transaction costs deferred at initial recognition and of any premium or discount to maturity amount using the effective interest method. Accrued interest income and accrued interest expense, including both accrued coupon and amortised discount or premium (including fees deferred at origination, if any), are not presented separately and are included in the carrying values of related items in the statement of financial position.

The effective interest method is a method of allocating interest income or interest expense over the relevant period, so as to achieve a constant periodic rate of interest (effective interest rate) on the carrying amount. The effective interest rate is the rate that exactly discounts estimated future cash payments or receipts (excluding future credit losses) through the expected life of the financial instrument or a shorter period, if appropriate, to the gross carrying amount of the financial instrument.

3 Significant Accounting Policies (Continued)

The effective interest rate discounts cash flows of variable interest instruments to the next interest repricing date, except for the premium or discount, which reflects the credit spread over the floating rate specified in the instrument, or other variables that are not reset to market rates. Such premiums or discounts are amortised over the whole expected life of the instrument. The present value calculation includes all fees paid or received between parties to the contract that are an integral part of the effective interest rate.

Financial instruments – initial recognition. Financial instruments at FVTPL are initially recorded at fair value. All other financial instruments are initially recorded at fair value adjusted for transaction costs. Fair value at initial recognition is best evidenced by the transaction price. A gain or loss on initial recognition is only recorded if there is a difference between fair value and transaction price which can be evidenced by other observable current market transactions in the same instrument or by a valuation technique whose inputs include only data from observable markets. After the initial recognition, an ECL allowance is recognised for financial assets measured at AC and investments in debt instruments measured at FVOCI, resulting in an immediate accounting loss.

All purchases and sales of financial assets that require delivery within the time frame established by regulation or market convention ("regular way" purchases and sales) are recorded at trade date, which is the date on which the Bank commits to deliver a financial asset. All other purchases are recognised when the entity becomes a party to the contractual provisions of the instrument.

Financial assets – classification and subsequent measurement – measurement categories. The Bank classifies financial assets in the following measurement categories: FVTPL, FVOCI and AC. The classification and subsequent measurement of debt financial assets depends on: (i) the Bank's business model for managing the related assets portfolio and (ii) the cash flow characteristics of the asset.

Financial assets – classification and subsequent measurement – business model. The business model reflects how the Bank manages the assets in order to generate cash flows – whether the Bank's objective is: (i) solely to collect the contractual cash flows from the assets ("hold to collect contractual cash flows",) or (ii) to collect both the contractual cash flows and the cash flows arising from the sale of assets ("hold to collect contractual cash flows and sell") or, if neither of (i) and (ii) is applicable, the financial assets are classified as part of "other" business model and measured at FVTPL.

Business model is determined for a group of assets (on a portfolio level) based on all relevant evidence about the activities that the Bank undertakes to achieve the objective set out for the portfolio available at the date of the assessment. Factors considered by the Bank in determining the business model include the purpose and composition of a portfolio, past experience on how the cash flows for the respective assets were collected, how risks are assessed and managed, how the assets' performance is assessed. Refer to Note 4 for critical judgements applied by the Bank in determining the business models for its financial assets.

Financial assets – classification and subsequent measurement – cash flow characteristics. Where the business model is to hold assets to collect contractual cash flows or to hold contractual cash flows and sell, the Bank assesses whether the cash flows represent solely payments of principal and interest ("SPPI"). Financial assets with embedded derivatives are considered in their entirety when determining whether their cash flows are consistent with the SPPI feature. In making this assessment, the Bank considers whether the contractual cash flows are consistent with a basic lending arrangement, i.e. interest includes only consideration for credit risk, time value of money, other basic lending risks and profit margin.

Where the contractual terms introduce exposure to risk or volatility that is inconsistent with a basic lending arrangement, the financial asset is classified and measured at FVTPL. The SPPI assessment is performed on initial recognition of an asset and it is not subsequently reassessed. Refer to Note 4 for critical judgements applied by the Bank in performing the SPPI test for its financial assets.

3 Significant Accounting Policies (Continued)

Financial assets – reclassification. Financial instruments are reclassified only when the business model for managing the portfolio as a whole changes. The reclassification has a prospective effect and takes place from the beginning of the first reporting period that follows after the change in the business model. The Bank did not change its business model during the current and comparative period and did not make any reclassifications. The entity did not change its business model during the current and comparative period and did not make any reclassifications.

Financial assets impairment – credit loss allowance for ECL. 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.

Debt instruments measured at AC are presented in the statement of financial position net of the allowance for ECL. For loan commitments and financial guarantees, a separate provision for ECL is recognised as a liability in the statement of financial position. For debt instruments at FVOCI, changes in amortised cost, net of allowance for ECL, are recognised in profit or loss and other changes in carrying value are recognised in OCI as gains less losses on debt instruments at FVOCI.

The Bank applies a three stage model for impairment, based on changes in credit quality since initial recognition. 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"). 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, that is, up until contractual maturity but considering expected prepayments, if any ("Lifetime ECL"). Refer to Note 23 for a description of how the Bank determines when a SICR has occurred. If the Bank determines that a financial asset is credit-impaired, the asset is transferred to Stage 3 and its ECL is measured as a Lifetime ECL. The Bank's definition of credit impaired assets and definition of default is explained in Note 23 .

As an exception, for certain financial instruments, such as credit cards, that may include both a loan and an undrawn commitment component, the Bank measures expected credit losses over the period that the Bank is exposed to credit risk, that is, until the expected credit losses would be mitigated by credit risk management actions, even if that period extends beyond the maximum contractual period. This is because contractual ability to demand repayment and cancel the undrawn commitment does not limit the exposure to credit losses to such contractual notice period.

Financial assets – write-off. Financial assets are written-off, in whole or in part, when the Bank exhausted all practical recovery efforts and has concluded that there is no reasonable expectation of recovery. The write-off represents a dercognition event. The Bank may write-off financial assets that are still subject to enforcement activity when the Bank seeks to recover amounts that are contractually due, however, there is no reasonable expectation of recovery.

Financial assets – derecognition. The Bank derecognises financial assets when (a) the assets are redeemed or the rights to cash flows from the assets otherwise expired or (b) the Bank has transferred the rights to the cash flows from the financial assets or entered into a qualifying pass-through arrangement while (i) also transferring substantially all risks and rewards of ownership of the assets or (ii) neither transferring nor retaining substantially all risks and rewards of ownership, but not retaining control. Control is retained if the counterparty does not have the practical ability to sell the asset in its entirety to an unrelated third party without needing to impose restrictions on the sale.

Financial assets – modification. The Bank sometimes renegotiates or otherwise modifies the contractual terms of the financial assets. The Bank assesses whether the modification of contractual cash flows is substantial considering, among other, the following factors: any new contractual terms that substantially affect the risk profile of the asset (eg profit share or equity-based return), significant change in interest rate,

3 Significant Accounting Policies (Continued)

change in the currency denomination, new collateral or credit enhancement that significantly affects the credit risk associated with the asset or a significant extension of a loan when the borrower is not in financial difficulties.

If the modified terms are substantially different, the rights to cash flows from the original asset expire and the Bank derecognises the original financial asset and recognises a new asset at its fair value. The date of renegotiation is considered to be the date of initial recognition for subsequent impairment calculation purposes, including determining whether a SICR has occurred. The Bank also assesses whether the new loan or debt instrument meets the SPPI criterion. Any difference between the carrying amount of the original asset derecognised and fair value of the new substantially modified asset is recognised in profit or loss, unless the substance of the difference is attributed to a capital transaction with owners.

In a situation where the renegotiation was driven by financial difficulties of the counterparty and inability to make the originally agreed payments, the Bank compares the original and revised expected cash flows to assets whether the risks and rewards of the asset are substantially different as a result of the contractual modification. If the risks and rewards do not change, the modified asset is not substantially different from the original asset and the modification does not result in derecognition. The Bank recalculates the gross carrying amount by discounting the modified contractual cash flows by the original effective interest rate, and recognises a modification gain or loss in profit or loss.

Financial liabilities – measurement categories. Financial liabilities are classified as subsequently measured at AC, except for (i) financial liabilities at FVTPL: this classification is applied to derivatives, financial liabilities held for trading (e.g. short positions in securities), contingent consideration recognised by an acquirer in a business combination and other financial liabilities designated as such at initial recognition and (ii) financial guarantee contracts and loan commitments.

Financial liabilities – derecognition. Financial liabilities are derecognised when they are extinguished (i.e. when the obligation specified in the contract is discharged, cancelled or expires).

Modifications of liabilities that do not result in extinguishment are accounted for as a change in estimate using a cumulative catch up method, with any gain or loss recognised in profit or loss, unless the economic substance of the difference in carrying values is attributed to a capital transaction with owners.

Cash and cash equivalents. Cash and cash equivalents are short-term items which are readily convertible to known amounts of cash and which are subject to an insignificant risk of changes in value. Cash and cash equivalents include cash on hand, amounts due from the CBAR, excluding obligatory reserves, and unrestricted balances on correspondent accounts including overnight deposits and deposits with original maturities of less than three months. Funds restricted for a period of more than three months on origination are excluded from cash and cash equivalents, both in the statement of financial position and for the purposes of the statement of cash flows. Cash and cash equivalents are carried at AC because: (i) they are held for collection of contractual cash flows and those cash flows represent SPPI, and (ii) they are not designated at FVTPL. Notes from CBAR represents cash and cash equivalents.

Mandatory cash balances with the CBAR. Mandatory cash balances with the CBAR are carried at AC and represent non-interest bearing mandatory reserve deposits, which are not available to finance the Bank's day to day operations, and hence are not considered as part of cash and cash equivalents for the purposes of the statement of cash flows.

Due from other banks. Amounts due from other banks are recorded when the Bank advances money to counterparty banks. Amounts due from other banks are carried at AC when: (i) they are held for the purposes of collecting contractual cash flows and those cash flows represent SPPI, and (ii) they are not designated at FVTPL.

Investments in debt securities. Based on the business model and the cash flow characteristics, the Bank classifies investments in debt securities as carried at AC, FVOCI or FVTPL. Debt securities are carried at AC if they are held for collection of contractual cash flows and where those cash flows represent SPPI, and if they are not voluntarily designated at FVTPL in order to significantly reduce an accounting mismatch.

3 Significant Accounting Policies (Continued)

Debt 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. An impairment allowance estimated using the expected credit loss model is recognised in profit or loss for the year. All other changes in the carrying value are recognised in OCI. When the debt security is derecognised, the cumulative gain or loss previously recognised in OCI is reclassified from OCI to profit or loss.

Investments in debt securities are carried at FVTPL if they do not meet the criteria for AC or FVOCI. The Bank may also irrevocably designate investments in debt securities at FVTPL on initial recognition if applying this option significantly reduces an accounting mismatch between financial assets and liabilities being recognised or measured on different accounting bases.

Loans and advances to customers. Loans and advances to customers are recorded when the Bank advances money to purchase or originate a loan due from a customer. Based on the business model and the cash flow characteristics, the Bank classifies loans and advances to customers into one of the following measurement categories: (i) AC: loans that are held for collection of contractual cash flows and those cash flows represent SPPI and loans that are not voluntarily designated at FVTPL, and (ii) FVTPL: loans that do not meet the SPPI test or other criteria for AC or FVOCI are measured at FVTPL.

Impairment allowances are determined based on the forward-looking ECL models. Note 23 provides information about inputs, assumptions and estimation techniques used in measuring ECL, including an explanation of how the Bank incorporates forward-looking information in the ECL models.

Notes Issued by Central Bank of the Republic of Azerbaijan (CBAR) and Other Bonds. Notes from CBAR have original maturity less than one month and represents cash and cash equivalents. Other investments in debt securities are measured at amortised cost.

Repossessed collateral. Repossessed collateral represents financial and non-financial assets acquired by the Bank in settlement of overdue loans. The assets are initially recognised at fair value when acquired and included in premises and equipment, other financial assets, investment properties or inventories within other assets depending on their nature and the Bank's intention in respect of recovery of these assets. The Bank measures a repossessed collateral at the lower of its carrying amount and fair value less costs to sell. The Bank recognizes an impairment loss for any initial or subsequent write-down of the asset to fair value less costs to sell if events or changes in circumstance indicate that their carrying amount may be impaired.

Loan commitments. The Bank issues commitments to provide loans. These commitments are irrevocable or revocable only in response to a material adverse change. Such commitments are initially recognised at their fair value, which is normally evidenced by the amount of fees received. This amount is amortised on a straight line basis over the life of the commitment, except for commitments to originate loans if it is probable that the Bank will enter into a specific lending arrangement and does not expect to sell the resulting loan shortly after origination; such loan commitment fees are deferred and included in the carrying value of the loan on initial recognition. At the end of each reporting period, the commitments are measured at (i) the remaining unamortised balance of the amount at initial recognition, plus (ii) the amount of the loss allowance determined based on the expected credit loss model, unless the commitment is to provide a loan at a below market interest rate, in which case the measurement is at the higher of these two amounts. The carrying amount of the loan commitments represents a liability. For contracts that include both a loan and an undrawn commitment and where the Bank cannot separately distinguish the ECL on the undrawn loan component from the loan component, the ECL on the undrawn commitment is recognised together with the loss allowance for the loan. To the extent that the combined ECLs exceed the gross carrying amount of the loan, they are recognised as a liability.

Financial guarantees. Financial guarantees require the Bank to make specified payments to reimburse the holder of the guarantee for a loss it incurs because a specified debtor fails to make payment when due in accordance with the original or modified terms of a debt instrument. Financial guarantees are initially recognised in "Other liabilities" at their fair value, which is normally evidenced by the amount of fees received. This amount is amortised on a straight line basis over the life of the guarantee. At the end of each reporting period, the guarantees are measured at the higher of (i) the amount of the loss allowance for the guaranteed exposure determined based on the expected loss model and (ii) the remaining unamortised balance of the amount at initial recognition. In addition, an ECL loss allowance is recognised for fees receivable that are recognised in the statement of financial position as an asset.

3 Significant Accounting Policies (Continued)

Taxation. The current income tax expense is calculated in accordance with the regulations of the Republic of Azerbaijan.

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

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

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

In addition, there are various operating taxes in Azerbaijan such as VAT, property tax, withholding tax and others which become relevant as a result of the Bank's operations. These taxes are included as a component of general and administrative expenses.

Property and equipment. Property and equipment are carried at cost, excluding the costs of day-to-day servicing, less accumulated depreciation and any accumulated impairment. Such cost includes the cost of replacing part of equipment when that cost is incurred if the recognition criteria are met.

The carrying values of property and equipment are reviewed for impairment when events or changes in circumstances indicate that the carrying value may not be recoverable.

Depreciation. Depreciation of an asset begins when it is available for use. Depreciation is calculated on a straight-line basis over the following estimated useful lives:

	Years
Leasehold improvements	4-15
Furniture and fixtures	4-5
Computers and office equipment	4
Motor vehicles	4

The asset's residual values, useful lives and methods are reviewed, and adjusted as appropriate, at each financial year-end.

Costs related to repairs and renewals are charged when incurred and included in other operating expenses, unless they qualify for capitalization.

Intangible assets. Intangible assets other than goodwill include computer software and licenses.

Intangible assets acquired separately are measured on initial recognition at cost. Following initial recognition, intangible assets are carried at cost less any accumulated amortization and any accumulated impairment losses. The useful lives of intangible assets are assessed to be either finite or indefinite. Intangible assets with finite lives are amortized over the useful economic lives of 1 to 10 years and assessed for impairment whenever there is an indication that the intangible asset may be impaired.

Amortization periods and methods for intangible assets with indefinite useful lives are reviewed at least at each financial year-end.

Accounting for leases by the Bank as a lessee from 1 January 2019. The Bank leases office premises, apartments, cars and ATMs. Leases are recognised as a right-of-use asset and a corresponding liability at the date at which the leased asset is available for use by the Bank. Each lease payment is allocated between the liability and finance cost. The finance cost is charged to profit or loss over the lease period so as to produce a constant periodic rate of interest on the remaining balance of the liability for each period. The right-of-use asset is recognised at cost and depreciated over the shorter of the asset's useful life and the lease term on a straight-line basis.

3 Significant Accounting Policies (Continued)

Liabilities arising from a lease are initially measured on a present value basis. Lease liabilities include the net present value of the following lease payments:

- fixed payments (including in-substance fixed payments), less any lease incentives receivable;
- variable lease payment that are based on an index or a rate;
- amounts expected to be payable by the lessee under residual value guarantees;
- the exercise price of a purchase option if the lessee is reasonably certain to exercise that option,
- payments of penalties for terminating the lease, if the lease term reflects the lessee exercising that option.

The lease payments are discounted using the interest rate implicit in the lease. If that rate cannot be determined, the lessee's incremental borrowing rate is used, being the rate that the lessee would have to pay to borrow the funds necessary to obtain an asset of similar value in a similar economic environment with similar terms and conditions.

Right-of-use assets are measured at cost comprising the following:

- the amount of the initial measurement of lease liability;
- any lease payments made at or before the commencement date less any lease incentives received;
- any initial direct costs, and
- restoration costs.

In determining the lease term, management of the Bank considers all facts and circumstances that create an economic incentive to exercise an extension option, or not exercise a termination option. Extension options (or periods after termination options) are only included in the lease term if the lease is reasonably certain to be extended or not terminated.

The assessment is reviewed if a significant event or a significant change in circumstances occurs which affects this assessment and that is within the control of the lessee.

Accounting for operating leases by the Bank as a lessee prior to 1 January 2019. Where the Bank is a lessee in a lease which does not transfer substantially all the risks and rewards incidental to ownership from the lessor to the Bank, the total lease payments are charged to profit or loss for the year (rental expense) on a straight-line basis over the period of the lease.

Due to other credit institutions. Amounts due to other banks are recorded when money or other assets are advanced to the Bank by counterparty banks. The non-derivative liability is carried at AC.

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

Provision. Provisions are recognized when the Bank has a present legal or constructive obligation as a result of past events, and it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation and a reliable estimate of the amount of obligation can be made.

Share Capital. Ordinary shares are classified as equity. External costs directly attributable to the issue of new shares, other than on a business combination, are shown as a deduction from the proceeds in equity.

Any excess of the fair value of consideration received over the par value of shares issued is recognized as additional paid-in capital.

Presentation of statement of financial position in order of liquidity. The Bank does not have a clearly identifiable operating cycle and therefore does not present current and non-current assets and liabilities separately in the statement of financial position. Instead, assets and liabilities are presented in order of their liquidity. Refer to Note 23 for analysis of financial instruments by expected maturity.

3 Significant Accounting Policies (Continued)

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

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

For financial assets that are originated or purchased credit-impaired, the effective interest rate is the rate that discounts the expected cash flows (including the initial expected credit losses) to the fair value on initial recognition (normally represented by the purchase price). As a result, the effective interest is credit-adjusted.

Interest income is calculated by applying the effective interest rate to the gross carrying amount of financial assets, except for (i) financial assets that have become credit impaired (Stage 3), for which interest revenue is calculated by applying the effective interest rate to their AC, net of the ECL provision, and (ii) financial assets that are purchased or originated credit impaired, for which the original credit-adjusted effective interest rate is applied to the AC.

Fees and commissions. The Bank earns fee and commission income from a diverse range of services it provides to its customers. Fee income can be divided into the following two categories:

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

Fee and commission income is recognised over time on a straight line basis as the services are rendered, when the customer simultaneously receives and consumes the benefits provided by the Bank's performance. Loan commitment fees for loans that are likely to be drawn down and other credit related fees are deferred (together with any incremental costs) and recognized as an adjustment to the effective interest rate on the loan.

- *Fee income from providing transaction services*

Fee and commission income is recognised at a point in time when the Bank satisfies its performance obligation, usually upon execution of the underlying transaction. The amount of fee or commission received or receivable represents the transaction price for the services identified as distinct performance obligations. Fees arising from negotiating or participating in the negotiation of a transaction for a third party are recognized on completion of the underlying transaction. Fees or components of fees that are linked to a certain performance are recognised after fulfilling the corresponding criteria.

Sales and purchases of foreign currencies and currency conversion. The Bank sells and purchases foreign currencies in the cash offices and through the bank accounts, as well as exchanges foreign currencies. The transactions are performed at the exchange rates established by the Bank, which are different from the official spot exchange rates at the particular dates. The differences between the official rates and Bank rates are recognised as gains less losses from trading in foreign currencies at a point in time when a particular performance obligation is satisfied.

Foreign currency translation. The financial statements are presented in Azerbaijani Manat, which is the Bank's functional 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 are retranslated at the functional currency rate of exchange ruling at the reporting date. Gains and losses resulting from the translation of foreign currency transactions are recognised in the statement of profit or loss and other comprehensive income as net gains (losses) from foreign currency translation differences. Non-monetary items that are measured in terms of historical cost in a foreign currency are translated using the exchange rates as at the dates of the initial transactions. Non-monetary items measured at fair value in a foreign currency are translated using the exchange rates at the date when the fair value was determined.

(Amounts expressed in thousands of Azerbaijani Manats)

3 Significant Accounting Policies (Continued)

Differences between the contractual exchange rate of a transaction in a foreign currency and the CBAR exchange rate on the date of the transaction are included in gains/ losses from dealing operations.

The Bank used the following official exchange rates at 31 December 2019 and 2018 in the preparation of these financial statements:

	2019	2018
1 US dollar	AZN 1.7000	AZN 1.7000
1 EUR	AZN 1.9035	AZN 1.9468

4 Critical Accounting Estimates, and Judgements in Applying Accounting Policies

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

ECL measurement. Measurement of ECLs is a significant estimate that involves determination of methodology, models and data inputs. Details of ECL measurement methodology are disclosed in Note 24 The following components have a major impact on credit loss allowance: definition of default, SICR, probability of default ("PD"), exposure at default ("EAD"), and loss given default ("LGD"), as well as models of macro-economic scenarios. The Bank regularly reviews and validates the models and inputs to the models to reduce any differences between expected credit loss estimates and actual credit loss experience.

A 10% increase or decrease in PD estimates at 31 December 2019 would result in an increase or decrease in total expected credit loss allowances of AZN 109 thousand. A 10% increase or decrease in LGD estimates at 31 December 2019 would result in an increase or decrease in total expected credit loss allowances of AZN 1,285 thousand.

Determination of collateral value. Management monitors market value of collateral on a regular basis. Management uses its experienced judgment or independent opinion to adjust the fair value to reflect the current circumstances. The amount and collateral required depend on the assessment of credit risk of the counterparty.

Initial recognition of related party transactions. In the normal course of business, the Bank enters into transactions with its related parties. IFRS 9 requires initial recognition of financial instruments based on their fair values. Judgement is applied in determining if transactions are priced at market or non-market interest rates, where there is no active market for such transactions. The basis for judgement is pricing for similar types of transactions with unrelated parties and effective interest rate analysis. Terms and conditions of related party balances are disclosed in Note 25 .

Credit exposure on revolving credit facilities (e.g. credit cards, overdrafts). For certain loan facilities, the Bank's exposure to credit losses may extend beyond the maximum contractual period of the facility. This exception applies to certain revolving credit facilities, which include both a loan and an undrawn commitment component and where the Bank's contractual ability to demand repayment and cancel the undrawn component in practice does not limit its exposure to credit losses.

For such facilities, the Bank measures ECLs over the period that the Bank is exposed to credit risk and ECLs are not mitigated by credit risk management actions. Application of this exception requires judgement. Management applied its judgement in identifying the facilities, both retail and commercial, to which this exception applies. The Bank applied this exception to facilities with the following characteristics:

4 Critical Accounting Estimates, and Judgements in Applying Accounting Policies (Continued)

(a) there is no fixed term or repayment structure, (b) the contractual ability to cancel the contract is not in practice enforced as a result of day-to-day management of the credit exposure and the contract may only be cancelled when the Bank becomes aware of an increase in credit risk at the level of an individual facility, and (c) the exposures are managed on a collective basis. Further, the Bank applied judgement in determining a period for measuring the ECL, including the starting point and the expected end point of the exposures.

The Bank considered historical information and experience about: (a) the period over which the Bank is exposed to credit risk on similar facilities, including when the last significant modification of the facility occurred and that therefore determines the starting point for assessing SICR, (b) the length of time for related defaults to occur on similar financial instruments following a SICR and (c) the credit risk management actions (eg the reduction or removal of undrawn limits), prepayment rates and other factors that drive expected maturity. In applying these factors, the Bank segments the portfolios of revolving facilities into sub-groups and applies the factors that are most relevant based on historical data and experience as well as forward-looking information.

Significant increase in credit risk ("SICR"). In order to determine whether there has been a significant increase in credit risk, the Bank compares the risk of a default occurring over the life of a financial instrument at the end of the reporting date with the risk of default at the date of initial recognition. The assessment considers relative increase in credit risk rather than achieving a specific level of credit risk at the end of the reporting period. The Bank considers all reasonable and supportable forward looking information available without undue cost and effort, which includes a range of factors, including behavioural aspects of particular customer portfolios. The Bank identifies behavioural indicators of increases in credit risk prior to delinquency and incorporated appropriate forward looking information into the credit risk assessment, either at an individual instrument, or on a portfolio level. Refer to Note 24 .

Business model assessment. The business model drives classification of financial assets. Management applied judgement in determining the level of aggregation and portfolios of financial instruments when performing the business model assessment. When assessing sales transactions, the Bank considers their historical frequency, timing and value, reasons for the sales and expectations about future sales activity. Sales transactions aimed at minimising potential losses due to credit deterioration are considered consistent with the "hold to collect" business model. Other sales before maturity, not related to credit risk management activities, are also consistent with the "hold to collect" business model, provided that they are infrequent or insignificant in value, both individually and in aggregate. The Bank assesses significance of sales transactions by comparing the value of the sales to the value of the portfolio subject to the business model assessment over the average life of the portfolio. In addition, sales of financial asset expected only in stress case scenario, or in response to an isolated event that is beyond the Bank's control, is not recurring and could not have been anticipated by the Bank, are regarded as incidental to the business model objective and do not impact the classification of the respective financial assets.

The "hold to collect and sell" business model means that assets are held to collect the cash flows, but selling is also integral to achieving the business model's objective, such as, managing liquidity needs, achieving a particular yield, or matching the duration of the financial assets to the duration of the liabilities that fund those assets.

The residual category includes those portfolios of financial assets, which are managed with the objective of realising cash flows primarily through sale, such as where a pattern of trading exists. Collecting contractual cash flow is often incidental for this business model.

Assessment whether cash flows are solely payments of principal and interest ("SPPI"). Determining whether a financial asset's cash flows are solely payments of principal and interest required judgement.

The time value of money element may be modified, for example, if a contractual interest rate is periodically reset but the frequency of that reset does not match the tenor of the debt instrument's underlying base interest rate, for example a loan pays three months interbank rate but the rate is reset every month. The effect of the modified time value of money was assessed by comparing relevant instrument's cash flows against a benchmark debt instrument with SPPI cash flows, in each period and cumulatively over the life of the instrument. The assessment was done for all reasonably possible scenarios, including reasonably possible financial stress situation that can occur in financial markets. In case of a scenario with cash flows that significantly differ from the benchmark, the assessed instrument's cash flows are not SPPI and the instrument is then carried at FVTPL.

4 Critical Accounting Estimates, and Judgements in Applying Accounting Policies (Continued)

The Bank identified and considered contractual terms that change the timing or amount of contractual cash flows. The SPPI criterion is met if a loan allows early settlement and the prepayment amount substantially represents principal and accrued interest, plus a reasonable additional compensation for the early termination of the contract. The asset's principal is the fair value at initial recognition less subsequent principal repayments, ie instalments net of interest determined using the effective interest method. As an exception to this principle, the standard also allows instruments with prepayment features that meet the following condition to meet SPPI: (i) the asset is originated at a premium or discount, (ii) the prepayment amount represents contractual par amount and accrued interest and a reasonable additional compensation for the early termination of the contract, and (ii) the fair value of the prepayment feature is immaterial at initial recognition.

Modification of financial assets. When financial assets are contractually modified (e.g. renegotiated), the Bank assesses whether the modification is substantial and should result in derecognition of the original asset and recognition of a new asset at fair value. This assessment is based primarily on qualitative factors, described in the relevant accounting policy and it requires significant judgment. In particular, the Bank applies judgment in deciding whether credit impaired renegotiated loans should be derecognised and whether the new recognised loans should be considered as credit impaired on initial recognition. The derecognition assessment depends on whether the risks and rewards, that is, the variability of expected (rather than contractual) cash flows, change as a result of such modifications. Management determined that risks and rewards did not change as a result of modifying such loans and therefore in substantially all such modifications, the loans were neither derecognised nor reclassified out of the credit-impaired stage.

Write-off policy. Financial assets are written-off, in whole or in part, when the Bank exhausted all practical recovery efforts and has concluded that there is no reasonable expectation of recovery. Determining the cash flows for which there is no reasonable expectation of recovery requires judgement. Management considered the following indicators that there is no reasonable expectation of recovery: liquidation or bankruptcy proceedings as well as decision of the court. Management also considers, based on past practices, that contractual default interest is not collectible for loans overdue over 360 days. Therefore, the default interest was written-off from the gross carrying amounts of the respective loans.

5 Adoption of New or Revised Standards and Interpretations

Adoption of IFRS 16, Leases. The Bank has adopted IFRS 16 retrospectively from 1 January 2019 with certain simplifications and exemptions, and has not restated comparatives for the 2018 reporting period, as permitted under the transitional provisions of IFRS 16. The reclassifications and the adjustments arising from the new leasing requirements are therefore recognised as an adjustment to the opening balance of retained earnings as of 1 January 2019.

On adoption of IFRS 16, the Bank recognised lease liabilities in relation to leases which had previously been classified as operating leases under the principles of IAS 17, Leases. These liabilities were measured at the present value of the remaining lease payments, discounted using the lessee's incremental borrowing rate as of 1 January 2019. The weighted average lessee's incremental borrowing rate applied to the lease liabilities on 1 January 2019 was 7.59%

In applying IFRS 16 for the first time, the Bank has used the following practical expedients permitted by the standard:

- applying a single discount rate to a portfolio of leases with reasonably similar characteristics,
- relying on previous assessments on whether leases are onerous as an alternative to performing an impairment review – there were no onerous contracts as at 1 January 2019,
- excluding initial direct costs for the measurement of the right-of-use asset at the date of initial application

(Amounts expressed in thousands of Azerbaijani Manats)

5 Adoption of New or Revised Standards and Interpretations (Continued)

The Bank has also elected not to reassess whether a contract is, or contains a lease at the date of initial application. Instead, for contracts entered into before the transition date the Bank relied on its assessment made applying IAS 17, Leases, and IFRIC 4, Determining whether an Arrangement contains a Lease.

The following table presents reconciliation of the operating lease commitments reported as of 31 December 2018 and lease liability recognised at 1 January 2019:

	1 January 2019
Total future minimum lease payments for operating leases as at 31 December 2018	7,711
Effect of discounting to present value	-1,523
Lease liability recognised as at 1 January 2019	**6,188**
Advances paid to lessors	186
Right-of-use asset recognised as at 1 January 2019	**6,374**

The change in accounting policy affected the following items in the statement of financial position on 1 January 2019:

	Impact of adopting IFRS 16
Increase in right-of-use assets	6,374
Increase in lease liabilities	6,188
Decrease in Prepayments	186

The associated right-of use assets were measured at the amount equal to the lease liability, adjusted by the amount of any prepaid or accrued lease payments relating to that lease recognised in the balance sheet as at 31 December 2018. There were no onerous lease contracts that would have required an adjustment to the right-of-use assets at the date of initial application.

The recognised right-of-use assets relate to the following types of assets:

	31 December 2019	1 January 2019
Properties for own use	5,392	5,624
Motor vehicles	359	651
Other	-	99
Total right-of-use assets	**5,751**	**6,374**

The recognised lease liabilities classified as follows:

	31 December 2019	1 January 2019
Current portion	1,389	1,913
Non-current portion	4,309	4,275
Total lease liabilities	**5,698**	**6,188**

5 Adoption of New or Revised Standards and Interpretations (Continued)

Amendment to IAS 12, Income Taxes, included in the Annual Improvements to IFRSs 2015-2017 cycle. The Bank adopted the changes to IAS 12, *Income Taxes*, with effect from 1 January 2019. As a result of these amendments, the tax benefits of distributions on perpetual instruments that are classified as equity under IFRS but are considered as liabilities for tax purposes are no longer recognised directly in equity but in profit or loss because these tax benefits are linked more directly to past transactions or events that generated distributable profits than to the distributions to owners.

The following amended standards became effective from 1 January 2019, but did not have any material impact on the Bank:

- IFRIC 23 "Uncertainty over Income Tax Treatments" (issued on 7 June 2017 and effective for annual periods beginning on or after 1 January 2019).
- Prepayment Features with Negative Compensation – Amendments to IFRS 9 (issued on 12 October 2017 and effective for annual periods beginning on or after 1 January 2019).
- Amendments to IAS 28 "Long-term Interests in Associates and Joint Ventures" (issued on 12 October 2017 and effective for annual periods beginning on or after 1 January 2019).
- Annual Improvements to IFRSs 2015-2017 cycle – amendments to IFRS 3, IFRS 11, IAS 12 and IAS 23 (issued on 12 December 2017 and effective for annual periods beginning on or after 1 January 2019).

Amendments to IAS 19 "Plan Amendment, Curtailment or Settlement" (issued on 7 February 2018 and effective for annual periods beginning on or after 1 January 2019).

6 New Accounting Pronouncements

Certain new standards and interpretations have been issued that are mandatory for the annual periods beginning on or after 1 January 2020 or later, and which the Bank has not early adopted.

IFRS 17 "Insurance Contracts" (issued on 18 May 2017 and effective for annual periods beginning on or after 1 January 2021). IFRS 17 replaces IFRS 4, which has given companies dispensation to carry on accounting for insurance contracts using existing practices. As a consequence, it was difficult for investors to compare and contrast the financial performance of otherwise similar insurance companies. IFRS 17 is a single principle-based standard to account for all types of insurance contracts, including reinsurance contracts that an insurer holds. The standard requires recognition and measurement of groups of insurance contracts at: (i) a risk-adjusted present value of the future cash flows (the fulfilment cash flows) that incorporates all of the available information about the fulfilment cash flows in a way that is consistent with observable market information; plus (if this value is a liability) or minus (if this value is an asset) (ii) an amount representing the unearned profit in the group of contracts (the contractual service margin). Insurers will be recognising the profit from a group of insurance contracts over the period they provide insurance coverage, and as they are released from risk. If a group of contracts is or becomes loss-making, an entity will be recognising the loss immediately.

Amendments to the Conceptual Framework for Financial Reporting (issued on 29 March 2018 and effective for annual periods beginning on or after 1 January 2020). The revised Conceptual Framework includes a new chapter on measurement; guidance on reporting financial performance; improved definitions and guidance - in particular the definition of a liability; and clarifications in important areas, such as the roles of stewardship, prudence and measurement uncertainty in financial reporting.

Definition of a business – Amendments to IFRS 3 (issued on 22 October 2018 and effective for acquisitions from the beginning of annual reporting period that starts on or after 1 January 2020).The amendments revise definition of a business. A business must have inputs and a substantive process that together significantly contribute to the ability to create outputs. The new guidance provides a framework to evaluate when an input and a substantive process are present, including for early stage companies that have not generated outputs. An organised workforce should be present as a condition for classification as a business if are no outputs. The definition of the term 'outputs' is narrowed to focus on goods and services provided to customers, generating investment income and other income, and it excludes returns in the form of lower costs and other economic benefits. It is also no longer necessary to assess whether market participants are capable of replacing missing elements or integrating the acquired activities and assets. An entity can apply a 'concentration test'. The assets acquired would not represent a

6 New Accounting Pronouncements (Continued)

business if substantially all of the fair value of gross assets acquired is concentrated in a single asset (or a group of similar assets).

Definition of materiality – Amendments to IAS 1 and IAS 8 (issued on 31 October 2018 and effective for annual periods beginning on or after 1 January 2020). The amendments clarify the definition of material and how it should be applied by including in the definition guidance that until now has featured elsewhere in IFRS. In addition, the explanations accompanying the definition have been improved. Finally, the amendments ensure that the definition of material is consistent across all IFRS Standards. Information is material if omitting, misstating or obscuring it could reasonably be expected to influence the decisions that the primary users of general purpose financial statements make on the basis of those financial statements, which provide financial information about a specific reporting entity.

Sale or Contribution of Assets between an Investor and its Associate or Joint Venture – Amendments to IFRS 10 and IAS 28 (issued on 11 September 2014 and effective for annual periods beginning on or after a date to be determined by the IASB). These amendments address an inconsistency between the requirements in IFRS 10 and those in IAS 28 in dealing with the sale or contribution of assets between an investor and its associate or joint venture. The main consequence of the amendments is that a full gain or loss is recognised when a transaction involves a business. A partial gain or loss is recognised when a transaction involves assets that do not constitute a business, even if these assets are held by a subsidiary.

Amendments to the Conceptual Framework for Financial Reporting (issued on 29 March 2018 and effective for annual periods beginning on or after 1 January 2020). The revised Conceptual Framework includes a new chapter on measurement; guidance on reporting financial performance; improved definitions and guidance – in particular the definition of a liability; and clarifications in important areas, such as the roles of stewardship, prudence and measurement uncertainty in financial reporting.

Unless otherwise described above, the new standards and interpretations are not expected to affect significantly the Bank's financial statements.

(Amounts expressed in thousands of Azerbaijani Manats)

7 Cash and Cash Equivalents

Cash and cash equivalents comprise:

	2019	2018
Cash on hand	24,381	33,323
Current accounts with the CBAR	67,271	34,307
Short-term deposits placed in the CBAR	18,033	7,726
Accounts with other credit institutions	92,932	88,254
Less credit loss allowance	(221)	(178)
Cash and cash equivalents	**202,396**	**163,432**

As at 31 December 2019, the Bank had short-term deposits placed in the CBAR amounting to AZN 17,940 (2018: AZN 7,694) maturing until 13 January 2019 (2018: 7 January 2019) with the annual interest rates of 5.76% p.a (2018: 7.76-8.92% p.a).

Current accounts with other credit institutions consist of interest bearing correspondent account balances with resident and non-resident banks of amounting AZN 5,088 (2018: AZN 8,563) and AZN 78,879 (2018: AZN 69,389), respectively.

The credit quality of cash and cash equivalents balances may be summarised based on ratings as follows at 31 December 2019: Refer to Note 23 for the description of the Bank's credit risk grading system.

	Cash balances with the CBAR, excluding mandatory reserves	Accounts with other credit institutions	Total
- Excellent	-	77,723	77,723
- Good	85,161	15,131	100,292
Total cash and cash equivalents, excluding cash on hand	**85,161**	**92,854**	**178,015**

For the purpose of ECL measurement cash and cash equivalents balances are included in Stage 1. Refer to Note 23 for the ECL measurement approach.

The credit quality of cash and cash equivalents balances may be summarised based on Fitch's ratings as follows at 31 December 2018:

	Cash balances with the CBAR, excluding mandatory reserves	Accounts with other credit institutions	Total
- Excellent	-	9,653	9,653
- Good	41,931	78,525	120,456
Total cash and cash equivalents, excluding cash on hand	**41,931**	**88,178**	**130,109**

As of 31 December 2019, the bank had AZN 70,811 or 76% (2018: AZN 67,800 or 77%) of total amounts with other credit institutions placed with one counterparty (2018: one).

Information on related party balances is disclosed in Note 25 .

(Amounts expressed in thousands of Azerbaijani Manats)

8 Amounts Due from Credit Institutions

Amounts due from credit institutions comprise:

	2019	2018
Short-term deposits placed in banks	18,639	59,321
Obligatory reserve with the CBAR	2,457	2,813
Amounts due from credit institutions (gross)	**21,096**	**62,134**
Less: allowance for impairment	(110)	(104)
Amounts due from credit institutions (net)	**20,986**	**62,030**

Credit institutions are required to maintain a non-interest earning cash deposit (obligatory reserve) with the CBAR, the amount of which depends on the level of funds attracted by the credit institution. The Bank's ability to withdraw such deposit is significantly restricted by the statutory legislation.

As at 31 December 2019, the Bank had short-term deposits placed in banks amounting to AZN 18,639 (2018: AZN 59,321) maturing in Feb-May-Oct 2020 (2018: Feb-May 2019), with the annual interest rates of 3.0-7.5% p.a (2018:3.0-3.8% p.a.).

Analysis by credit quality of amounts due from credit institutions outstanding at 31 December 2019, is as follows: Refer to Note 24 for the estimated fair value of each class of amounts due from other banks. Interest rate analysis of due from other banks is disclosed in Note 23. Information on related party balances is disclosed in Note 25:

	Stage 1 (12-months ECL)	Total
Placements with credit institutions		
- Excellent	-	-
- Good	21,096	21,096
Gross carrying amount	**21,096**	**21,096**
Credit loss allowance	(110)	(110)
Total due from credit institutions (carrying amount)	**20,986**	**20,986**

Analysis by credit quality of amounts due from credit institutions outstanding at 31 December 2018, is as follows:

	Stage 1 (12-months ECL)	Total
Placements with credit institutions		
- Excellent	38,370	38,370
- Good	23,764	23,764
Gross carrying amount	**62,134**	**62,134**
Credit loss allowance	(104)	(104)
Total due from credit institutions (carrying amount)	**62,030**	**62,030**

9 Loans to Customers

Loans to customers comprise:

	31 December 2019	31 December 2018
Gross carrying amount of loans and advances to customers at AC	204,171	191,385
Less credit loss allowance	(43,493)	(46,554)
Total carrying amount of loans and advances to customers at AC	**160,678**	**144,831**
Total loans and advances to customers	**160,678**	**144,831**

As at 31 December 2019, out of the total amount of loans 37.6% (2018: 35.5%) are denominated in foreign currencies.

Gross carrying amount and credit loss allowance amount for loans and advances to customers at AC by classes at 31 December 2019 and 31 December 2018 are disclosed in the table below:

	31 December 2019			31 December 2018		
In thousands of Azerbaijani Manat	Gross carrying amount	Credit loss allowance	Carrying amount	Gross carrying amount	Credit loss allowance	Carrying amount
Loans to corporate / commercial customers	129,808	23,323	106,485	106,858	22,667	**84,191**
Loans to SME	14,946	8,310	6,636	19,447	9,061	10,386
Consumer Loans	49,096	10,241	38,855	55,587	13,224	42,363
Residential Mortgage loans	10,321	1,619	8,702	9,493	1,602	7,891
Total loans and advances to customers at AC	**204,171**	**43,493**	**160,678**	**191,385**	**46,554**	**144,831**

More detailed explanation of classes of loans to legal entities is provided below:

- Loans to corporate / commercial customers – loans issued to commercial entities;
- Loans to SME – loans issued to small and medium-sized enterprises;
- Consumer Loans – loans issued to individuals for personal needs;
- Residential Mortgage loans - loans issued to individuals for mortgage purposes.

(Amounts expressed in thousands of Azerbaijani Manats)

9 Loans to Customers (Continued)

The following table discloses the changes in the credit loss allowance and gross carrying amount for loans and advances to customers carried at amortised cost between the beginning and the end of the reporting period and comparative periods.

	Credit loss allowance				Gross carrying amount			
	Stage 1 (12-months ECL)	Stage 2 (lifetime ECL for SICR)	Stage 3 (lifetime ECL for credit im-paired)	Total	Stage 1 (12-months ECL)	Stage 2 (lifetime ECL for SICR)	Stage 3 (lifetime ECL for credit im-paired)	Total
Loans to corporate / commercial customers								
At 31 December 2018	**379**	**347**	**21,942**	**22,668**	**60,645**	**11,462**	**34,751**	**106,858**
Movements with impact on credit loss allowance charge for the period:								
Transfers:								
- to lifetime (from Stage 1 to Stage 2)	(429)	429	-	-	(3,040)	3,040	-	-
- to credit-impaired (from Stage 1 and Stage 2 to Stage 3)	-	(101)	101	-	-	(101)	101	-
- to 12-months ECL (from Stage 2 and Stage 3 to Stage 1)	-	-	-	-	-	-	-	-
New originated or purchased	707	1,584	1,743	4,034	80,607	4,587	3,243	88,437
Derecognized during the period	(247)	(243)	(872)	(1,362)	(47,707)	(11,219)	(1,638)	(60,564)
Other movements	(32)	(1)	(241)	(274)	(2,184)	(37)	274	(1,947)
Total movements with impact on credit loss allowance charge for the period	**378**	**2,015**	**22,673**	**25,066**	**88,321**	**7,732**	**36,731**	**132,784**
Movements without impact on credit loss allowance charge for the period:								
Write-offs	-	-	(1,743)	(1,743)	-	-	(2,976)	(2,976)
At 31 December 2019	**378**	**2,015**	**20,930**	**23,323**	**88,321**	**7,732**	**33,755**	**129,808**

(Amounts expressed in thousands of Azerbaijani Manats)

9 Loans to Customers (Continued)

	Credit loss allowance				Gross carrying amount			
	Stage 1 (12-months ECL)	**Stage 2 (lifetime ECL for SICR)**	**Stage 3 (lifetime ECL for credit im-paired)**	**Total**	**Stage 1 (12-months ECL)**	**Stage 2 (lifetime ECL for SICR)**	**Stage 3 (lifetime ECL for credit im-paired)**	**Total**
Loans to corporate / commercial customers								
At 1 January 2018	**118**	**3,307**	**15,585**	**19,010**	**28,597**	**21,422**	**23,718**	**73,737**
Movements with impact on credit loss allowance charge for the period:								
Transfers:								
- to lifetime (from Stage 1 to Stage 2)	(6)	6	-	-	(1,422)	1,422	-	-
- to credit-impaired (from Stage 1 and Stage 2 to Stage 3)	(37)	(1,970)	2,007	-	(80)	(4,650)	4,730	-
- to 12-months ECL (from Stage 2 and Stage 3 to Stage 1)	3	(3)	-	-	598	(598)	-	-
New originated or purchased	363	309	2,121	2,793	58,213	10,266	4,044	72,523
Derecognised during the period	(112)	(1,546)	(2,015)	(3,673)	(27,970)	(14,465)	(3,441)	(45,876)
Other movements	50	244	4,243	4,537	2,709	(1,935)	5,700	6,474
At 31 December 2018	**379**	**347**	**21,941**	**22,667**	**60,645**	**11,462**	**34,751**	**106,858**

(Amounts expressed in thousands of Azerbaijani Manats)

9 Loans to Customers (Continued)

	Credit loss allowance				Gross carrying amount			
	Stage 1 (12-months ECL)	**Stage 2 (lifetime ECL for SICR)**	**Stage 3 (lifetime ECL for credit im-paired)**	**Total**	**Stage 1 (12-months ECL)**	**Stage 2 (lifetime ECL for SICR)**	**Stage 3 (lifetime ECL for credit im-paired)**	**Total**
Loans to SME								
At 31 December 2018	**20**	**34**	**9,007**	**9,061**	**3,237**	**1,499**	**14,711**	**19,447**
Movements with impact on credit loss allowance charge for the period:								
Transfers:								
- to lifetime (from Stage 1 to Stage 2)	(34)	34	-	-	(92)	92	-	-
- to credit-impaired (from Stage 1 and Stage 2 to Stage 3)	-	(14)	14	-	-	(737)	737	-
- to 12-months ECL (from Stage 2 and Stage 3 to Stage 1)	-	-	-	-	-	-	-	-
New originated or purchased	5	-	9	14	829	-	16	845
Derecognised during the period	(24)	(20)	(661)	(705)	(1,529)	(805)	(1,152)	(3,486)
Other movements	47	(13)	265	299	(205)	-	54	(151)
Total movements with impact on credit loss allowance charge for the period	**14**	**21**	**8,634**	**8,669**	**2,240**	**49**	**14,366**	**16,655**
Movements without impact on credit loss allowance charge for the period:								
Write-offs	-	-	(359)	(359)	-	-	(1,709)	(1,709)
At 31 December 2019	**14**	**21**	**8,275**	**8,310**	**2,240**	**49**	**12,657**	**14,946**

(Amounts expressed in thousands of Azerbaijani Manats)

9 Loans to Customers (Continued)

	Credit loss allowance				Gross carrying amount			
	Stage 1 (12-months ECL)	**Stage 2 (lifetime ECL for SICR)**	**Stage 3 (lifetime ECL for credit im-paired)**	**Total**	**Stage 1 (12-months ECL)**	**Stage 2 (lifetime ECL for SICR)**	**Stage 3 (lifetime ECL for credit im-paired)**	**Total**
Loans to SME								
At 1 January 2018	**66**	**761**	**7,173**	**8,000**	**5,638**	**5,008**	**11,128**	**21,774**
Movements with impact on credit loss allowance charge for the period:								
Transfers:								
- to lifetime (from Stage 1 to Stage 2)	(17)	17	-	-	(667)	667	-	-
- to credit-impaired (from Stage 1 and Stage 2 to Stage 3)	-	(225)	225	-	-	(618)	618	-
- to 12-months ECL (from Stage 2 and Stage 3 to Stage 1)	8	(8)	-	-	287	(287)	-	-
New originated or purchased	21	7	1,074	1,102	3,154	282	1,944	5,380
Derecognised during the period	(52)	(308)	(82)	(442)	(4,369)	(3,511)	(89)	(7,969)
Other movements	(6)	(210)	617	401	(806)	(42)	1,110	262
At 31 December 2018	**20**	**34**	**9,007**	**9,061**	**3,237**	**1,499**	**14,711**	**19,447**

(Amounts expressed in thousands of Azerbaijani Manats)

9 Loans to Customers (Continued)

	Credit loss allowance				Gross carrying amount			
	Stage 1 (12-months ECL)	Stage 2 (lifetime ECL for SICR)	Stage 3 (lifetime ECL for credit im-paired)	Total	Stage 1 (12-months ECL)	Stage 2 (lifetime ECL for SICR)	Stage 3 (lifetime ECL for credit im-paired)	Total
Consumer loans								
At 31 December 2018	**245**	**51**	**12,928**	**13,224**	**39,896**	**1,041**	**14,650**	**55,587**
Movements with impact on credit loss allowance charge for the period:								
Transfers:								
- to lifetime (from Stage 1 to Stage 2)	(12)	12	-	-	(1,224)	1,224	-	-
- to credit-impaired (from Stage 1 and Stage 2 to Stage 3)	(4)	(15)	19	-	(309)	(244)	553	-
- to 12-months ECL (from Stage 2 and Stage 3 to Stage 1)	5	(5)	-	-	241	(241)	-	-
New originated or purchased	1,305	60	128	1,493	16,607	430	224	17,261
Derecognised during the period	(40)	(18)	(2,242)	(2,300)	(13,323)	(460)	(2,818)	(16,601)
Other movements	(60)	24	(544)	(580)	(4,275)	116	(1,167)	(5,326)
Total movements with impact on credit loss allowance charge for the period	**1,439**	**109**	**10,289**	**11,837**	**37,613**	**1,866**	**11,442**	**50,921**
Movements without impact on credit loss allowance charge for the period:								
Write-offs	-	-	(1,596)	(1,596)	-	-	(1,825)	(1,825)
At 31 December 2019	**1,439**	**109**	**8,693**	**10,241**	**37,613**	**1,866**	**9,617**	**49,096**

(Amounts expressed in thousands of Azerbaijani Manats)

9 Loans to Customers (Continued)

	Credit loss allowance				Gross carrying amount			
	Stage 1 (12-months ECL)	**Stage 2 (lifetime ECL for SICR)**	**Stage 3 (lifetime ECL for credit im-paired)**	**Total**	**Stage 1 (12-months ECL)**	**Stage 2 (lifetime ECL for SICR)**	**Stage 3 (lifetime ECL for credit im-paired)**	**Total**
Consumer loans								
At 1 January 2018	**4**	**138**	**9,621**	**9,763**	**34,884**	**1,742**	**15,561**	**52,187**
Movements with impact on credit loss allowance charge for the period:								
Transfers:								
- to lifetime (from Stage 1 to Stage 2)	(34)	34	-	-	(2,375)	2,375	-	-
- to credit-impaired (from Stage 1 and Stage 2 to Stage 3)	(227)	(209)	436	-	(418)	(362)	780	-
- to 12-months ECL (from Stage 2 and Stage 3 to Stage 1)	4	(4)	-	-	499	(474)	(25)	-
New originated or purchased	136	16	95	247	18,331	357	162	18,850
Derecognised during the period	(1)	(49)	(769)	(819)	(9,983)	(627)	(1,361)	(11,971)
Other movements	363	125	3,545	4,033	(1,042)	(1,970)	(467)	(3,479)
At 31 December 2018	**245**	**51**	**12,928**	**13,224**	**39,896**	**1,041**	**14,650**	**55,587**

(Amounts expressed in thousands of Azerbaijani Manats)

9 Loans to Customers (Continued)

	Credit loss allowance				Gross carrying amount			
	Stage 1 (12-months ECL)	**Stage 2 (lifetime ECL for SICR)**	**Stage 3 (lifetime ECL for credit im-paired)**	**Total**	**Stage 1 (12-months ECL)**	**Stage 2 (lifetime ECL for SICR)**	**Stage 3 (lifetime ECL for credit im-paired)**	**Total**
Residential mortgage loans								
At 31 December 2018	**13**	**1**	**1,588**	**1,602**	**6,708**	**229**	**2,556**	**9,493**
Movements with impact on credit loss allowance charge for the period:								
Transfers:								
- to lifetime (from Stage 1 to Stage 2)	(1)	1	-	-	(89)	89	-	-
- to credit-impaired (from Stage 1 and Stage 2 to Stage 3)	-	(1)	1	-	(51)	(55)	106	-
- to 12-months ECL (from Stage 2 and Stage 3 to Stage 1)	-	-	-	-	23	(23)	-	-
New originated or purchased	20	-	-	20	1,911	-	-	1,911
Derecognised during the period	(10)	-	(61)	(71)	(313)	(37)	(188)	(538)
Other movements	44	1	23	68	(507)	(27)	(11)	(545)
Total movements with impact on credit loss allowance charge for the period	**66**	**2**	**1,551**	**1,619**	**7,682**	**176**	**2,463**	**10,321**
Movements without impact on credit loss allowance charge for the period:								
Write-offs	-	-	-	-	-	-	-	-
At 31 December 2019	**66**	**2**	**1,551**	**1,619**	**7,682**	**176**	**2,463**	**10,321**

(Amounts expressed in thousands of Azerbaijani Manats)

9 Loans to Customers (Continued)

	Credit loss allowance				Gross carrying amount			
	Stage 1 (12-months ECL)	**Stage 2 (lifetime ECL for SICR)**	**Stage 3 (lifetime ECL for credit im-paired)**	**Total**	**Stage 1 (12-months ECL)**	**Stage 2 (lifetime ECL for SICR)**	**Stage 3 (lifetime ECL for credit im-paired)**	**Total**
Residential mortgage loans								
At 1 January 2018	**22**	**94**	**1,159**	**1,275**	**6,073**	**1,059**	**1,772**	**8,904**
Movements with impact on credit loss allowance charge for the period:								
Transfers:								
- to lifetime (from Stage 1 to Stage 2)	(1)	1	-	-	(362)	362	-	-
- to credit-impaired (from Stage 1 and Stage 2 to Stage 3)	(34)	(420)	454	-	(63)	(757)	820	-
- to 12-months ECL (from Stage 2 and Stage 3 to Stage 1)	-	-	-	-	150	(62)	(88)	-
New originated or purchased	4	-	30	34	1,770	19	54	1,843
Derecognised during the period	(2)	(8)	(18)	(28)	(415)	(153)	(33)	(601)
Other movements	24	334	(37)	321	(445)	(239)	31	(653)
At 31 December 2018	**13**	**1**	**1,588**	**1,602**	**6,708**	**229**	**2,556**	**9,493**

The credit loss allowance for loans and advances to customers recognised in the period impacted by a variety of factors. Details of ECL measurement are provided in Note 23. The main reasons for movements are as follows:

- 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;
- Additional allowances for new financial instruments recognised during the period, as well as releases for financial instruments derecognised in the period;
- Write-offs of allowances related to assets that were written off during the period.

(Amounts expressed in thousands of Azerbaijani Manats)

9 Loans to Customers (Continued)

Allowance for impairment of loans to customers

Information about collateral at 31 December 2019 is as follows:

	Corporate lending	Small business lending	Consumer lending	Residential mortgages	Total
Unsecured loans	13,812	1,724	48,138	277	63,951
Loans collateralized by:					
Real estate	89,553	13,040	351	10,044	112,988
Cash deposits	16,622	-	187	-	16,809
Other assets	9,820	182	419	-	10,421
Less impairment provisions	(23,322)	(8,310)	(10,240)	(1,619)	(43,491)
Total loans to customers	**106,485**	**6,636**	**38,855**	**8,702**	**160,678**

Information about collateral at 31 December 2018 is as follows:

	Corporate lending	Small business lending	Consumer lending	Residential mortgages	Total
Unsecured loans	17,795	2,750	51,386	73	72,004
Loans collateralized by:					
Real estate	81,057	15,705	1,104	9,420	107,286
Cash deposits	7,245	–	1,391	–	8,636
Other assets	761	992	1,706	–	3,459
Less impairment provisions	(22,667)	(9,061)	(13,224)	(1,602)	(46,554)
Total loans to customers	**84,191**	**10,386**	**42,363**	**7,891**	**144,831**

Other assets mainly include vehicles and equipment. The disclosure above represents the lower of the carrying value of the loan or collateral taken; the remaining part is disclosed within the unsecured exposures. The carrying value of loans was allocated based on liquidity of the assets taken as collateral.

It is the Bank's policy to maintain accurate and consistent risk ratings across the credit portfolio. This facilitates focused management of the applicable risks and the comparison of credit exposures across all lines of business and products. The rating system is supported by a variety of financial analytics, combined with processed market information to provide the main inputs for the measurement of counterparty risk. All internal risk ratings are tailored to the various categories and are derived in accordance with the Bank's rating policy. The attributable risk ratings are assessed and updated regularly.

Loans to customers and other financial assets with good financial position and good debt service are included in the standard grade. Sub-standard grade comprises loans below standard grade that had changes in the terms and conditions of loan agreements, but not individually impaired.

The following tables contain analyses of the credit risk exposure of loans and advances to customers measured at AC and for which ECL allowance is recognised. The carrying amount of loans and advances to customers below also represents the Bank's maximum exposure to credit risk on these loans.

(Amounts expressed in thousands of Azerbaijani Manats)

9 Loans to Customers (Continued)

Analysis by credit quality of loans outstanding at 31 December 2019 is as follows:

	Stage 1 (12-months ECL)	Stage 2 (lifetime ECL for SICR)	Stage 3 (lifetime ECL for credit impaired)	Total
Corporate lending				
Less than 30 days	88,321	5,370	-	93,691
30 to 90 days overdue	-	2,362	-	2,362
91-180 days overdue	-	-	3,340	3,340
181 to 360 days averdue	-	-	192	192
Over 360 days overdue	-	-	30,223	30,223
Gross carrying amount	**88,321**	**7,732**	**33,755**	**129,808**
Credit loss allowance	(378)	(2,015)	(20,930)	(23,323)
Carrying amount	**87,943**	**5,717**	**12,825**	**106,485**
Small business lending				
Less than 30 days	2,240	6	35	2,281
30 to 90 days overdue	-	43	-	43
91-180 days overdue	-	-	-	-
181 to 360 days averdue	-	-	707	707
Over 360 days overdue	-	-	11,915	11,915
Gross carrying amount	**2,240**	**49**	**12,657**	**14,946**
Credit loss allowance	(14)	(21)	(8,275)	(8,310)
Carrying amount	**2,226**	**28**	**4,382**	**6,636**
Consumer lending				
Less than 30 days	37,613	1,086	18	38,717
30 to 90 days overdue	-	780	14	794
91-180 days overdue	-	-	227	227
181 to 360 days averdue	-	-	437	437
Over 360 days overdue	-	-	8,921	8,921
Gross carrying amount	**37,613**	**1,866**	**9,617**	**49,096**
Credit loss allowance	(1,440)	(109)	(8,692)	(10,241)
Carrying amount	36,173	**1,757**	**925**	**38,855**

(Amounts expressed in thousands of Azerbaijani Manats)

9 Loans to Customers (Continued)

	Stage 1 (12-months ECL)	Stage 2 (lifetime ECL for SICR)	Stage 3 (lifetime ECL for credit impaired)	Total
Residential mortgage loans				
Less than 30 days	7,682	9	-	7,691
30 to 90 days overdue	-	168	-	168
91-180 days overdue	-	-	28	28
181 to 360 days averdue	-	-	50	50
Over 360 days overdue	-	-	2,384	2,384
Gross carrying amount	**7,682**	**177**	**2,462**	**10,321**
Credit loss allowance	(67)	(2)	(1,550)	(1,619)
Carrying amount	7,615	**175**	**912**	**8,702**

Analysis by credit quality of loans outstanding at 31 December 2018 is as follows:

	Stage 1 (12-months ECL)	Stage 2 (lifetime ECL for SICR)	Stage 3 (lifetime ECL for credit impaired)	Total
Corporate lending				
Less than 30 days	60,645	11,462	137	72,244
30 to 90 days overdue	-	-	66	66
91-180 days overdue	-	-	3,818	3,818
181 to 360 days averdue	-	-	1,413	1,413
Over 360 days overdue	-	-	29,317	29,317
Gross carrying amount	**60,645**	**11,462**	**34,751**	**106,858**
Credit loss allowance	(379)	(347)	(21,941)	(22,667)
Carrying amount	**60,266**	**11,115**	**12,810**	**84,191**
Small business lending				
Less than 30 days	3,237	168	70	3,475
30 to 90 days overdue	-	1,331	-	1,331
91-180 days overdue	-	-	1,872	1,872
181 to 360 days averdue	-	-	207	207
Over 360 days overdue	-	-	12,562	12,562
Gross carrying amount	**3,237**	**1,499**	**14,711**	**19,447**
Credit loss allowance	(21)	(33)	(9,007)	(9,061)
Carrying amount	**3,216**	**1,466**	**5,704**	**10,386**

(Amounts expressed in thousands of Azerbaijani Manats)

9 Loans to Customers (Continued)

Consumer lending				
Less than 30 days	39,895	494	142	40,531
30 to 90 days overdue	-	546	32	578
91-180 days overdue	-	-	205	205
181 to 360 days averdue	-	-	355	355
Over 360 days overdue	-	-	13,918	13,918
Gross carrying amount	**39,895**	**1,040**	**14,652**	**55,587**
Credit loss allowance	(245)	(51)	(12,928)	(13,224)
Carrying amount	**39,650**	**989**	**1,724**	**42,363**
Residential mortgage loans				
Less than 30 days	6,707	113	116	6,936
30 to 90 days overdue	-	117	-	117
91-180 days overdue	-	-	727	727
181 to 360 days averdue	-	-	41	41
Over 360 days overdue	-	-	1,672	1,672
Gross carrying amount	**6,707**	**230**	**2,556**	**9,493**
Credit loss allowance	**(13)**	**(1)**	**(1,588)**	**(1,602)**
Carrying amount	**6,694**	**229**	**968**	**7,891**

Impairment assessment. The main considerations for the loan impairment assessment are based on the information provided by the roll-rate model, which measures the movement of the past due amounts balances in various time brackets. The Bank addresses impairment assessment in two areas: individually assessed allowances and collectively assessed allowances.

Individually assessed allowances. The Bank determines the allowances appropriate for each individually significant loan on an individual basis. Items considered when determining allowance amounts include the sustainability of the counterparty's business plan, its ability to improve performance once a financial difficulty has arisen, projected receipts and the expected dividend payout should bankruptcy ensue, the availability of other financial support and the realizable value of collateral, the timing of the expected cash flows and expected recoverability of unsecured portion based on management estimates. The impairment losses are evaluated at each reporting date, unless unforeseen circumstances require more careful attention.

Collectively assessed allowances. Allowances are assessed collectively for losses on loans to customers that are not individually significant (including credit cards, residential mortgages and unsecured consumer lending) and for individually significant loans where there is not yet objective evidence of individual impairment. Allowances are evaluated on each reporting date with each portfolio receiving a separate review. The collective assessment takes account of impairment that is likely to be present in the portfolio even though there is no yet objective evidence of the impairment in an individual assessment. Impairment losses are estimated by taking into consideration the roll-rate model assessment. The impairment allowance is then reviewed by credit management to ensure alignment with the Bank's overall policy.

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

(Amounts expressed in thousands of Azerbaijani Manats)

9 Loans to Customers (Continued)

The primary factors that the Bank considers in determining whether a loan is impaired are its overdue status and realis ability of related collateral, if any. As a result, the Bank presents above an ageing analysis of loans that are individually determined to be impaired.

The financial effect of collateral is presented by disclosing collateral values separately for (i) those assets where collateral and other credit enhancements are equal to or exceed carrying value of the asset ("over-collateralised assets") and (ii) those assets where collateral and other credit enhancements are less than the carrying value of the asset ("under-collateralised assets").

The effect of collateral at 31 December 2019:

	Over-collateralized Assets		Under-collateralized assets	
	Carrying value of the assets	Fair value of collateral	Carrying value of the assets	Fair value of collateral
Corporate lending	66,638	147,633	62,923	36,949
Small business lending	3,348	7,196	11,479	6,404
Consumer lending	736	2,511	48,678	356
Residential mortgages	9,094	16,971	1,275	695

The effect of collateral at 31 December 2018:

	Over-collateralised Assets		Under-collateralised assets	
	Carrying value of the assets	Fair value of collateral	Carrying value of the assets	Fair value of collateral
Corporate lending	56,836	142,256	50,022	21,507
Small business lending	8,486	16,448	10,961	4,617
Consumer lending	1,745	7,015	53,842	1,766
Residential mortgages	8,292	17,051	1,201	791

Individually impaired loans

As at 31 December 2019, loans in the amount of AZN 65,939 (2018: AZN 66,668) were assessed individually. An individual impairment allowance of AZN 33,931 (2018: AZN 33,698) were recognized for such loans.

In accordance with the CBAR requirements, loans may only be written off with the approval of the Supervisory Board and, in certain cases, with the respective decision of the Court.

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 corporate lending – charges over real estate and trade receivables, third party guarantees;
- for consumer lending – cash, charges over credited consumer appliances and mortgages over residential properties;
- for auto lending – cash and liens over vehicles.

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

(Amounts expressed in thousands of Azerbaijani Manats)

9 Loans to Customers (Continued)

Concentration of loans to customers

As of 31 December 2019, the Bank had a concentration of loans represented by AZN 65,064 or 32% of gross loan portfolio (2018: AZN 45,904 or 24%) due from the ten (2018: ten) largest third party borrowers.

Loans have been extended to the following types of customers (amounts are presented prior to allowance):

	2019	2018
Private companies	129,808	106,858
Individuals	74,363	84,527
Gross loans to customers	**204,171**	**191,385**

Loans are provided within Azerbaijan in the following industry sectors (amounts are presented prior to allowance):

	2019	2018
Individuals	74,363	84,527
Trading enterprises	86,985	64,881
Real estate construction	24,483	23,366
Manufacturing	18,340	18,611
Gross loans to customers	**204,171**	**191,385**

Refer to Note 24 for the estimated fair value of each class of loans and to customers. Maturity analysis of loans to customers is disclosed in Note 23 . Information on related party balances is disclosed in Note 25 .

(Amounts expressed in thousands of Azerbaijani Manats)

10 Notes Issued by Central Bank of the Republic of Azerbaijan (CBAR) and Other Bonds

	2019	2018
Notes issued by the Central Bank of the Republic of Azerbaijan (CBAR)	33,868	34,706
Bonds issued by the Ministry of Finance of Azerbaijan Republic	2,798	10,699
Other	60	60
Less credit loss allowance	(190)	(239)
Total	**36,536**	**45,226**

As of 31 December 2019, all Notes issued by the Central Bank of the Republic of Azerbaijan (CBAR) and Other Bonds were classified as Stage 1.

Nominal interest rates and maturities of debt securities are as follows:

	2019		2018	
	Annual interest rate	**Maturity**	**Annual interest rate**	**Maturity**
Notes issued by the CBAR	5.76%-6.01%	Jan'20	7.8%-8.3%	Jan'19
Bonds issued by the Ministry of Finance of Azerbaijan Republic	8.46% - 8.79%	Mar"21	7.5%-8.8%	Feb'19-Mar"21

Notes from CBAR has original maturity of 28 days and as per Bank policy represents cash and cash equivalents. Notes from CBAR are neither past due nor impaired.

Bonds from the Ministry of Finance of Azerbaijan Republic has original maturity of 1,092 days. Bonds from Ministry of Finance are neither past due nor impaired.

All debt securities are measured at amortised cost. The credit quality of the debt securities is good. Refer to Note 23 for the description of the Bank's credit risk grading system.

Refer to Note 24 for the estimated fair value of notes issued by Central Bank of the Republic of Azerbaijan and other bonds.

(Amounts expressed in thousands of Azerbaijani Manats)

11 Property and Equipment

The movements in tangible assets were as follows:

	Leasehold improvements	Computers and office equipment	Furniture and fixtures	Motor vehicles	Total
Cost					
31 December 2018	**8,770**	**13,067**	**1,985**	**110**	**23,932**
Additions	88	940	7	1	1,036
Disposals	-	(162)	(11)	–	(173)
Transfers	-	(53)	42	–	(11)
31 December 2019	**8,858**	**13,792**	**2,023**	**111**	**24,784**
Accumulated depreciation					
31 December 2018	**(6,657)**	**(10,820)**	**(1,781)**	**(101)**	**(19,359)**
Depreciation charge	(669)	(833)	(77)	(6)	**(1,585)**
Disposals	–	25	9	–	**34**
Transfers	–	-	-	–	**–**
31 December 2019	**(7,326)**	**(11,628)**	**(1,849)**	**(107)**	**(20,910)**
Net book value					
31 December 2018	**2,113**	**2,247**	**204**	**9**	**4,573**
31 December 2019	**1,532**	**2,164**	**174**	**4**	**3,874**

	Leasehold improvements	Computers and office equipment	Furniture and fixtures	Motor vehicles	Total
Cost					
31 December 2017	**8,722**	**12,111**	**1,948**	**127**	**22,908**
Additions	48	957	61	0	1,066
Disposals	-	(1)	(24)	(17)	(42)
Transfers	-	-	-	–	0
31 December 2018	**8,770**	**13,067**	**1,985**	**110**	**23,932**
Accumulated depreciation					
31 December 2017	**(5,830)**	**(10,035)**	**(1,720)**	**(113)**	**(17,698)**
Depreciation charge	(827)	(786)	(72)	(5)	**(1,690)**
Disposals	–	1	11	17	**29**
Transfers	–	-	-	–	**0**
31 December 2018	**(6,657)**	**(10,820)**	**(1,781)**	**(101)**	**(19,359)**
Net book value					
31 December 2017	**2,892**	**2,076**	**228**	**14**	**5,210**
31 December 2018	**2,113**	**2,247**	**204**	**9**	**4,573**

As at 31 December 2019 gross carrying amount of fully depreciated property and equipment was AZN 11,564 (2018: AZN 10,693).

(Amounts expressed in thousands of Azerbaijani Manats)

12 Intangible Assets

The movements in intangible assets were as follows:

	Licenses	Computer software	Total
Cost			
31 December 2018	**9,568**	**10,212**	**19,780**
Additions	1,144	1,061	2,205
Disposals	(31)		(31)
Transfers	11		11
31 December 2019	**10,692**	**11,273**	**21,965**
Accumulated amortization			
31 December 2018	**(8,336)**	**(3,504)**	**(11,840)**
Amortization charge	(1,198)	(1,037)	(2,235)
31 December 2019	**(9,534)**	**(4,541)**	**(14,075)**
Net book value			
31 December 2018	**1,232**	**6,708**	**7,940**
31 December 2019	**1,158**	**6,732**	**7,890**

	Licenses	Computer software	Total
Cost			
31 December 2017	**8,485**	**8,929**	**17,414**
Additions	1,083	1,283	2,366
31 December 2018	**9,568**	**10,212**	**19,780**
Accumulated amortization			
31 December 2017	**(6,933)**	**(2,529)**	**(9,462)**
Amortization charge	(1,403)	(975)	(2,378)
31 December 2018	**(8,336)**	**(3,504)**	**(11,840)**
Net book value			
31 December 2017	**1,552**	**6,400**	**7,952**
31 December 2018	**1,232**	**6,708**	**7,940**

As at 31 December 2019 gross carrying amount of fully amortized intangible assets was AZN 8,661 (2018: AZN 7,646).

(Amounts expressed in thousands of Azerbaijani Manats)

13 Right of Use Assets and Lease Liabilities

The Bank leases buildings, vehicles and others. Rental contracts are typically made for fixed periods but may have extension options.

Contracts may contain both lease and non-lease components. The Bank elected not to separate lease and non-lease components and instead accounts for these as a single lease component.

Lease terms are negotiated on an individual basis and contain a wide range of different terms and conditions. The lease agreements do not impose any covenants other than the security interests in the leased assets that are held by the lessor. Leased assets may not be used as security for borrowing purposes.

Extension and termination options are included in a number of leases across the Bank. These are used to maximise operational flexibility in terms of managing the assets used in the Bank's operations. The majority of extension and termination options held are exercisable by both the Bank and the respective lessors.

Until 31 December 2018 leases of premises and equipment were classified as operating leases. From 1 January 2019, leases are recognised as a right-of-use asset and a corresponding liability from the date when the leased asset becomes available for use by the Bank.

The right of use assets by class of underlying items is analysed as follows:

	Buildings	**Vehicles**	**Other**	**Total**
Carrying amount at 1 January 2019	**5,624**	**651**	**99**	**6,374**
Additions	2,009	540	74	**2,623**
Disposals	(190)	(651)	(77)	**(918)**
Depreciation charge	(2,051)	(181)	(96)	**(2,328)**
Carrying amount at 31 December 2019	**5,392**	**359**	**-**	**5,751**

Interest expense on lease liabilities was AZN 360. Total cash outflow for leases in 2019 was AZN 2,680.

At the end of each reporting period, the expected residual values are reviewed to reflect actual residual values achieved on comparable assets and expectations about future prices. As at 31 December 2019, AZN 9,123 is expected to be payable and is included in calculating the lease liabilities.

(Amounts expressed in thousands of Azerbaijani Manats)

14 Income Taxes

The corporate income tax expense comprises:

	2019	2018
Current tax charge	(1,403)	(1,894)
Prior year tax expense actualization	(36)	(2)
Deferred income tax credit for the year	29	(225)
Income tax expense	**(1,410)**	**(2,121)**

Standard corporate income tax rate for companies (including banks) comprised 20% for 2019 and 2018. The effective income tax rate differs from the statutory income tax rates. A reconciliation of the income tax expense based on statutory rates with actual is as follows:

	2019	2018
Profit before income tax expense	**7,605**	**8,075**
Statutory tax rate	20%	20%
Income tax expense at the statutory rate	(1,521)	(1,615)
Tax effect of items which are not deductible or assessable for taxation purposes:		
Impact of Non-deductible expenses	118	(279)
Impact of Prior year tax expense	(36)	(2)
Impact of temporary difference	29	(225)
Income tax expense	**(1,410)**	**(2,121)**

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

	2017	Recognized in retained earnings (Adoption of IFRS 9)	Recognized in the statement of profit or loss and other comprehensive income	2018	Recognized in the statement of profit or loss and other comprehensive income	2019
Tax effect of temporary differences						
Cash and cash equivalents	-	227	-	227	(183)	44
Investment securities available-for-sale	-	-	-	-	38	38
Amounts due from credit institutions	(291)	-	-	(291)	241	(50)
Loans to customers	(2,828)	203	(363)	(2,988)	1	(2,987)
Property and equipment	285	-	37	322	75	397
Intangible assets	(59)	-	-	(59)	(36)	(95)
Other liabilities	610	-	(91)	519	74	593
Other assets	(87)	20	192	125	(181)	(56)
Deferred tax liability	**(2,370)**	**450**	**(225)**	**(2,145)**	**29**	**(2,116)**

(Amounts expressed in thousands of Azerbaijani Manats)

15 Other Assets and Liabilities

Other assets comprise:

	2019	2018
Amounts in the course of settlement	2,865	2,957
Other financial assets	**2,865**	**2,957**
Repossessed collateral	2,703	2,803
Prepayments	2,892	2,011
Tax Receivables	473	-
Other	3	22
Other non-financial assets	**6,071**	**4,836**
Other assets	**8,936**	**7,793**

As at 31 December 2019, prepayments of AZN 2,892 (2018: AZN 2,011) primarily comprise of advance payments for purchase of property, equipment and insurance.

Other liabilities comprise:

	2019	2018
Settlements on plastic cards	3,469	3,057
Lease Liabilities	5,698	-
Other	174	122
Other financial liabilities	**9,341**	**3,179**
Accrued employee costs	1,644	1,168
Payables to social funds	430	613
Deferred income	463	519
Provisions	383	356
Other	661	258
Other non-financial liabilities	**3,581**	**2,914**
Other liabilities	**12,922**	**6,093**

Accrued employee costs include bonuses for employees based on the financial performance of the Bank of AZN 926 (2018: AZN 458) and an accrual for unused vacations of AZN 718 (2018: AZN 710).

As at 31 December 2019 and 2018, deferred income represents deferred revenue which was primarily comprised of fee received for issuance of plastic cards, guarantees and letter of credits.

As at 31 December 2019, AZN 230 (2018: 53) of other non-financial liabilities is other tax liabilities.

Analysis by credit quality of other financial assets outstanding at 31 December 2019 is as follows:

Settlements on money transfers	**2019**	**2018**
Neither past due nor impaired		
Other financial assets		
Good	2,865	2,957
Total other financial assets	**2,865**	**2,957**

(Amounts expressed in thousands of Azerbaijani Manats)

16 Amounts Due to Credit Institutions

Amounts due to credit institutions comprise:

	2019	2018
Amounts due to Azerbaijan Mortgage Fund	5,624	4,558
Amounts due to the National Fund for Entrepreneurship Support	4,289	2,200
Demand deposits	138	512
Amounts due to credit institutions	**10,051**	**7,270**

As at 31 December 2019, the Bank had loans financed by the Azerbaijan Mortgage Fund and National Fund for Entrepreneurship Support amounting to AZN 5,624 (2018: AZN 4,558) and AZN 4,289 (2018: AZN 2,200) maturing in 2043 (2018: 2048) and 2024 (2018: 2023), with the annual interest rates of 1-4% p.a. (2018: 1-4% p.a.) and 1% p.a. (2018: 1% p.a.), respectively.

17 Amounts Due to Customers

The amounts due to customers include the following:

	2019	2018
Current accounts	276,430	235,334
Time deposits	54,179	99,716
Amounts due to customers	**330,609**	**335,050**

As at 31 December 2019, amounts due to customers of AZN 144,537 or 44% (2018: AZN 136,650 or 41%) of total amounts due to customers were due to ten (2018: ten) largest customers.

The average annual interest rate on term deposits of individual customers outstanding at 31 December 2019 comprised 2.39% (2018: 2.73%), while the average annual interest rate on term deposits of legal entities outstanding at 31 December 2019 was 3.59% (2018: 2.16%).

Amounts due to customers include accounts with the following types of customers:

	2019	2018
Private enterprises	231,322	227,960
Individuals	99,244	106,931
Public organizations	43	159
Amounts due to customers	**330,609**	**335,050**

An analysis of customer accounts by economic sector follows:

	2019	2018
Trade	142,026	181,521
Individuals	99,244	106,931
Real estate constructions	60,783	18,901
Insurance and other financial institutions	8,914	14,221
Transport and communication	13,524	11,304
State and public organizations	6,118	2,172
Amounts due to customers	**330,609**	**335,050**

Refer to Note 24 for the disclosure of the fair value of each class of customer accounts. Information on related party balances is disclosed in Note 25 .

(Amounts expressed in thousands of Azerbaijani Manats)

18 Share Capital

As at 31 December 2019 number of ordinary shares are 2,769,035,194 (2018: 2,769,035,194). All ordinary shares have a nominal value of 0.02 per share denominated in Azerbaijani Manats and rank equally. Each share carries one vote.

The share capital of the Bank was contributed by the shareholders in Azerbaijani Manats and they are entitled to dividends and any capital distribution in Azerbaijani Manats.

At 31 December 2019 and 2018, the share capital of the Bank was, as follows:

	Number of outstanding ordinary shares	Total nominal value of paid-in and registered ordinary shares
31 December 2018	**2,769,035,194**	**55,381**
New shares issued	-	-
31 December 2019	**2,769,035,194**	**55,381**

19 Commitments and Contingencies

Legal proceedings. 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 of the Bank.

Tax contingencies. Azerbaijani tax, currency and customs legislation is subject to varying interpretations, and changes, which can occur frequently. Management's interpretation of such legislation as applied to the transactions and activity of the Bank may be challenged by the relevant authorities. Recent events within Azerbaijan suggest that the tax authorities are taking a more assertive position in its interpretation of the legislation and assessments and, as a result, it is possible that transactions and activities that have not been challenged in the past may be challenged. As such, significant additional taxes, penalties and interest may be assessed. Fiscal periods remain open to review by the authorities in respect of taxes for three calendar years preceding the year of review.

Management believes that as at 31 December 2019 its interpretation of the relevant legislation is appropriate and that the Bank's tax and social contribution position will be sustained.

Insurance. The Bank has not currently obtained insurance coverage related to liabilities arising from errors or omissions. Liability insurance is generally not available in Azerbaijan at present.

Compliance with regulatory ratios. The regulator requires banks to maintain certain prudential ratios computed based on statutory financial statements. As at 31 December 2019, the Bank was in compliance with all prudential ratios.

The Bank provides guarantees and letters of credit to customers with primary purpose of ensuring that funds are available to a customer as required. Guarantees and standby letters of credit represent irrevocable assurances that the Bank will make payments in the event that a customer cannot meet its obligations to third parties. Documentary and commercial letters of credit, which are written undertakings by the Bank on behalf of a customer authorizing a third party to draw drafts on the Bank up to a stipulated amount under specific terms and conditions, are collateralized by the underlying shipments of goods, to which they relate, or cash deposits and, therefore, carry less risk than a direct borrowing.

(Amounts expressed in thousands of Azerbaijani Manats)

19 Commitments and Contingencies (Continued)

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

	2019	2018
Credit related commitments		
Undrawn loan commitments	78,792	73,939
Guarantees issued	17,628	21,666
Letters of credit	1,904	7,489
Total	**98,324**	**103,094**
Less – cash held as security against guarantees	(4,284)	(881)
Commitments and contingencies	**94,040**	**102,213**

Most of the outstanding guarantee letters as at 31 December 2019 and 2018 represent guarantees issued to clients for the letters' performance on delivering goods and services, and tender guarantees issued to clients as a pledge of their intent to participate in a bidding tender, announced by various institutions.

20 Net Fee and Commission Income

Net fee and commission income comprises:

	2019	2018
Plastic card operations	4,030	4,628
Settlements operations	3,872	3,709
Cash operations	1,587	1,455
Guarantees and letters of credit	737	800
Agent activities	248	266
Other	55	36
Fee and commission income	**10,529**	**10,894**
Plastic card operations	(3,711)	(3,658)
Settlements operations	(1,287)	(1,425)
Agent activities	(219)	(234)
Guarantees and letters of credit	(13)	(16)
Other	(342)	(320)
Fee and commission expense	**(5,572)**	**(5,653)**
Net fee and commission income	**4,957**	**5,241**

21 Personnel Expenses

	2019	2018
Salaries and bonuses	(8,013)	(7,395)
Social security costs	(1,013)	(1,457)
Other employee benefits	(893)	(935)
Personnel expenses	**(9,919)**	**(9,787)**

(Amounts expressed in thousands of Azerbaijani Manats)

22 General and Administrative Expenses

	2019	2018
Support expenses	(1,722)	(1,723)
Repairs and Maintenance	(892)	(763)
Communications	(846)	(961)
Legal and consultancy	(840)	(882)
Security	(838)	(758)
Marketing and advertising	(467)	(640)
Membership	(324)	(362)
Utilities	(279)	(300)
Operating taxes other than income tax	(208)	(79)
Entertainment	(143)	(115)
Insurance	(123)	(83)
Office supplies	(115)	(114)
Losses on disposal of fixed assets and intangible assets	(35)	(13)
Business travel	(27)	(49)
Occupancy and rent	-	(2,569)
Other expenses	(477)	(906)
General and administrative expenses	**(7,336)**	**(10,317)**

23 Financial Risk Management

Risk is inherent in the Bank's activities and managed through a process of ongoing identification, measurement and monitoring, subject to risk limits and other controls. This process of risk management is critical to the Bank's sustainability and profitability and each individual within the Bank is accountable for the risk exposures relating to his or her responsibilities. The Bank is exposed to credit risk, liquidity risk, market risk and operating risks.

The independent risk control process does not include business risks such as changes in the environment, technology and industry. They are monitored through the Bank's strategic planning process.

Risk management structure. The Board of Directors is ultimately responsible for identifying and controlling risks; however, there are separate independent bodies responsible for managing and monitoring risks.

Board of Directors. The Board of Directors is responsible for the overall risk management approach and for approving the risk strategies and principles.

Management Board. The Management Board has the responsibility to monitor the overall risk process within the Bank.

Risk Committee. The Risk Committee has the overall responsibility for the development of the risk strategy and implementing principles, frameworks, policies and limits. It is responsible for the fundamental risk issues and manages and monitors relevant risk decisions.

Risk Management Unit. The Risk Management Unit is responsible for implementing and maintaining risk related procedures to ensure an independent control process.

Risk Controlling Unit. The Risk Controlling Unit is responsible for monitoring compliance with risk principles, policies and limits, across the Bank. Each business group has a decentralized unit which is responsible for the independent control of risks, including monitoring the risk of exposures against limits and the assessment of risks of new products and structured transactions. This unit also ensures the complete capture of the risks in risk measurement and reporting systems.

Bank Treasury. Bank Treasury is responsible for managing the Bank's assets and liabilities and the overall financial structure. It is also primarily responsible for the funding and liquidity risks of the Bank.

Internal Audit. Risk management processes throughout the Bank are audited annually by the internal audit function that examines both the adequacy of the procedures and the Bank's compliance with the procedures. Internal Audit discusses the results of all assessments with management, and reports its findings and recommendations to the Audit Committee.

23 Financial Risk Management (Continued)

Risk measurement and reporting systems. The Bank's risks are measured using a method which reflects both the expected loss likely to arise in normal circumstances and unexpected losses, which are an estimate of the ultimate actual loss based on statistical models. The models make use of probabilities derived from historical experience, adjusted to reflect the economic environment. The Bank also runs worst case scenarios that would arise in the event that extreme events which are unlikely to occur do, in fact, occur.

Monitoring and controlling risks is primarily performed based on limits established by the Bank. These limits reflect the business strategy and market environment of the Bank as well as the level of risk that the Bank is willing to accept, with additional emphasis on selected industries. In addition the Bank monitors and measures the overall risk bearing capacity in relation to the aggregate risk exposure across all risks types and activities.

Information compiled from all the businesses is examined and processed in order to analyze, control and identify early risks. On a regular basis detailed reporting of industry and customer risks takes place.

Excessive risk concentration. Concentrations arise when a number of counterparties are engaged in similar business activities, or activities in the same geographic region, or have similar economic features that would cause their ability to meet contractual obligations to be similarly affected by changes in economic, political or other conditions. Concentrations indicate the relative sensitivity of the Bank's performance to developments affecting a particular industry.

In order to avoid excessive concentrations of risks, the Bank's policies and procedures include specific guidelines to focus on maintaining a diversified portfolio. Identified concentrations of credit risks are controlled and managed accordingly.

Credit risk. The Bank exposes itself to credit risk, which is the risk that one party to a financial instrument will cause a financial loss for the other party by failing to meet an obligation.

Exposure to credit risk arises as a result of the Bank's lending and other transactions with counterparties, giving rise to financial assets and off-balance sheet credit-related commitments.

The Bank's maximum exposure to credit risk is reflected in the carrying amounts of financial assets in the statement of financial position. For financial guarantees issued, commitments to extend credit, undrawn credit lines and export/import letters of credit, the maximum exposure to credit risk is the amount of the commitment.

Credit-related commitments risks. The Bank offers guarantees to its customers which may require that the Bank makes payments on their behalf. Such payments are collected from customers based on the terms of the letter of credit. They expose the Bank to risks similar 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, before the effect of mitigation through the use of master netting and collateral agreements, is best represented by their carrying amounts.

Credit quality per class of financial assets. The credit quality of financial assets is managed by the Bank internal credit ratings. The table below shows the credit quality by class of asset for loan-related lines in the statement of financial position, based on the Bank's credit rating system.

The Bank manages and controls credit risk by setting limits on the amount of risk it is willing to accept for individual counterparties and for geographical and industry concentrations, and by monitoring exposures in relation to such limits.

The Bank has established a credit quality review process to provide early identification of possible changes in the creditworthiness of counterparties, including regular collateral revisions. Counterparty limits are established by the use of a credit risk classification system, which assigns each counterparty a risk rating at initiation. The Bank actively uses collateral to reduce its credit risks.

Expected credit loss (ECL) is a probability-weighted estimate of the present value of future cash shortfalls (i.e., the weighted average of credit losses, with the respective risks of default occurring in a given time

23 Financial Risk Management (Continued)

period used as weights). An ECL measurement is unbiased and is determined by adjusting risk of default to the expectations on development of macroeconomic situation in future. ECL measurement is based on four components used by the Bank: Probability of Default ("PD"), Exposure at Default ("EAD"), Loss Given Default ("LGD") and Discount Rate.

Default definition. The Bank defines default as a situation when the exposure meets one or more of the following criteria:

- The loan was 90+ days overdue at any point within the considered time horizon

Expected credit losses are modelled over instrument's *lifetime period*. The *lifetime period* is equal to the remaining contractual period to maturity of debt instruments, adjusted for expected prepayments, if any. For loan commitments and financial guarantee contracts, it is the contractual period over which an entity has a present contractual obligation to extend credit. As a matter of exception from determining the lifetime exposure based on contractual maturity, for credit cards issued to individuals, the lifetime exposure is measured over a period that is based on expected life of the credit card contracts, based on internal statistics, and it is equal on average to 1 to 5 years.

Management models *Lifetime ECL,* that is, losses that result from all possible default events over the remaining lifetime period of the financial instrument. The *12-month ECL,* represents a portion of lifetime ECLs that result from default events on a financial instrument that are possible within 12 months after the reporting period, or remaining *lifetime period* of the financial instrument if it is less than a year.

The Bank has three approaches for ECL measurement: (i) assessment on an individual basis; (ii) assessment on a portfolio basis: internal ratings are estimated on an individual basis but the same credit risk parameters (e.g. PD, LGD) will be applied during the process of ECL calculations for the same creditrisk ratings and homogeneous segments of the loan portfolio; and (iii) assessment based on external ratings

The level of ECL that is recognised in these financial statements depends on whether the credit risk of the borrower has increased significantly since initial recognition. This is a three-stage model for ECL measurement. A financial instrument that is not credit-impaired on initial recognition and its credit risk has not increased significantly since initial recognition has a credit loss allowance based on 12-month ECLs (Stage 1). If a SICR since initial recognition is identified, the financial instrument is moved to Stage 2 but is not yet deemed to be credit-impaired and the loss allowance is based on lifetime ECLs. If a financial instrument is credit-impaired, the financial instrument is moved to Stage 3 and loss allowance is based on lifetime ECLs. The consequence of an asset being in Stage 3 is that the entity ceases to recognise interest income based on gross carrying value and applies the asset's effective interest rate to the carrying amount, net of ECL, when calculating interest income.

If there is evidence that the SICR criteria are no longer met, the instrument is transferred back to Stage 1. If an exposure has been transferred to Stage 2 based on a qualitative indicator, the Bank monitors whether that indicator continues to exist or has changed.

Leaving default status depends on which defaulted triggers exposure experienced during its default. Number of scenarios can be limited to two:

- if exposure experienced only more than 90 days past due then it's no longer considered as default when it reaches 30 days delinquency;
- if exposure experienced also other default triggers then it leaves default status when it no longer meets any of the default criteria for a consecutive period of twelve months;

This logic has been determined based on an analysis that considers the likelihood of a financial instrument returning to default status after curing by using different possible definitions of cures

ECL measurement for financial guarantees and loan commitments. The ECL measurement for these instruments includes the same steps as described above for on-balance sheet exposures and differs with respect to EAD calculation. The EAD is a product of credit conversion factor ("CCF") and amount of the commitment ("$ExOff$"). CCF for undrawn credit lines of corporate customers, credit cards issued to individuals and for financial guarantees is defined based on statistical analysis of past exposures at default. CCF for overdrafts is defined as 100% since the limits can be used by the customers at any time.

23 Financial Risk Management (Continued)

Internal ratings. For purpose of PD modelling were created simplified behavioural scoring models that were developed to differentiate the risk profile of an individual exposure.

Credit scoring is an instrument widely used by companies for the internal processes of portfolio risk measurement and management. Scoring can be defined in general as a statistical technique to predict, at a specific point in time with the available information, the probability of a future event. More specifically it allows banks to estimate the probability of default of a person requesting credit (then application scoring model is usually used) or a customer already in the portfolio (behavioural scoring model).

The main assumption for scoring model development is that the past behaviour is a good predictor for the future, thus models are developed based on historical data. In particular, behavioural models are leveraging the information regarding past delinquency, historical credit utilization, history of payments or collection actions. In practice, credit scoring results in the definition of a table listing the characteristics that provide the most predictive information together with the associated attributes and weightings. A total score is obtained as the sum of the points for each characteristic.
Credit granting authorization levels are also determined in accordance with the rating of Corporate, Commercial and SME customers. By using this methodology; it is aimed to establish risk based optimization of credit processes through assigning the lower rated customer to higher authority levels whereas assigning higher rated customer to lower authority levels.

The Bank takes following criterias into consideration for the identification of default:

- The loan is overdue more than 90 days.
- The borrower is not able to pay at least one of the loans he received from the Bank (cross default)
- Having a negative intelligence and bad-record for the borrower in the market.
- Deterioration of the creditworthiness of the borrower

Ratings, which were created base on score values, gather exposures with similar risk profile. Therefore PDs are estimated on homogenies risk groups (i.e. per segment and rating).

External ratings. External ratings are assigned to counterparties by independent international rating agencies, such as S&P, Moody's and Fitch. These ratings are publicly available. Such ratings and the corresponding range of PD are applied for the following financial instruments: amounts due from the CBAR, balances on correspondent accounts including overnight deposits and deposits.

Master scale credit risk grade	Corresponding ratings of external international rating agencies (S&P)	Corresponding PD interval
Excellent	AAA to BB+	0,01% - 0,5%
Good	BB to B+	0,51% - 3%
Satisfactory	B, B-	3% - 10%
Special monitoring	CCC+ to CC-	10% - 99,9%
Default	C, D-I, D-II	100%

Each master scale credit risk grade is assigned a specific degree of creditworthiness:

- *Excellent* – strong credit quality with low expected credit risk;
- *Good* – adequate credit quality with a moderate credit risk;e
- *Satisfactory* – moderate credit quality with a satisfactory credit risk;
- *Special monitoring* – facilities that require closer monitoring and remedial management; and
- *Default* – facilities in which a default has occurred.

External ratings are assigned to counterparties by independent international rating agencies, such as S&P, Moody's and Fitch. These ratings are publicly available.

23 Financial Risk Management (Continued)

Probability of default (PD). PD is an estimate of the likelihood of default to occur over a given time period. For every exposure is estimated lifetime PD curve which is dependant from time, credit risk rating and segment. 12-month PD is calculated as part of lifetime PD curve. The Bank uses different statistical approaches depending on the segment and product type to calculated lifetime PDs, such as Bayesian Scalar approach, Weibull and Adjusted Weibull distribution.

Two types of PDs are used for calculating ECLs: 12-month and lifetime PD. An assessment of a 12-month PD is based on the latest available historic default data and adjusted for supportable forward-looking information when appropriate. Lifetime PDs represent the estimated probability of a default occurring over the remaining life of the financial instrument and it is a sum of the 12 months PDs over the life of the instrument. The Bank uses different statistical approaches depending on the segment and product type to calculated lifetime PDs, such as the extrapolation of 12-month PDs based on migration matrixes, developing lifetime PD curves based on the historical default data, hazard rate approach or other.

Macro-economic factors. Internal bank forecasts provide the best estimate of the expected macro-economic development over the next 3 years. After 3 years, no macro-economic impact is used. The impact of the relevant economic variables on the PD has been determined by performing statistical regression analysis to understand the impact that the changes in these variables historically had on the default rates.

As with any economic forecast, the projections are subject to a high degree of inherent uncertainty, and therefore the actual outcomes may be significantly different to those projected. The Bank considers these forecasts to represent its best estimate of the possible outcomes.

Loss given default (LGD). LGD is an estimate of the loss arising on default. It is based on the difference between the contractual cash flows due and those that the lender would expect to receive. It is usually expressed as a percentage of the gross book value. The expected losses are discounted to present value at the end of the reporting period.

LGD varies by the type of counterparty and product type. The LGDs are determined based on the factors that impact the expected recoveries after a default event. The calculation of LGD is based on recovery statistics.

LGD represents the Bank's expectation of the extent of loss on a defaulted exposure. LGD varies by the type of counterparty, type and seniority of the claim, and the availability of collateral or other credit support.

The 12-month and lifetime LGDs are determined based on the factors that impact the expected recoveries after a default event. The approach to LGD measurement can be divided into three possible approaches:

- measurement of LGD based on the specific characteristics of the collateral;
- calculation of LGD on a portfolio basis based on recovery statistics; or
- individually defined LGD depending on different factors and scenarios.

The Bank calculates LGD based on specific characteristics of the collateral, such as projected collateral values, historical discounts on sales and other factors for loans secured by real estate, cash and liquid securities. LGD is calculated on a collective basis based on the latest available recovery statistics for the remainder of the corporate loan portfolio and for retail secured and unsecured products.

Exposure at default (EAD). EAD is an estimate of exposure at a future default date, taking into account expected changes in the exposure after the reporting period, including repayments of principal and interest, and expected drawdowns on committed facilities.

For revolving products EAD is estimated using Credit Conversion Factor ("CCF"). CCF is a coefficient that shows the probability of conversion of the off-balance amounts to an on-balance sheet exposure within a defined period. CCF for financial guarantees is defined based on globally accepted Basel 3 standard.

23 Financial Risk Management (Continued)

The EADs are determined based on the expected payment profile that varies by product type. EAD is based on the contractual repayments owed by the borrower over a 12-month or lifetime basis for amortising products and bullet repayment loans. This will also be adjusted for any expected overpayments made by a borrower. Early repayment or refinancing assumptions are also incorporated into the calculation. For revolving products, the EAD is predicted by taking the current drawn balance and adding a "credit conversion factor" that accounts for the expected drawdown of the remaining limit by the time of default. These assumptions vary by product type, current limit utilisation and other borrower-specific behavioural characteristics.

Staging

The level of ECL that is recognised in these financial statements depends on which stage was assigned to exposure from a three stage model. A financial instrument that is not credit-impaired on initial recognition and its credit risk has not deteriorated significantly since initial recognition has a credit loss allowance based on 12-month ECLs (Stage 1). If a stage 2 since initial recognition is identified, the financial instrument is moved to Stage 2 but is not yet deemed to be credit-impaired and the loss allowance is based on lifetime ECLs. If a financial instrument is credit-impaired, the financial instrument is moved to Stage 3 and loss allowance is based on lifetime ECLs. The consequence of an asset being in Stage 3 is that the entity ceases to recognise interest income based on gross carrying value and applies the asset's nominal interest rate to the carrying amount, net of ECL, when calculating interest income.

- *Significant deterioration in credit risk (Stage 2)*

The assessment whether or not there has been a significant deterioration in credit risk (stage 2) since initial recognition is performed on whole portfolio. The criteria used to identify stage 2 are monitored and reviewed periodically for appropriateness by the Bank's Risk Management Department. The presumption, being that there have been significant deterioration in credit risk since initial recognition when financial assets are more than 30 days past due, has not been rebutted.

The Bank considers a financial instrument to have experienced a stage 2 when one or more of the following quantitative, qualitative or backstop criteria have been met:

- 31-90 days overdue
- Restructured overdue loans
- Clients with specific monitoring status
- Any other relevant management information on financial situation deterioration on the customer.

If there is evidence that the stage 2 criteria are no longer met, the instrument is transferred back to Stage 1 after quarantine, which is defined as 6 months.

If an exposure has been transferred to Stage 2 based on a qualitative indicator, the Bank monitors whether that indicator continues to apply or it is no longer valid.

Forward-looking information incorporated in the ECL models. The assessment of SICR and the calculation of ECLs both incorporate supportable forward-looking information. The Bank identified certain key economic variables that correlate with developments in credit risk and ECLs. Forecasts of economic variables (the "base economic scenario") are provided by the Bank's and provide the best estimate of the expected macro-economic development over the next three years. The impact of the relevant economic variables on the PD, EAD and LGD has been determined by performing statistical regression analysis to understand the impact that the changes in these variables historically had on the default rates and on the components of LGD and EAD.

In addition to the base economic scenario, the Bank's Risk Department also provides other possible scenarios along with scenario weightings. The number of other scenarios used is set based on the analysis of each major product type to ensure that non-linearities are captured. The number of scenarios and their attributes are reassessed at each reporting date. The scenario weightings are determined by a combination of statistical analysis and expert credit judgement, taking into account the range of possible outcomes of which each chosen scenario is representative. The assessment of SICR is performed using the Lifetime PD under each of the bases and the other scenarios, multiplied by the associated scenario weighting, along with qualitative and backstop indicators. This determines whether the whole financial instrument is in

(Amounts expressed in thousands of Azerbaijani Manats)

23 Financial Risk Management (Continued)

Stage 1, Stage 2, or Stage 3 and hence whether a 12-month or lifetime ECL should be recorded. Following this assessment, the Bank measures ECL as either a probability-weighted 12 month ECL (Stage 1), or a probability weighted lifetime ECL (Stages 2 and 3). These probability-weighted ECLs are determined by running each scenario through the relevant ECL model and multiplying it by the appropriate scenario weighting (as opposed to weighting the inputs).

As with any economic forecast, the projections and likelihoods of occurrence are subject to a high degree of inherent uncertainty, and therefore the actual outcomes may be significantly different to those projected. The Bank considers these forecasts to represent its best estimate of the possible outcomes and has analysed the non-linearities and asymmetries within the Bank's different portfolios to establish that the chosen scenarios are appropriately representative of the range of possible scenarios.

The Bank regularly reviews its methodology and assumptions to reduce any difference between the estimates and the actual loss of credit. Such backtesting is performed at least once a year.

The results of backtesting the ECL measurement methodology are communicated to Bank Management and further steps for tuning models and assumptions are defined after discussions between authorised persons.

The geographical concentration of the Bank's monetary assets and liabilities is set out below:

	2019				2018			
	Azerbaijan	**OECD**	**CIS and other foreign countries**	**Total**	**Azerbaijan**	**OECD**	**CIS and other foreign countries**	**Total**
Assets								
Cash and cash equivalents	114,592	87,731	73	**202,396**	83,833	79,384	215	**163,432**
Amounts due from credit institutions	8,551	6,156	6,279	**20,986**	2,807	42,579	16,644	**62,030**
Loans to customers	160,678	–	–	**160,678**	144,831	–	–	**144,831**
Notes issued by CBAR and other bonds	36,536	–	–	**36,536**	45,226	–	–	**45,226**
Other financial assets	2,865	–	–	**2,865**	2,957	–	–	**2,957**
Total assets	**323,222**	**93,887**	**6,352**	**423,461**	**279,654**	**121,963**	**16,859**	**418,476**
Liabilities								
Amounts due to credit institutions	10,051	–	–	**10,051**	7,237	–	33	**7,270**
Amounts due to customers	330,609	–	–	**330,609**	335,050	–	–	**335,050**
Other financial liabilities	9,341	–	–	**9,341**	3,179	–	–	**3,179**
Total liabilities	**350,001**	**-**	**-**	**350,001**	**345,466**	**-**	**33**	**345,499**
Net assets/(liabilities)	**(26,779)**	**93,887**	**6,352**	**73,460**	**(65,812)**	**121,963**	**16,826**	**72,977**

Liquidity risk and funding management

Liquidity risk is the risk that the Bank will be unable to meet its payment obligations when they fall due under normal and stress circumstances. To limit this risk, management has developed a sophisticated system for comprehensive assessment of expected cash flows. The methodology of the liquidity management tools and reports is approved by the Supervisory Board of the Bank, prepared by the Assets and Liabilities Management department and reviewed on the monthly basis by Asset Liabilities Committee.

The Bank maintains a portfolio of highly marketable and diverse assets that can be easily liquidated in the event of an unforeseen interruption of cash flow. Additionally, the Bank maintains obligatory reserve

(Amounts expressed in thousands of Azerbaijani Manats)

23 Financial Risk Management (Continued)

with the CBAR and utilizes a highly effective cash management system across all its branches, ATMs and balances of the correspondent accounts.

The liquidity position is assessed and managed by the Bank primarily on a standalone basis, based on minimum liquidity ratio of 30% established by the CBAR. As at 31 December, these ratios were as follows:

	2019	2018
Instant Liquidity Ratio	48.25%	45.27%

Analysis of financial liabilities by remaining contractual maturities. The tables below summarize the maturity profile of the Bank's financial liabilities at 31 December based on contractual undiscounted repayment obligations. Repayments which are subjected to notice are treated as if notice were to be given immediately. However, the Bank expects that many customers will not request repayment on the earliest date the Bank could be required to pay and the table does not reflect the expected cash flows indicated by the Bank's deposit retention history.

As at 31 December 2019	Less than 3 months	3 to 12 months	1 to 5 years	Over 5 years	Total
Financial liabilities					
Amounts due to credit institutions	1,565	925	4,115	6,332	**12,937**
Amounts due to customers	295,234	17,756	9,060	10,948	**332,998**
Other financial liabilities	3,777	1,255	2,934	1,375	**9,341**
Total undiscounted financial liabilities	**300,576**	**19,936**	**16,109**	**18,655**	**355,276**

As at 31 December 2018	Less than 3 months	3 to 12 months	1 to 5 years	Over 5 years	Total
Financial liabilities					
Amounts due to credit institutions	550	210	3,677	5,441	**9,878**
Amounts due to customers	393,308	32,439	10,729	–	**436,476**
Other financial liabilities	3,179	–	–	–	**3,179**
Total undiscounted financial liabilities	**397,037**	**32,649**	**14,406**	**5,441**	**449,533**

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

	Less than 3 months	3 to 12 months	1 to 5 years	Over 5 years	Total
2019	11,485	12,633	38,817	35,389	**98,324**
2018	12,624	16,656	56,221	17,593	**103,094**

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

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

(Amounts expressed in thousands of Azerbaijani Manats)

23 Financial Risk Management (Continued)

The Bank does not receive any significant funds from any one organization or private individual.
Included in due to customers are term deposits of individuals. In accordance with the Azerbaijan legislation, the Bank is obliged to repay such deposits upon demand of a depositor. Refer to Note 17 .
The Bank does not use the above maturity analysis based on undiscounted contractual maturities of liabilities to manage liquidity. Instead, the Bank monitors expected maturities and the resulting expected liquidity gap as follows:
The maturity analysis of financial instruments at 31 December 2019 is as follows:

	Less than 3 months	3 to 12 months	1 to 5 years	Over 5 years	Total
At 31 December 2019					
Financial assets	310,825	69,037	37,084	6,515	423,461
Financial liabilities	300,578	19,307	13,897	16,219	350,001
Net liquidity gap based on expected maturities	**10,247**	**49,730**	**23,187**	**(9,704)**	**73,460**
At 31 December 2018					
Financial assets	289,787	78,809	45,382	4,498	418,476
Financial liabilities	293,881	32,011	11,281	8,326	345,499
Net liquidity gap based on expected maturities	**(4,094)**	**46,798**	**34,101**	**(3,828)**	**72,977**

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 and foreign exchanges. The Bank does not have any significant equity, corporate fixed income or derivatives holdings.

Interest rate risk Interest rate risk arises from the possibility that changes in interest rates will affect future cash flows or the fair values of financial instruments. As at 31 December 2019 and 2018, the Bank did not have any instruments with floating interest rates.

Currency risk is defined as the risk that the value of a financial instrument will fluctuate due to changes in foreign exchange rates. The Bank is exposed to the effects of fluctuations in the prevailing foreign currency exchange rates on its financial position and cash flows.

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

Currency	Increase in currency rate in % 2019	Effect on profit before tax 2019	Increase in currency rate in % 2018	Effect on profit before tax 2018
USD	0.00	-	0.00	-
EUR	0.92	(32)	5.06	40

Currency	Decrease in currency rate in % 2019	Effect on profit before tax 2019	Decrease in currency rate in % 2018	Effect on profit before tax 2018
USD	0.00	-	(0.01)	(1)
EUR	(4.90)	170	(5.86)	(47)

(Amounts expressed in thousands of Azerbaijani Manats)

23 Financial Risk Management (Continued)

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

24 Fair Values of Financial Instruments

	Date of valuation	Fair value measurement using: Quoted prices in active markets (Level 1)	Significant observable inputs (Level 2)	Significant unobservable inputs (Level 3)	Total
Assets for which fair values are disclosed					
Amounts due from credit institutions	31 December 2019	–	–	20,986	**20,986**
Loans to customers	31 December 2019	–	–	160,678	**160,678**
Notes issued by CBAR and other bonds	31 December 2019	36,476	–	60	**36,536**
Other financial assets	31 December 2019	–	–	2,865	**2,865**
Liabilities for which fair values are disclosed					
Amounts due to credit institutions	31 December 2019	–	–	10,051	**10,051**
Amounts due to customers	31 December 2019	–	–	330,609	**330,609**
Other financial liabilities	31 December 2019	–	–	9,341	**9,341**

	Date of valuation	Fair value measurement using: Quoted prices in active markets (Level 1)	Significant observable inputs (Level 2)	Significant unobservable inputs (Level 3)	Total
Assets for which fair values are disclosed					
Amounts due from credit institutions	31 December 2018	–	–	62,030	**62,030**
Loans to customers	31 December 2018	–	–	144,831	**144,831**
Notes issued by CBAR and other bonds issued	31 December 2018	45,166	-	60	**45,226**
Liabilities for which fair values are disclosed					
Amounts due to credit institutions	31 December 2018	–	–	7,270	**7,270**
Amounts due to customers	31 December 2018	–	–	335,050	**335,050**

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

(Amounts expressed in thousands of Azerbaijani Manats)

24 Fair Values of Financial Instruments (Continued)

2019	Carrying value	Fair value	Unrecognized gain/(loss)
Financial assets			
Cash and cash equivalents	202,396	202,396	-
Amounts due from credit institutions	20,986	20,986	-
Loans to customers	204,171	204,171	-
Other financial assets	2,865	2,865	-
Financial liabilities			
Amounts due to credit institutions	10,051	10,051	-
Amounts due to customers	330,609	330,609	-
Other financial liabilities	9,341	9,341	-

2018	Carrying value	Fair value	Unrecognized gain/(loss)
Financial assets			
Cash and cash equivalents	163,432	163,432	-
Amounts due from credit institutions	62,030	62,030	-
Loans to customers	191,385	191,385	-
Other financial assets	2,957	2,957	-
Financial liabilities			
Amounts due to credit institutions	7,270	7,270	-
Amounts due to customers	335,050	335,050	-
Other financial liabilities	3,179	3,179	-

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.

Financial assets and financial liabilities carried at amortized cost. Fair value of the quoted notes 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 credit institutions and other financial assets and liabilities is estimated by discounting future cash flows using rates currently available for debt on similar terms, credit risk and remaining maturities. Short term instruments are ignored for this working.

25 Related Party Disclosures

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

Related parties may enter into transactions which unrelated parties might not, and transactions between related parties may not be effected on the same terms, conditions and amounts as transactions between unrelated parties.

YKB and KFS directly and indirectly control and have significant influence over a significant number of entities. The Bank enters into banking transactions with these entities including but not limited to lending, deposit taking, cash.

(Amounts expressed in thousands of Azerbaijani Manats)

25 Related Party Disclosures (Continued)

The outstanding balances of related party transactions are as follows:

	2019		2018	
	Parent	Entities under common control	Parent	Entities under common control
Loans outstanding at 1 January, gross	-	**1,466**	-	**504**
Loans issued during the year	–	–	–	1,464
Loan repayments during the year	–	(1,464)	-	(504)
Other movements	–	(2)	–	2
Loans outstanding at 31 December, gross	-	-	-	**1,466**
Less: allowance for impairment at 31 December	–	-	-	(9)
Loans outstanding at 31 December, net	-	-	-	**1,457**
Deposits outstanding at 1 January, gross	**1,677**	**5,943**	–	–
Deposits placed during the year	1,620	–	103,627	5,780
Deposit repayments during the year	(3,297)	(5,780)	(102,290)	–
Other movements	1,294	(163)	418	163
Translation gain/loss	66	–	(78)	–
Deposits outstanding at 31 December, gross	**1,360**	-	**1,677**	**5,943**
Less: allowance for impairment at 31 December	(18)	–	(22)	–
Deposits outstanding at 31 December, net	**1,342**	-	**1,655**	**5,943**
Current accounts at 31 December	**1,360**	**186**	**1,681**	**6,229**

Total current accounts with the parent as at December 31,2019 is AZN 1,360 (2018: AZN 1,681). During the year AZN 1,620 (2018: AZN 103,627) of deposit placed with parent carrying 0.37% interest rate (2018: 0.32%) and no deposit was placed (2018: AZN 5,780) with entities under common control (2018: 3.25%).

The income and expense arising from related party transactions are as follows:

	2019		2018	
	Parent	Entities under common control	Parent	Entities under common control
Interest income	10	152	423	298
Interest expense	-	(31)	-	(36)
Fee and commission income	-	23	-	34
Fee and commission expense	(109)	(14)	(112)	(13)
General and administrative expenses	(225)	(373)	(78)	(623)

Compensation of key management personnel of 5 members (2018: 6 members) comprised the following:

	2019	2018
Salaries and short term benefits	1,413	1,331
Other accrued employee costs	110	100
Total key management personnel compensation	**1,523**	**1,431**

(Amounts expressed in thousands of Azerbaijani Manats)

26 Capital Adequacy

The objectives of management when managing the Bank's capital are (i) to comply with the capital requirements set by Regulatory, (ii) to safeguard the Bank's ability to continue as a going concern and (iii) to maintain strong credit ratings and healthy capital ratios in order to support its business and to maximize shareholders' value. Compliance with capital adequacy ratios set by the Regulatory is monitored monthly with reports outlining their calculation reviewed and signed by the Bank's Chief Executive Officer and Chief Accountant. The other objectives of capital management are evaluated annually.

The Bank manages its capital structure and makes adjustments to it in the light of changes in economic conditions and the risk characteristics of its activities. In order to maintain or adjust the capital structure, the Bank may adjust the amount of dividend payment to shareholders or return capital to shareholders. No changes were made in the objectives, policies and processes from the previous years.

The Regulatory requires each bank or banking group to: (a) hold the minimum level of total capital of AZN 50,000 (2018: AZN 50,000); (b) maintain a ratio of total regulatory capital to the risk-weighted assets (the "total capital ratio") at or above the prescribed minimum of 10% (2018: 10%) and (c) maintain a ratio of tier 1 capital to the risk-weighted assets (the "Tier 1 capital ratio") at or above the prescribed minimum of 5% (2018: 5%).

Management believes that the Bank was in compliance with the statutory capital adequacy ratio throughout 2019.

As at 31 December 2019, the Bank's capital adequacy ratio based on the Regulatory requirements was as follows:

	2019	**2018**
Tier 1 capital	74,992	69,605
Tier 2 capital	6,269	9,071
Less: deductions from capital	(8,475)	(8,449)
Total regulatory capital	**72,786**	**70,227**
Risk-weighted assets	220,850	294,648
Tier 1 capital adequacy ratio	30.15%	20.73%
Total capital adequacy ratio	32.96%	23.79%