JSC PASHA Bank Georgia

Interim Condensed Financial Statements

Together with Report on Review of Interim Condensed Financial Statements
30 June 2017

Contents

EY
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EY Georgia LLC
Kote Abkhazi Street, 44
Tbilisi, 0105, Georgia
Tel: +995 (32) 215 8811
Fax: +995 (32) 215 8822
www.ey.com/ge

შპს იუაი საქართველო
საქართველო, 0105 თბილისი
კოტე აფხაზის ქუჩა 44
ტელ: +995 (32) 215 8811
ფაქსი: +995 (32) 215 8822

Report on Review of Interim Condensed Financial Statements

To the Shareholders and Board of Directors of JSC PASHA Bank Georgia

We have reviewed the accompanying interim condensed financial statements of JSC PASHA Bank Georgia, which comprise the interim condensed statement of financial position as at 30 June 2017 and the related interim condensed statements of comprehensive income for the six month period then ended, interim condensed statements of changes in equity and of cash flows for the six month period then ended and selected explanatory notes.

Management is responsible for the preparation and presentation of these interim condensed financial statements in accordance with International Financial Reporting Standard IAS 34, "Interim Financial Reporting" ("IAS 34"). Our responsibility is to express a conclusion on these interim condensed financial statements based on our review.

Scope of Review

We conducted our review in accordance with International Standard on Review Engagements 2410, "Review of Interim Financial Information Performed by the Independent Auditor of the Entity".

A review of interim condensed financial statements consists of making inquiries, primarily of persons responsible for financial and accounting matters, and applying analytical and other review procedures. A review is substantially less in scope than an audit conducted in accordance with International Standards on Auditing and consequently does not enable us to obtain assurance that we would become aware of all significant matters that might be identified in an audit. Accordingly, we do not express an audit opinion.

Conclusion

Based on our review, nothing has come to our attention that causes us to believe that the accompanying interim condensed financial statements are not prepared, in all material respects, in accordance with IAS 34 Interim Financial Reporting.

Ruslan Khoroshvili
On behalf of EY Georgia LLC
Tbilisi, Georgia
22 August 2017

INTERIM CONDENSED STATEMENT OF FINANCIAL POSITION

As at 30 June 2017

(Figures in tables are in thousands of Georgian lari)

	Notes	*30 June 2017 (unaudited)*	*31 December 2016*
Assets			
Cash and cash equivalents	4	21,199	7,599
Amounts due from credit institutions	5	42,808	83,261
Loans to customers	6	116,982	95,090
Investment securities	7	61,982	91,880
Property and equipment	8	966	1,108
Intangible assets	9	2,092	2,060
Deferred income tax assets	13	610	924
Other assets	10	1,308	563
Total assets		**247,947**	**282,485**
Liabilities			
Amounts due to credit institutions	11	94,444	131,681
Amounts due to customers	12	46,912	46,024
Provisions for guarantees and letters of credit	15	85	85
Other liabilities	10	646	1,411
Total liabilities		**142,087**	**179,201**
Equity			
Share capital	14	103,000	103,000
Retained earnings / (accumulated deficit)		2,860	354
Other reserves		–	(70)
Total equity		**105,860**	**103,284**
Total equity and liabilities		**247,947**	**282,485**

Signed and authorised for release on behalf of the Board of Directors of the Bank:

Shahin Mammadov Chairman of the Board of Directors

Chingiz Abdullayev Chief Financial Officer,
Member of the Board of Directors

22 August 2017

The accompanying notes on pages 5 to 18 are an integral part of these interim condensed financial statements.

INTERIM CONDENSED STATEMENT OF COMPREHENSIVE INCOME

For the six months ended 30 June 2017

(Figures in tables are in thousands of Georgian lari)

	Notes	For the six months ended 30 June 2017 (unaudited)	For the six months ended 30 June 2016 (unaudited)
Interest income			
Loans to customers		5,851	6,353
Investment securities		2,991	4,639
Amounts due from credit institutions		1,021	632
		9,863	**11,624**
Interest expense			
Amounts due to credit institutions		(1,814)	(3,646)
Amounts due to customers		(440)	(351)
		(2,254)	**(3,997)**
Net interest income		**7,609**	**7,627**
(Provision)/reversal of provision for impairment losses on interest bearing assets	6, 7	(343)	24
Net interest income after impairment losses		**7,266**	**7,651**
Net gains from foreign currencies			
- dealing		582	288
- translation differences		272	8
Net fee and commission income	16	92	71
Other operating income		44	67
Non-interest income		**990**	**434**
Personnel expenses	17	(2,394)	(2,656)
General and administrative expenses	17	(2,115)	(1,923)
Depreciation and amortisation	8, 9	(924)	(957)
Non-interest expenses		**(5,433)**	**(5,536)**
Income before income tax expense		**2,823**	**2,549**
Income tax expense	13	(317)	(311)
Net income for the period		**2,506**	**2,238**
Other comprehensive income			
Other comprehensive income to be reclassified to profit or loss in subsequent periods			
Net unrealized gain on investment securities		67	197
Income tax effect on net gain/(loss) on investment securities available-for-sale	13	3	(7)
Total comprehensive income for the year		**2,576**	**2,428**

The accompanying notes on pages 5 to 18 are an integral part of these interim condensed financial statements.

INTERIM CONDENSED STATEMENT OF CHANGES IN EQUITY

For the six months ended 30 June 2017

(Figures in tables are in thousands of Georgian lari)

	Share capital	*Retained earnings*	*Other reserves*	*Total equity*
1 January 2016	**103,000**	**(4,527)**	**(292)**	**98,181**
Total comprehensive income for the six months ended 30 June 2016 (unaudited)	–	2,238	190	2,428
At 30 June 2016 (unaudited)	**103,000**	**(2,289)**	**(102)**	**100,609**
As at 1 January 2017	**103,000**	**354**	**(70)**	**103,284**
Profit for the six months ended 30 June 2017 (unaudited)	–	2,506	–	2,506
Other comprehensive income for the six months ended 30 June 2017 (unaudited)	–	–	70	70
Total comprehensive income for the six months ended 30 June 2017 (unaudited)	**–**	**2,506**	**70**	**2,576**
At 30 June 2017 (unaudited)	**103,000**	**2,860**	**–**	**105,860**

The accompanying notes on pages 5 to 18 are an integral part of these interim condensed financial statements.

INTERIM CONDENSED STATEMENT OF CASH FLOWS

For the six months ended 30 June 2017

(Figures in tables are in thousands of Georgian lari)

	Notes	For the six months ended 30 June 2017 (unaudited)	For the six months ended 30 June 2016 (unaudited)
Cash flows from operating activities			
Interest received		10,453	13,044
Interest paid		(2,431)	(4,183)
Fees and commissions received		307	269
Fees and commissions paid		(205)	(171)
Realised gains less losses from dealing in foreign currencies		582	288
Personnel expenses paid		(3,044)	(2,804)
General and administrative expenses paid		(2,872)	(1,998)
Other income received		44	67
Cash flows from operating activities before changes in operating assets and liabilities		**2,834**	**4,512**
Net (increase)/decrease in operating assets			
Amounts due from credit institutions		35,662	(18,636)
Loans to customers		(25,097)	6,022
Net increase/(decrease) in operating liabilities			
Amounts due to credit institutions		(28,585)	(17,669)
Amounts due to customers		3,983	25,777
Net cash (used in)/from operating activities		**(11,203)**	**6**
Cash flows from investing activities			
Purchase of investment securities		(40,071)	(33,017)
Proceeds from redemption of investment securities		66,967	59,628
Purchase of property and equipment		(732)	(120)
Purchase of intangible assets		(210)	(97)
Net cash from investing activities		**25,954**	**26,394**
Effect of exchange rates changes on cash and cash equivalents		(1,151)	1,606
Net increase in cash and cash equivalents		**13,600**	**28,006**
Cash and cash equivalents, beginning	4	7,599	22,282
Cash and cash equivalents, ending	4	**21,199**	**50,288**

The accompanying notes on pages 5 to 18 are an integral part of these interim condensed financial statements.

(Figures in tables are in thousands of Georgian lari)

1. Principal activities

JSC PASHA Bank Georgia (the "Bank") was formed on 17 December 2012 as a joint stock company under the laws of Georgia. The Bank operates under a general banking license issued by the National Bank of Georgia (the "NBG") on 17 January 2013.

The Bank accepts deposits and extends credit, transfers payments in Georgia and abroad, exchanges currencies and provides other banking services to its commercial customers. The Bank has one service office in Georgia as of 30 June 2017. The Bank's registered legal address is 15 Rustaveli Avenue, Tbilisi, 0108, Georgia.

As at 30 June 2017 and 31 December 2016, the Bank's 100% owner was OJSC PASHA Bank (the "Parent"), domiciled in the Republic of Azerbaijan. The Bank is ultimately owned by Mrs. Leyla Aliyeva and Mrs. Arzu Aliyeva, who exercise joint control over the Bank.

These interim condensed financial statements have not yet been approved by the Parent on the General Meeting of Shareholders of the Bank. The shareholders have the power and authority to amend the financial statements after the issuance.

2. Basis of preparation

These interim condensed financial statements for the six months ended 30 June 2017, have been prepared in accordance with International Accounting Standard ("IAS") 34 *Interim Financial Reporting*.

The Bank is required to maintain its records and prepare its financial statements for regulatory purposes in Georgian lari in accordance with International Financial Reporting Standards ("IFRS"). The interim condensed financial statements do not include all the information and disclosures required in the annual financial statements, and should be read in conjunction with the Bank's annual financial statements as at 31 December 2016. These interim condensed financial statements are prepared under the historical cost convention.

These interim condensed financial statements are presented in thousand of Georgian lari ("GEL") unless otherwise indicated.

3. Changes in accounting policies

The accounting policies adopted in the preparation of the interim condensed financial statements are consistent with those followed in the preparation of the Bank's annual financial statements for the year ended 31 December 2016, except for the adoption of new Standards effective as of 1 January 2017. The Bank has not early adopted any other standard, interpretation or amendment that has been issued but is not yet effective.

The nature and the effect of these changes are disclosed below. Although these new standards and amendments apply for the first time in 2017, they do not have a material effect on the annual statements of the Bank or the interim condensed financial statements of the Bank. The nature and the impact of each new standard or amendment are described below:

Amendments to IAS 7 Statement of Cash Flows: Disclosure Initiative

The amendments require entities to provide disclosures about changes in their liabilities arising from financing activities, including both changes arising from cash flows and non-cash changes (such as foreign exchange gains or losses). On initial application of the amendment, entities are not required to provide comparative information for preceding periods. The Bank is not required to provide additional disclosures in its condensed interim financial statements, but will disclose additional information in its annual financial statements for the year ended 31 December 2017.

Amendments to IAS 12 Income Taxes: Recognition of Deferred Tax Assets for Unrealised Losses

The amendments clarify that an entity needs to consider whether tax law restricts the sources of taxable profits against which it may make deductions on the reversal of that deductible temporary difference. Furthermore, the amendments provide guidance on how an entity should determine future taxable profits and explain the circumstances in which taxable profit may include the recovery of some assets for more than their carrying amount.

Entities are required to apply the amendments retrospectively. However, on initial application of the amendments, the change in the opening equity of the earliest comparative period may be recognised in opening retained earnings (or in another component of equity, as appropriate), without allocating the change between opening retained earnings and other components of equity. Entities applying this relief must disclose that fact.

The Bank applied the amendments retrospectively. However, their application has no effect on the Bank's financial position and performance.

(Figures in tables are in thousands of Georgian lari)

4. Cash and cash equivalents

Cash and cash equivalents comprise:

	30 June 2017 (unaudited)	*31 December 2016*
Cash on hand	632	656
Current accounts with the NBG	202	665
Current accounts with credit institutions	8,936	3,778
Time deposits with credit institutions up to 90 days	11,429	2,500
Cash and cash equivalents	**21,199**	**7,599**

As at 30 June 2017, current accounts and time deposit accounts with credit institutions denominated in USD and EUR represent 13.31% and 39.71% of total current and time deposit accounts respectively (31 December 2016: USD 14.31%, EUR 31.62%).

The outstanding balance of current accounts and time deposit accounts, consist of interest bearing correspondent account balances with credit institutions in the amount of GEL 19,667 thousand (31 December 2016: GEL 2,947 thousand) and non-interest bearing correspondent account balances with credit institution in the amounts of GEL 698 thousand (31 December 2016: GEL 3,331 thousand).

5. Amounts due from credit institutions

Amounts due from credit institutions comprise:

	30 June 2017 (unaudited)	*31 December 2016*
Time deposits for more than 90 days	26,683	52,576
Mandatory reserve with the NBG	16,125	30,685
Amounts due from credit institutions	**42,808**	**83,261**

Time deposits comprise of deposits in USD and GEL placed with resident and non-resident commercial banks with maturities ranging from July 2017 to June 2018 and interest rates of 7.0%-9.0% on GEL deposits and 0.5%-4.5% on USD deposits (31 December 2016: deposits in USD and GEL placed with resident and non-resident commercial banks with maturities ranging from February 2017 to December 2017 and interest rates of 4.0%-5.5% on GEL deposits and 6.5%-7.2% on USD deposits).

Credit institutions are required to maintain a mandatory interest earning cash deposit with the NBG at the level of 7% and 20% of the average of funds attracted from customers by a credit institution for the appropriate two-week period in GEL and foreign currencies, respectively, since June 2016 (31 December 2016: 7% and 20% respectively).

6. Loans to customers

Loans to customers comprise:

	30 June 2017 (unaudited)	*31 December 2016*
Private entities	82,267	66,767
Foreign state controlled entities	36,643	30,129
Individuals	603	314
Loans to customers	**119,513**	**97,210**
Less – allowance for impairment	(2,531)	(2,120)
Loans to customers	**116,982**	**95,090**

(Figures in tables are in thousands of Georgian lari)

6. Loans to customers (continued)

The movement in allowance for impairment losses for loans to customers was as follows:

	For the six months ended 30 June 2017 (unaudited)		
	Legal entities	*Individuals*	*Total*
At 1 January 2017	**(2,049)**	**(71)**	**(2,120)**
Charge for the period (unaudited)	(401)	(10)	(411)
At 30 June 2017 (unaudited)	**(2,450)**	**(81)**	**(2,531)**
Collective impairment (unaudited)	(1,269)	(11)	(1,280)
Individual impairment (unaudited)	(1,181)	(70)	(1,251)
Gross amount of loans, individually determined to be impaired, before deducting any individually assessed impairment allowance	(8,402)	(70)	(8,472)

	For the six months ended 30 June 2016 (unaudited)		
	Legal entities	*Individuals*	*Total*
At 1 January 2016	**(1,253)**	**(58)**	**(1,311)**
Reversal/(charge) for the period (unaudited)	30	(6)	24
At 30 June 2016 (unaudited)	**(1,223)**	**(64)**	**(1,287)**
Collective impairment (unaudited)	(1,223)	(64)	(1,287)

As at 30 June 2017, the Bank had a concentration of loans due from three major group of borrowers with the total exposure of GEL 64,807 thousand that represented 54.23% of the total gross loan portfolio (31 December 2016: GEL 53,847 thousand with 55.39% of the gross loan portfolio). An allowance of GEL 516 thousand (2016: GEL 467 thousand) was recognized against these loans.

Loans are made in the following industry sectors:

	30 June2017 (unaudited)	*31 December 2016*
Trade and services	44,469	48,881
Energy	41,325	14,929
Non-banking credit organizations	12,164	20,664
Transport and telecommunications	9,834	-
Construction	8,738	8,778
Mining	2,380	3,644
Individuals	603	314
	119,513	**97,210**

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 charges over real estate properties and guarantees from the Parent. The Bank also obtains guarantees from parent companies for loans to their subsidiaries.

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

(Figures in tables are in thousands of Georgian lari)

7. Investment securities

As at 30 June 2017, investment securities mainly comprised of debt securities of the Ministry of Finance of Georgia, debt securities of companies and commercial banks registered in Georgia and Azerbaijan.

Investment securities comprise:

	30 June2017 (unaudited)	*31 December 2016*
Certificates of deposits of financial institutions	24,379	26,543
Bonds of financial institutions	21,445	21,541
Corporate bonds	8,946	12,969
Treasury bonds of the Ministry of Finance of Georgia	7,345	31,028
Investment securities: loans and receivables	**62,115**	**92,081**
Less: allowance for impairment (a)	(133)	(201)
Total investment securities: loans and receivables	**61,982**	**91,880**

(a) The allowance for the impairment relates to the collectively impaired exposures of corporate bonds.

The movement in allowance for the period is attributed to reversal of the provision of GEL 68 thousand.

8. Property and equipment

The movements in property and equipment were as follows:

	Furniture and fixtures	*Computers and equipment*	*Motor vehicles*	*Other equipment*	*Leasehold improve-ments*	*Total*
Cost						
31 December 2015	**1,840**	**2,390**	**247**	**459**	**1,912**	**6,848**
Additions (unaudited)	1	31	66	22	-	120
30 June 2016 (unaudited)	**1,841**	**2,421**	**313**	**481**	**1,912**	**6,968**
31 December 2016	**1,843**	**2,412**	**313**	**486**	**1,912**	**6,966**
Additions (unaudited)	6	588	-	4	-	598
30 June 2017 (unaudited)	**1,849**	**3,000**	**313**	**490**	**1,912**	**7,564**
Accumulated depreciation						
31 December 2015	**(1,173)**	**(1,447)**	**(108)**	**(232)**	**(1,199)**	**(4,159)**
Depreciation charge (unaudited)	(229)	(304)	(37)	(47)	(229)	(846)
30 June 2016 (unaudited)	**(1,402)**	**(1,751)**	**(145)**	**(279)**	**(1,428)**	**(5,005)**
31 December 2016	**(1,634)**	**(2,052)**	**(185)**	**(327)**	**(1,660)**	**(5,858)**
Depreciation charge (unaudited)	(182)	(249)	(33)	(48)	(228)	(740)
30 June 2017 (unaudited)	**(1,816)**	**(2,301)**	**(218)**	**(375)**	**(1,888)**	**(6,598)**
Net book value						
30 June 2016 (unaudited)	439	670	168	202	484	1,963
31 December 2016	209	360	128	159	252	1,108
30 June 2017 (unaudited)	33	699	95	115	24	966

(Figures in tables are in thousands of Georgian lari)

9. Intangible assets

The movements in intangible assets were as follows:

	Licenses	*Computer software*	*Total*
Cost			
31 December 2015	**488**	**1,829**	**2,317**
Additions (unaudited)	23	8	31
Disposals (unaudited)	(12)	(6)	(18)
30 June 2016 (unaudited)	**499**	**1,831**	**2,330**
31 December 2016	**897**	**1,829**	**2,726**
Additions (unaudited)	217	–	217
Write-off (unaudited)	(190)	(1)	(191)
30 June 2017 (unaudited)	**924**	**1,828**	**2,752**
Accumulated amortization			
31 December 2015	**(108)**	**(185)**	**(293)**
Amortization charge (unaudited)	(46)	(65)	(111)
Disposals (unaudited)	12	5	17
30 June 2016 (unaudited)	**(142)**	**(245)**	**(387)**
31 December 2016	**(308)**	**(358)**	**(666)**
Amortization charge (unaudited)	(95)	(89)	(184)
Write-off (unaudited)	190	–	190
30 June 2017 (unaudited)	**(213)**	**(447)**	**(660)**
Net book value			
30 June 2016 (unaudited)	**357**	**1,586**	**1,943**
31 December 2016	**589**	**1,471**	**2,060**
30 June 2017 (unaudited)	**711**	**1,381**	**2,092**

10. Other assets and liabilities

Other assets comprise:

	30 June 2017 (unaudited)	*31 December 2016*
Other non-financial assets		
Prepaid expenses	825	365
Prepayments for operating lease	214	170
Prepayments for acquisition of property and equipment and intangible assets	188	4
Prepaid taxes other than on income tax	59	16
Other	22	8
Other assets	**1,308**	**563**

Other liabilities comprise:

	30 June 2017 (unaudited)	*31 December 2016*
Other financial liabilities		
Other financial liabilities	86	223
	86	**223**
Other non-financial liabilities		
Payable to employees	500	1,150
Deferred income	59	38
Taxes other than income tax	1	–
	560	**1,188**
Other liabilities	**646**	**1,411**

(Figures in tables are in thousands of Georgian lari)

11. Amounts due to credit institutions

Amounts due to credit institutions comprise:

	30 June 2017 (unaudited)	*31 December 2016*
Time deposits of the Parent	39,856	37,617
Time deposits of non-resident commercial banks	27,951	39,956
Time deposits of resident commercial banks	17,002	14,478
Overdraft from the Parent	3,554	3,003
Current accounts of the Parent	3,072	8,597
Short-term loan from the NBG	3,009	28,030
Amounts due to credit institutions	**94,444**	**131,681**

The deposits placed by resident commercial banks denominated in GEL, USD, EUR and a single non-resident commercial bank, denominated in USD and EUR, outstanding as at 30 June 2017, matured in July 2017.

The loan from the NBG outstanding as at 30 June 2017 was obtained on 15 June 2017 and matured in July 2017.

As at 30 June 2017, time deposits placed by the Parent are denominated in USD (31 December 2016: USD) and mature during 2018.

12. Amounts due to customers

The amounts due to customers include the following:

	30 June 2017 (unaudited)	*31 December 2016*
Time deposits	32,566	33,492
Current accounts	14,346	12,532
Amounts due to customers	**46,912**	**46,024**
Held as security against guarantees (Note 15)	624	757

As at 30 June 2017, amounts due to customers included balances with three major customers of GEL 28,682 thousand that constituted 61.14% of the total customer accounts (31 December 2016: GEL 27,561 thousand that constituted 59.88% the total of customer accounts).

13. Taxation

The corporate income tax expense for the six months ended 30 June 2017 comprises of deferred tax expense of GEL 317 thousand (six months ended 30 June 2016: GEL 311 thousand).

The income tax rate applicable to the Bank's income is 15%. The effective income tax rate differs from the statutory income tax rate. A reconciliation of the income tax expense on statutory rates with actual is as follows:

	Six months ended 30 June 2017 (unaudited)	*Six months ended 30 June 2016 (unaudited)*
Profit before income tax	**2,823**	**2,549**
Statutory tax rate	15%	15%
Theoretical income tax charge at the statutory rate	**(423)**	**(382)**
Tax effect of items which are not deductible for taxation purposes		
Non-deductible expenses	(42)	(3)
Tax exempt income	148	74
Income tax expense	**(317)**	**(311)**

(Figures in tables are in thousands of Georgian lari)

13. Taxation (continued)

Deferred tax assets and liabilities as at 30 June 2017 and 31 December 2016 and their movements for the respective period of six months comprise:

	31 December 2016	*Through statement of profit and loss (unaudited)*	*Through statement of OCI (unaudited)*	*30 June 2017 (unaudited)*
Tax effect of deductible temporary differences				
Tax losses carried forward	804	(224)	–	580
Property and equipment	–	46	–	46
Loans to customers	–	11	–	11
Other liabilities	135	33	–	168
Investment securities	(17)	10	–	(7)
Deferred tax asset	**922**	**(124)**	**–**	**798**
Tax effect of taxable temporary differences				
Property and equipment	226	(1)	–	225
Intangible assets	(52)	(5)	–	(57)
Loans to customers	(177)	(57)	–	(234)
Other liabilities	–	(114)	–	(114)
Investment securities	5	(16)	3	(8)
Deferred tax liability	**2**	**(193)**	**3**	**(188)**
Deferred tax asset	**924**	**(317)**	**3**	**610**

	31 December 2015	*Through statement of profit and loss (unaudited)*	*Through statement of OCI (unaudited)*	*30 June 2016 (unaudited)*
Tax effect of deductible temporary differences				
Tax losses carried forward	1,818	(624)	–	1,194
Property and equipment	73	76	–	149
Other liabilities	68	19	–	87
Investment securities	6	10	(7)	9
Deferred tax asset	**1,965**	**(519)**	**(7)**	**1,439**
Tax effect of taxable temporary differences				
Intangible assets	(49)	(7)	–	(56)
Loans to customers	(394)	215	–	(179)
Deferred tax liability	**(443)**	**208**	**–**	**(235)**
Deferred tax liability	**1,522**	**(311)**	**(7)**	**1,204**

In June 2016, amendments to the Georgian tax law in respect of corporate income tax became enacted. The amendments become effective from 1 January 2017 for all Georgian companies except the banks, insurance companies and microfinance organization, for which the effective date is 1 January 2019. Under the new regulation, corporate income tax will be levied on profit distributed as dividends, rather than on profit earned as under the current regulation. The amount of tax payable on a dividend distribution will be calculated as 15/85 of the amount of net distribution. The companies will be able to offset corporate income tax liability arising from dividend distributions out of profits earned in 2008-2016 by the amount of corporate income tax paid for the respective period under the current regulation. Dividends distributions between Georgian resident companies will not be subject to corporate income tax.

Following the enactment of the amendments, as at 30 June 2017 the Bank premeasured its deferred tax assets and liabilities at the tax rates that were expected to apply to the period when the asset is realised or the liability is settled. As IAS 12 *Income Taxes* requires, the Bank used 0% tax rate applicable for undistributed profits in respect of assets and liabilities expected to be realized or settled in the periods when the new regulation becomes effective starting from 1 January 2019.

(Figures in tables are in thousands of Georgian lari)

13. Taxation (continued)

The amendments to the Georgian tax law described above also provide for charging corporate income tax on certain transactions that are considered deemed profit distributions, e.g. some transactions at non-market prices, non-business related expenses or supply of goods and services free of charge. Taxation of such transaction is outside scope of IAS 12 *Income Taxes* and will be accounted similar to operating taxes starting from 1 January 2019. Tax law amendments related to such deemed profit distribution did not have any effect on the Bank's condensed financial statements for the period ended 30 June 2017.

14. Equity

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

As at 30 June 2017 and 31 December 2016, the Bank's authorized, issued and fully paid capital amounted to GEL 103,000 thousand comprising of 103,000,000 common shares with nominal value of GEL 1.00. Each common share entitles one vote to the shareholder.

In accordance with the Georgian legislation, dividends may only be declared by the Bank's Parent from the net income as shown in the Bank's financial statements prepared in compliance with the NBG requirements. The disbursement of the dividends needs pre-approval of the NBG.

No dividends were declared or paid during the six months ended 30 June 2017 (2016: nil).

15. Commitments and contingencies

Taxation

Georgian tax 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 tax authorities. 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. Under certain circumstances reviews may cover longer periods.

Management believes that its interpretation of the relevant legislation as at 30 June 2017 is appropriate and that the Bank's tax, currency and customs positions will be sustained.

Commitments and contingencies

As at 30 June 2017, the Bank's commitments and contingencies comprised the following:

	30 June 2017 (unaudited)	*31 December 2016*
Credit related commitments		
Guarantees issued	17,284	13,026
Letters of credit	1,373	318
Unused credit lines	924	5,230
	19,581	**18,574**
Operating lease commitments		
Not later than 1 year	1,626	1,723
More than 1 year but less than 5 years	7,193	8,016
Contingency over 5 years	–	868
	8,819	**10,607**
Less: provisions for guarantees and letters of credit	(85)	(85)
Commitments and contingencies (before deducting collateral)	**28,315**	**29,096**
Less: deposits held as security against guarantees issued (Note 12)	(624)	(757)
Commitments and contingencies	**27,691**	**28,339**

(Figures in tables are in thousands of Georgian lari)

16. Net fee and commission income

Net fee and commission income comprise:

	Six months ended 30 June 2017 (unaudited)	*Six months ended 30 June 2016 (unaudited)*
Guarantees and letters of credits issued	195	156
Settlements operations	54	57
Brokerage operations	24	24
Cash operations	9	3
Currency conversion operations	4	–
Plastic cards	3	–
Fee and commission income	**289**	**240**
Settlements operations	(92)	(78)
Guarantees and letters of credit issued	(61)	(53)
Plastic cards	(43)	(29)
Cash operations	(1)	(9)
Fee and commission expense	**(197)**	**(169)**
Net fee and commission income	**92**	**71**

17. Personnel, general and administrative expenses

Personnel, general and administrative expenses comprise:

	Six months ended 30 June 2017 (unaudited)	*Six months ended 30 June 2016 (unaudited)*
Salaries	1,801	1,879
Bonuses and other employee benefits	593	777
Personnel expenses	**2,394**	**2,656**
Operating leases	808	733
Professional services	734	534
Advertising costs	228	221
Personnel trainings	80	84
Utilities	57	54
Insurance	36	40
Security expenses	29	29
Corporate hospitality and entertainment	29	26
Transportation and business trip expenses	28	34
Membership fees	19	17
Maintenance and exploitation	14	41
Charity costs	9	11
Other	44	99
General and administrative expenses	**2,115**	**1,923**

18. Fair values of financial instruments

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

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

(Figures in tables are in thousands of Georgian lari)

18. Fair values of financial instruments (continued)

The following table shows an analysis of financial instruments recorded at fair value by level of the fair value hierarchy:

	Fair value measurement using			
At 30 June 2017	***Level 1 (unaudited)***	***Level 2 (unaudited)***	***Level 3 (unaudited)***	***Total (unaudited)***
Assets for which fair values are disclosed				
Cash and cash equivalents	21,199	–	–	**21,199**
Amounts due from credit institutions	–	–	42,808	**42,808**
Loans to customers	–	–	116,982	**116,982**
Investment securities	–	2,920	59,062	**61,982**

	Fair value measurement using			
At 30 June 2017	***Level 1 (unaudited)***	***Level 2 (unaudited)***	***Level 3 (unaudited)***	***Total (unaudited)***
Liabilities for which fair values are disclosed				
Amounts due to credit institutions	–	–	94,444	**94,444**
Amounts due to customers	–	–	46,912	**46,912**

	Fair value measurement using			
At 31 December 2016	***Level 1***	***Level 2***	***Level 3***	***Total***
Assets for which fair values are disclosed				
Cash and cash equivalents	7,599	–	–	**7,599**
Amounts due from credit institutions	–	–	83,261	**83,261**
Loans to customers	–	–	95,090	**95,090**
Investment securities	–	3,020	88,860	**91,880**

	Fair value measurement using			
At 31 December 2016	***Level 1***	***Level 2***	***Level 3***	***Total***
Liabilities for which fair values are disclosed				
Amounts due to credit institutions	–	–	131,681	**131,681**
Amounts due to customers	–	–	46,024	**46,024**

Valuation techniques and assumptions

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

Assets for which fair value approximates carrying value

For financial assets and financial liabilities that are liquid or having a short term maturity (less than three months) it is assumed that the carrying amounts approximate to their fair value. All of the Bank's financial assets excluding loans to customers (i.e. cash and cash equivalents and amounts due from credit institutions) and financial liabilities (amounts due to customers) are either liquid or are maturing within 3 months from the reporting date.

The majority of loans to customers outstanding as at 30 June 2017 were issued in 2016 year at market interest rates, while the market interest rates as at 30 June 2017 approximate market interest rates prevailing during 2016. Hence their carrying value approximates their fair value.

Investment securities

As at 30 June 2017 investment securities represent fixed and floating rated financial assets carried at amortized cost. The fair value for investment securities loans and receivables is derived by discounting the future cash flows using current market rates for newly issued similar financial assets.

(Figures in tables are in thousands of Georgian lari)

18. Fair values of financial instruments (continued)

Amounts due to customers

As at 30 June 2017 amounts due to customers represent fixed rate financial liabilities carried at amortized cost. The fair value for the amounts due to customers is derived by disclosing future cash flows using broad industry average rates for similar financial liabilities.

Fair value of financial assets and liabilities not carried at fair value

	30 June 2017 (unaudited)			*31 December 2016*		
	Carrying value	*Fair value*	*Unrecognised gain/(loss)*	*Carrying value*	*Fair value*	*Unrecognised gain/(loss)*
Financial assets						
Cash and cash equivalents	21,199	21,199	-	7,599	7,599	-
Amounts due from credit institutions	42,808	42,808	-	83,261	83,261	-
Loans to customers	116,982	116,982	-	95,090	95,090	-
Investments securities	61,982	64,599	2,617	91,880	94,704	2,824
Financial liabilities						
Amounts due to credit institutions	94,444	94,444	-	131,681	131,681	-
Amounts due to customers	46,912	46,912	-	46,024	46,024	-
Total unrecognized change in fair value			**2,617**			**2,824**

19. Related party disclosures

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

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

The outstanding balances of related party transactions are as follows:

	30 June 2017 (unaudited)			*31 December 2016*		
	The Parent	*Key management personnel*	*Entities under common control*	*The Parent*	*Key management personnel*	*Entities under common control*
Cash and cash equivalents	7,575	-	-	2,435	-	-
Amounts due from credit institutions	-	-	5,024	-	-	5,025
Loans to customers	-	182	-	-	-	-
Purchase of property plant and equipment	-	-	-	21	-	-
Amounts due to credit institutions	(46,482)	-	(27,951)	(49,218)	-	(39,956)
Amounts due to customers	-	(6,132)	(23,092)	-	(7,259)	(23,027)
Other liabilities	(6)	-	(1)	(2)	-	-

(Figures in tables are in thousands of Georgian lari)

19. Related party disclosures (continued)

Income and expense arising from related party transactions are as follows:

	For the six months ended	
	30 June 2017 (unaudited)	*30 June 2016 (unaudited)*
Fee and commission income	–	47
Interest income	187	47
Fee and commission expense	79	44
Interest expense	1,224	1,065
Professional fees expense	–	21

Compensation of key management personnel was comprised of the following:

	For the six months ended	
	30 June 2017 (unaudited)	*30 June 2016 (unaudited)*
Salaries and other short-term benefits	889	592

Key management personnel as at 30 June 2017 comprised of 5 members of the Supervisory Board (31 December 2016: 4 members) and 3 members of the Board of Directors of the Bank (31 December 2016: 3 members).

20. Capital adequacy

The Bank maintains an actively managed capital base to cover risks inherent in the business. The adequacy of the Bank's capital is monitored using, among other measures, the ratios established by the NBG.

The primary objectives of the Bank's capital management are (i) to ensure that the Bank complies with externally imposed capital requirements set by the NBG, (ii) to safeguard the Bank's ability to continue as a going concern and (iii) to maintain sufficient capital base to achieve a capital adequacy ratio of at least 9.6% (2016: 10.80%). Compliance with capital adequacy ratios set by the NBG is monitored monthly with reports outlining their calculation reviewed and signed by the Bank's Chairman of Board of Directors and Chief Accountant subsequently submitted to the NBG.

NBG capital adequacy ratio

The NBG requires banks to maintain a capital adequacy ratio of 9.6% (2016: 10.80%) of risk-weighted assets and Tier 1 Capital adequacy ratio of 6.4% (2016: 7.2%). As at 30 June 2017, the Bank's capital adequacy ratios on this basis were as follows:

	Notes	*30 June 2017 (unaudited)*	*Adjustments (unaudited)*	*30 June 2017 per the NBG (unaudited)*
Share capital	14	103,000	–	103,000
Retained earnings/(accumulated deficit)		354	(2,149)	(1,795)
Less: intangible assets, net	9	(2,092)	–	(2,092)
Other adjustments		–	(3,611)	(3,611)
Main capital		**101,262**	**(5,760)**	**95,502**
Current period income		2,823	(374)	2,449
General reserves		2,682	48	2,730
Additional capital		**5,505**	**(326)**	**5,179**
Total capital		**106,767**	**(6,086)**	**100,681**
Risk weighted assets				**241,480**
Capital adequacy ratio				41.69%
Tier 1 Capital adequacy ratio				39.55%

(Figures in tables are in thousands of Georgian lari)

20. Capital adequacy (continued)

NBG capital adequacy ratio (continued)

	Notes	*31 December 2016*	*Adjustments*	*31 December 2016 per the NBG*
Share capital	14	103,000	-	103,000
Accumulated deficit		(4,527)	(4,632)	(9,159)
Less: Intangible assets, net	9	(2,060)	-	(2,060)
Main capital		**96,413**	**(4,632)**	**91,781**
Prior year income		4,881	2,483	7,364
General reserves		2,406	(356)	2,050
Additional capital		**7,287**	**2,127**	**9,414**
Total capital		**103,700**	**(2,505)**	**101,195**
Risk weighted assets				**218,136**
Capital adequacy ratio				46.39%
Tier 1 Capital adequacy ratio				42.08%

Regulatory capital consists of main capital, which comprises share capital and retained earnings including current year profit. Certain adjustments are made to IFRS-based results and reserves, as prescribed by the NBG. The other component of regulatory capital is Additional capital, which includes subordinated debt and revaluation reserve.

Basel II capital adequacy ratio

Starting from 30 June 2014 the NBG requires that all banks comply with Basel II regulations in their capital adequacy assessment. This implies the minimum ratio of 10.50% for total regulatory capital coefficient, minimum 7.00% of the core Tier 1 capital coefficient and minimum 8.50% for Tier 1 capital coefficient. As at 30 June 2017 and 31 December 2016, the Bank's capital adequacy ratios on the Basel II basis were as follows:

	Notes	*30 June 2017 (unaudited)*	*Adjustments (unaudited)*	*30 June 2017 per the NBG (unaudited)*
Share capital	14	103,000	-	103,000
Retained earnings / (accumulated deficit)		354	(2,149)	(1,795)
Less: intangible assets, net	9	(2,092)	-	(2,092)
Other adjustments		-	(3,611)	(3,611)
Current period income		2,823	(374)	2,449
Core tier 1 capital		**104,085**	**(6,134)**	**97,951**
Tier 1 capital		**104,085**	**(6,134)**	**97,951**
Supplementary capital		2,682	48	2,730
Total regulatory capital		**106,767**	**(6,086)**	**100,681**
Risk weighted assets				**293,837**
Capital adequacy ratio				34.26%
Core Tier 1 capital/Tier 1 capital adequacy ratio				33.34%

(Figures in tables are in thousands of Georgian lari)

20. Capital adequacy (continued)

Basel II capital adequacy ratio (continued)

	Notes	*31 December 2016*	*Adjustments*	*31 December 2016 per the NBG*
Additional tier 1 capital	14	103,000	–	103,000
Accumulated deficit		(4,527)	(4,632)	(9,159)
Less: intangible assets, net	9	(2,060)	–	(2,060)
Prior year income		4,881	2,483	7,364
Core tier 1 capital		**101,294**	**(2,149)**	**99,145**
Tier 1 capital		**101,294**	**(2,149)**	**99,145**
Supplementary capital		2,406	(356)	2,050
Total regulatory capital		**103,700**	**(2,505)**	**101,195**
Risk weighted assets				**296,917**
Capital adequacy ratio				34.08%
Core Tier 1 capital/Tier 1 capital adequacy ratio				33.39%