Consolidated financial statements

OJSC Xalq Bank and its subsidiaries

for the year ended 31 December 2018

with independent auditor's report

Open Joint Stock Company Xalq Bank

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Statement of Management's Responsibilities for the Preparation and Approval of the Consolidated Financial Statements for the Year Ended 31 December 2018

The following statement, which should be read in conjunction with the independent auditor's responsibilities stated in the independent auditor's report set out on pages 2 - 4, is made with a view to distinguishing the respective responsibilities of management and those of the independent auditors in relation to the consolidated financial statements of Open Joint Stock Company Xalq Bank (the "Group").

Management is responsible for the preparation of the consolidated financial statements that present fairly the financial position of the Group at 31 December 2018, and the results of its operations, cash flows and changes in equity for the year then ended, in accordance with International Financial Reporting Standards ("IFRS").

In preparing the consolidated financial statements, management is responsible for:

- Selecting suitable accounting principles and applying them consistently;
- Making judgments and estimates that are reasonable and prudent;
- Stating whether IFRS have been followed, subject to any material departures disclosed and explained in the consolidated financial statements; and
- Preparing the consolidated financial statements on a going concern basis, unless it is inappropriate to presume that the Group will continue in business for the foreseeable future.

Management is also responsible for:

- Designing, implementing and maintaining an effective and sound system of internal controls, throughout the Group;
- Maintaining proper accounting records that disclose, with reasonable accuracy at any time, the financial position of the Group, and which enable them to ensure that the consolidated financial statements of the Group comply with IFRS;
- Maintaining statutory accounting records in compliance with legislation of the Republic of Azerbaijan;
- Taking such steps as are reasonably available to them to safeguard the assets of the Group; and
- Detecting and preventing fraud and other irregularities.

The consolidated financial statements for the year ended 31 December 2018 were authorized for issue on 25 April 2019 by the Management Board.

Approved for issue and signed on behalf of the Management Board on 25 April 2019.

Chairman
Mr. Elkhan Aghayev

AZƏRBAYCAN RESPUBLİKASI AÇIQ SƏHMDAR CƏMİYYƏTİ "XALQ" BANKI
Xalq Bank
XALQ BANK OPEN JOINT-STOCK COMPANY AZERBAIJAN REPUBLIC

Chief Accountant
Mrs. Tamilla Asadova

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Independent auditor's report

To the Shareholders and Board of Directors of Open Joint Stock Company "Xalq Bank"

Report on the audit of the consolidated financial statements

Opinion

We have audited the consolidated financial statements of OJSC Xalq Bank (the Bank) and its subsidiaries (together, the Group), which comprise the consolidated statement of financial position as at 31 December 2018, and the consolidated statement of profit or loss, consolidated statement of changes in equity and consolidated statement of cash flows for the year then ended, and notes to the consolidated financial statements, including a summary of significant accounting policies.

In our opinion, the accompanying consolidated financial statements present fairly, in all material respects, the financial position of the Group as at 31 December 2018, and its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards (IFRSs).

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 consolidated financial statements"* section of this Independent auditor's report.

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

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

Responsibilities of management and the Audit Committee for the consolidated financial statements

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

In preparing the consolidated financial statements, management is responsible for assessing the Group'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 Group or to cease operations, or has no realistic alternative but to do so.

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

Auditor's responsibilities for the audit of the consolidated financial statements

Our objectives are to obtain reasonable assurance about whether the consolidated 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 consolidated financial statements.

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

- Identify and assess the risks of material misstatement of the consolidated 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 Group'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 Group'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 consolidated 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 Group to cease to continue as a going concern.

- Evaluate the overall presentation, structure and content of the consolidated financial statements, including the disclosures, and whether the consolidated financial statements represent the underlying transactions and events in a manner that achieves fair presentation.

- Obtain sufficient appropriate audit evidence regarding the financial information of the entities or business activities within the Group to express an opinion on the consolidated financial statements. We are responsible for the direction, supervision and performance of the group audit. We remain solely responsible for our audit opinion.

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

The engagement partner on the audit resulting in this independent auditor's report is Samir Asadullayev.

"Baltik Kaspian AUDIT" MMC
AUDIT
"Baltic Caspian AUDIT" LLC

Samir Asadullayev
Licensed auditor (license no. 072786)
Baltic Caspian Audit LLC
Member Firm of Crowe Global

25 April 2019
Baku, the Republic of Azerbaijan

Open Joint Stock Company Xalq Bank

Consolidated Statement of Profit or Loss for the year ended 31 December 2018
(in Azerbaijan Manats)

	Notes	Year ended 31 December 2018	Year ended 31 December 2017
Interest income	5	109,399,694	100,130,599
Interest expense	5	(23,158,018)	(25,552,727)
Net interest income		**86,241,676**	**74,577,872**
Credit loss expense on interest bearing assets	6	(24,893,112)	(25,681,851)
Net interest income after credit loss expense		**61,348,564**	**48,896,021**
Net fee and commission income	7	4,377,772	5,678,187
Net gain on foreign exchange operations	8	1,888,606	3,173,637
Net (loss) / gain on precious metals operations	9	(211,205)	1,219,629
Gain on revaluation of investment property	19	201,940	41,806
Provision for impairment losses on non-interest bearing assets	20	3,039,742	(6,613,841)
Other income		954,049	1,104,813
Non-interest income		**10,250,904**	**4,604,231**
Personnel expenses	10	(21,330,532)	(15,434,956)
General and administrative expenses	10	(13,863,957)	(12,115,114)
Depreciation and amortisation	18	(4,878,483)	(4,854,423)
Recovery of provision / (provision) for impairment losses on guarantees and other commitments	5	53,171	(105,036)
Non-interest expense		**(40,019,801)**	**(32,509,529)**
Profit before income tax		**31,579,667**	**20,990,723**
Income tax expense	11	(6,353,987)	(4,048,565)
Net profit for the year		**25,225,680**	**16,942,158**
Attributable to:			
- shareholders of the Bank		25,221,584	16,940,080
- non-controlling interest		4,096	2,078
		25,225,680	16,942,158
EARNINGS PER SHARE			
Basic and diluted (AZN)	12	6.948	4.666

Approved for issue and signed on behalf of the Management Board on 25 April 2019.

Chairman
Mr. Elkhan Aghayev

Chief Accountant
Mrs. Tamilla Asadova

Open Joint Stock Company Xalq Bank

Consolidated Statement of Financial Position as at 31 December 2018
(in Azerbaijan Manats)

	Notes	31 December 2018	31 December 2017
Assets			
Cash and cash equivalents	13	278,209,512	107,085,013
Precious metals		14,989,411	15,305,466
Amounts due from credit institutions	14	66,439,965	62,232,884
Loans to customers	15	1,332,211,034	1,263,204,930
Forfeiting	16	-	4,498,167
Investment securities	17	165,521,670	236,824,246
Property and equipment	18	66,571,711	68,214,636
Investment property	19	7,027,246	6,825,306
Intangible assets	18	1,511,655	1,551,970
Other assets	20	59,266,324	27,022,390
Total assets		**1,991,748,528**	**1,792,765,008**
Liabilities			
Amounts due to banks and government agencies	21	376,157,633	356,642,796
Customer accounts	22	1,335,034,786	1,183,456,480
Provision for impairment losses on other operations	25	61,703	203,376
Current income tax liability		4,159,131	2,439,634
Deferred income tax liability	11	2,387,920	1,457,705
Other liabilities	23	7,087,571	7,564,346
Total liabilities		**1,724,888,744**	**1,551,764,337**
Equity			
Share capital	24	225,078,600	225,078,600
Retained earnings		41,671,137	15,813,360
Non-controlling interest		110,047	108,711
Total equity		**266,859,784**	**241,000,671**
Total liabilities and equity		**1,991,748,528**	**1,792,765,008**

Approved for issue and signed on behalf of the Management Board on 25 April 2019.

AZƏRBAYCAN RESPUBLİKASI AÇIQ SƏHMDAR CƏMİYYƏTİ "XALQ" BANKI Xalq Bank "XALQ BANK" OPEN JOINT-STOCK COMPANY AZERBAIJAN REPUBLIC

Chairman
Mr. Elkhan Aghayev

Chief Accountant
Mrs. Tamilla Asadova

Open Joint Stock Company Xalq Bank

Consolidated Statement of Changes in Equity for the year ended 31 December 2018
(in Azerbaijan Manats)

	Share capital	Retained earnings	Non-controlling *interest*	Total equity
31 December 2016	**211,646,490**	**12,305,390**	**117,911**	**224,069,791**
Capitalization of retained earnings	13,432,110	(13,432,110)	-	-
Total income for the year	-	16,940,080	2,078	16,942,158
Change in ownership interest in subsidiary	-	-	(11,278)	(11,278)
31 December 2017	**225,078,600**	**15,813,360**	**108,711**	**241,000,671**
Impact of adopting IFRS 9 (Note 4)	-	6,626,188	-	6,626,188
Restated opening balance under IFRS 9	**225,078,600**	**22,439,548**	**108,711**	**247,626,859**
Dividends to shareholders of Bank	-	(5,989,995)	-	(5,989,995)
Total income for the year		25,221,584	4,096	25,225,680
Change in ownership interest in subsidiary	-	-	(2,760)	(2,760)
31 December 2018	**225,078,600**	**41,671,137**	**110,047**	**266,859,784**

Approved for issue and signed on behalf of the Management Board on 25 April 2019.

Chairman
Mr. Elkhan Aghayev

Chief Accountant
Mrs. Tamilla Asadova

Open Joint Stock Company Xalq Bank

Consolidated Statement of Cash Flows for the year ended 31 December 2018
(in Azerbaijan Manats)

	Notes	Year ended 31 December 2018	Year ended 31 December 2017
CASH FLOWS FROM OPERATING ACTIVITIES:			
Profit before income tax		31,579,667	20,990,723
Adjustments for:			
Provision for impairment losses on interest bearing assets	6	24,893,112	25,681,851
Recovery of provision for guarantees and other commitments		(74,534)	105,036
Provision for impairment losses on non-interest bearing assets		(3,039,742)	6,613,841
Net unrealized loss / (gain) arising from changes in foreign currency exchange rates		297,371	1,133,068
Depreciation and amortization	18	4,878,483	4,864,423
Gain on revaluation of investment property	19	(201,940)	(41,806)
Gain on disposal of property and equipment		(40,170)	(102,243)
Change in interest accruals, net		(1,233,190)	3,525,321
Cash flows from operating activities before changes in operating assets and liabilities		**57,059,057**	**62,760,214**
Changes in operating assets and liabilities			
(Increase)/decrease in operating assets:			
Precious metals		316,055	(1,192,784)
Amounts due from credit institutions		(3,869,207)	32,254,101
Loans to customers		(84,513,085)	(75,973,298)
Forfeiting		4,589,966	8,712,644
Other assets		(29,202,870)	(9,567,480)
Increase/(decrease) in operating liabilities:			
Amounts due to banks and government agencies		19,489,573	73,415,776
Customer accounts		151,566,731	53,169,642
Other liabilities		(476,775)	(4,660,817)
Cash inflow from operating activities before taxation		**114,959,445**	**138,917,998**
Income tax paid		(5,360,822)	(1,360,164)
Net cash inflow from operating activities		**109,598,623**	**137,557,834**
CASH FLOWS FROM INVESTING ACTIVITIES:			
Purchase of property, equipment and intangible assets	18	(3,238,673)	(4,744,162)
Proceeds on disposal of property and equipment		83,600	155,750
Proceeds from sale and redemption of investment securities		70,971,075	(160,163,312)
Acquisition of subsidiary, net of cash acquired		(2,760)	(11,278)
Net cash inflow / (outflow) from investing activities		**67,813,242**	**(164,763,002)**

Consolidated Statement of Cash Flows for the year ended 31 December 2018 (Continued)
(in Azerbaijan Manats)

	Notes	Year ended 31 December 2018	Year ended 31 December 2017
CASH FLOWS FROM FINANCING ACTIVITIES:			
Dividends paid to shareholders of the Bank		(5,989,995)	-
Net cash inflow from financing activities		**(5,989,995)**	**-**
Effect of foreign exchange rate changes on cash and cash equivalents		(297,371)	(1,133,068)
Net increase / (decrease) in cash and cash equivalents		171,124,499	(28,338,236)
Cash and cash equivalents, beginning of year		107,085,013	135,423,249
Cash and cash equivalents, end of year	**13**	**278,209,512**	**107,085,013**

Interest paid and received by the Group in cash during the year ended 31 December 2018 amounted to AZN 23,121,179 and AZN 108,129,665, respectively.

Interest paid and received by the Group in cash during the year ended 31 December 2017 amounted to AZN 26,443,386 and AZN 104,546,579, respectively.

Approved for issue and signed on behalf of the Management Board on 25 April 2019.

Chairman
Mr. Elkhan Aghayev

Chief Accountant
Mrs. Tamilla Asadova

1. Background

Xalq Bank is a joint stock company which was established on 24 December 2004 in accordance with establishment agreement and was registered by the Central Bank of Azerbaijan Republic on 27 December 2004. The address of its registered office is 22L Inshaatchilar Avenue, Baku, AZ 1006, Azerbaijan. The Bank is regulated by Financial Market Supervision Authority of Azerbaijan Republic (the "FIMSA") and conducts its business under the general banking license number 246. The Bank had 29 and 29 branches in Azerbaijan as at 31 December 2018 and 2017 respectively. The Bank's primary business consists of commercial activities, trading with foreign currencies, originating loans and guarantees.

The number of employees of the Bank at 31 December 2018 and 2017 was 628 and 572, respectively.

The Bank is a parent company of a banking group (the "Group") which consists of the following enterprises consolidated in the financial statements:

		The Bank ownership interest/ voting rights		
Name	**Country of operation**	**2018**	**2017**	**Type of operation**
Xalq Kapital LLC	*The Republic of Azerbaijan*	100 %	100 %	*Securities market transactions*
Baki Ayaqqabi -2 OJSC	*The Republic of Azerbaijan*	98.36%	98.35%	*Dormant*

"Xalq Kapital" LLC is a limited liability company registered in the Republic of Azerbaijan on 17 August 2007. The company's principal activity is operations with securities, broker and dealer operations.

"Baki Ayaqqabi -2" OJSC is a Joint Stock Company registered in the Republic of Azerbaijan in December 1980. The Company's principal activity had been the manufacture of footwear. The Company has not been functioning since June 1999. The Group has acquired the controlling interest in the Company's capital with the primary purpose of using it as investment property. The Group's management is still uncertain of the detailed plans regarding the Company.

As at 31 December 2018 and 2017 the following shareholders owned the issued shares of the Bank:

	31 December 2018	**31 December 2017**
	Ownership interest, %	**Ownership interest, %**
Ideal Biznes Ko LLC	50.00	50.00
Yevro Standart LLC	33.85	33.85
AMAL Invest Group LLC	16.15	16.15
Total	**100**	**100**

As at 31 December 2018 and 2017 the Bank is ultimately owned by Mrs. Leyla Aliyeva and Mrs. Arzu Aliyeva, who exercise joint control over the Bank.

2. Basis of presentation

Accounting basis

These consolidated financial statements of the Group have been prepared in accordance with International Financial Reporting Standards ("IFRS") issued by the International Accounting Standards Board ("IASB") and Interpretations issued by the International Financial Reporting Interpretations Committee ("IFRIC"). These consolidated financial statements are presented in Azerbaijan Manats ("AZN") unless otherwise indicated. These consolidated financial statements have been prepared under the historical cost convention, except for the measurement at fair value of certain financial instruments and measurement of investment property at revalued amounts according to International Accounting Standard ("IAS") No. 40 "Investment Property".

The Group maintains its accounting records in accordance with Azerbaijan law. These consolidated financial statements have been prepared based on the Azerbaijani statutory accounting records and have been adjusted to conform with IFRS. These adjustments include certain reclassifications to reflect the economic substance of underlying transactions including reclassifications of certain assets and liabilities, income and expenses to appropriate financial statement captions.

3. Summary of significant accounting policies

Basis of consolidation

The consolidated financial statements incorporate the financial statements of the Bank and entities controlled by the Bank (its subsidiaries) made up to 31 December each year. Control is achieved where the Bank has the power to govern the financial and operating policies of an investee entity so as to obtain benefits from its activities.

On acquisition, the assets and liabilities and contingent liabilities of a subsidiary are measured at their fair values at the date of acquisition. Any excess of the cost of acquisition over the fair values of the identifiable net assets acquired is recognized as goodwill. Any deficiency of the cost of acquisition below the fair values of the identifiable net assets acquired (i.e. discount on acquisition) is credited to the consolidated income statement in the period of acquisition. The minority interest is stated at the minority's proportion of the fair values of the assets and liabilities recognized. Subsequently, any losses applicable to the minority interest in excess of the minority interest are allocated against the interests of the parent. The equity attributable to equity holders of the parent and net income attributable to minority shareholders' interests are shown separately in the consolidated statement of financial position and income statement, respectively.

The results of subsidiaries acquired or disposed of during the year are included in the consolidated income statement from the effective date of acquisition or up to the effective date of disposal, as appropriate. Where necessary, adjustments are made to the financial statements of subsidiaries to bring the accounting policies used into line with those used by the Group.

All significant intra-group transactions, balances, income and expenses are eliminated on consolidation.

The difference, if any, between the carrying amount of minority interest and the amount received on its purchase is recognized in equity attributable to the equity holders of the parent.

Fair value measurement

The Group measures financial instruments carried at FVPL and FVOCI and non-financial assets such as investment property, at fair value at each balance sheet date.

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

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

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

The Group uses valuation techniques that are appropriate in the circumstances and for which sufficient data are available to measure fair value, maximising the use of relevant observable inputs and minimising the use of unobservable inputs. All assets and liabilities for which fair value is measured or disclosed in the consolidated financial statements are categorised within the fair value hierarchy, described as follows, based on the lowest level input that is significant to the fair value measurement as a whole:

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

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

Financial assets and liabilities

Initial recognition

Date of recognition

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

Initial measurement

The classification of financial instruments at initial recognition depends on their contractual terms and the business model for managing the instruments. Financial instruments are initially measured at their fair value and, except in the case of financial assets and financial liabilities recorded at FVPL, transaction costs are added to, or subtracted from, this amount.

Measurement categories of financial assets and liabilities

From 1 January 2018, the Group classifies all of its financial assets based on the business model for managing the assets and the asset's contractual terms, measured at either:

- Amortised cost;
- FVOCI;
- FVPL.

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

Before 1 January 2018, the Bank classified its financial assets as loans and receivables (amortised cost), FVPL, available-for-sale or held-to-maturity (amortised cost)

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

Amounts due from credit institutions, loans to customers, investments securities at amortised cost

Before 1 January 2018, amounts due from credit institutions and loans to customers included non-derivative financial assets with fixed or determinable payments that were not quoted in an active market, other than those:

- That the Group intended to sell immediately or in the near term;
- That the Group, upon initial recognition, designated as at FVPL or as available-for-sale;
- For which the Group may not recover substantially all of its initial investment, other than because of credit deterioration, which were designated as available-for-sale.

From 1 January 2018, the Group only measures amounts due from credit institutions, loans to customers and other financial investments at amortised cost if both of the following conditions are met:

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

The details of these conditions are outlined below.

Business model assessment

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

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

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

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

The SPPI test

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

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

The most significant elements of interest within a lending arrangement are typically the consideration for the time value of money and credit risk. To make the SPPI assessment, the Group applies judgement and considers relevant factors such as the currency in which the financial asset is denominated, and the period for which the interest rate is set.

In contrast, contractual terms that introduce a more than de minimis exposure to risks or volatility in the contractual cash flows that are unrelated to a basic lending arrangement do not give rise to contractual cash flows that are solely payments of principal and interest on the amount outstanding. In such cases, the financial asset is required to be measured at FVPL.

Debt instruments at FVOCI

From 1 January 2018, the Group applies the new category under IFRS 9 of debt instruments measured at FVOCI when both of the following conditions are met:

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

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

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

Equity instruments at FVOCI

From 1 January 2018, upon initial recognition, the Group occasionally elects to classify irrevocably some of its equity investments as equity instruments at FVOCI when they meet the definition of equity under IAS 32 *Financial Instruments: Presentation* and are not held for trading. Such classification is determined on an instrument-by-instrument basis.

Gains and losses on these equity instruments are never recycled to profit or loss. Dividends are recognised in profit or loss as other income when the right of the payment has been established, except when the Group benefits from such proceeds as a recovery of part of the cost of the instrument, in which case, such gains are recorded in OCI. Equity instruments at FVOCI are not subject to an impairment assessment. Upon disposal of these instruments, the accumulated revaluation reserve is transferred to retained earnings.

Financial guarantees, letters of credit and undrawn loan commitments

The Group issues financial guarantees, letters of credit and loan commitments.

Financial guarantees are initially recognised in the financial statements at fair value, being the premium received. Subsequent to initial recognition, the Group's liability under each guarantee is measured at the higher of the amount initially recognised less cumulative amortisation recognised in the consolidated statement of profit or loss, and – under IAS 37 (before 1 January 2018) – the best estimate of expenditure required to settle any financial obligation arising as a result of the guarantee, or – under IFRS 9 (from 1 January 2018) – an ECL provision.

Undrawn loan commitments and letters of credits are commitments under which, over the duration of the commitment, the Group is required to provide a loan with pre-specified terms to the customer. Similar to financial guarantee contracts, under IAS 39, a provision was made if they were an onerous contract but, from 1 January 2018, these contracts are in the scope of the ECL requirements.

Performance guarantees

Performance guarantees are contracts that provide compensation if another party fails to perform a contractual obligation. Performance guarantees do not transfer credit risk. The risk under performance guarantee contracts is the possibility that the failure to perform the contractual obligation by another party occurs. Therefore, performance guarantees are not considered financial instruments and thus do not fall in scope of IFRS 9.

Loans and receivables

Before 1 January 2018, loans and receivables were non-derivative financial assets with fixed or determinable payments that were not quoted in an active market. They were not entered into with the intention of immediate or short-term resale and were not classified as trading securities or designated as investment securities available-for-sale. Such assets were carried at amortised cost using the effective interest method. Gains and losses were recognised in profit or loss when the loans and receivables were derecognised or impaired, as well as through the amortisation process.

Held-to-maturity investments

Before 1 January 2018, non-derivative financial assets with fixed or determinable payments and fixed maturity were classified as held-to-maturity when the Group has the positive intention and ability to hold them to maturity. Investments intended to be held for an undefined period were not included in this classification. Held-to-maturity investments were subsequently measured at amortised cost. Gains and losses were recognised in profit or loss when the investments are impaired, as well as through the amortisation process.

Available-for-sale financial assets

Before 1 January 2018, available-for-sale financial assets were those non-derivative financial assets that were designated as available-for-sale or were not classified in any of the three preceding categories. After initial recognition available-for sale financial assets were measured at fair value with gains or losses being recognised in other comprehensive income until the investment was derecognised or until the investment was determined to be impaired at which time the cumulative gain or loss previously reported in other comprehensive income was reclassified to the consolidated statement of profit or loss. However, interest calculated using the effective interest method was recognised in profit or loss.

Reclassification of financial assets and liabilities

From 1 January 2018, the Group does not reclassify its financial assets subsequent to their initial recognition, apart from the exceptional circumstances in which the Group changes the business model for managing financial assets. Financial liabilities are never reclassified. The Group did not reclassify any of its financial assets and liabilities in 2017.

Cash and cash equivalents

Cash and cash equivalents consist of cash on hand, amounts due from the Central Bank of Azerbaijan Republic, including time deposits ut to 15 days, and correspondent accounts with other banks.

Precious metals

Assets and liabilities denominated in gold and other precious metals are translated at the current rate computed based on the Central Bank rate effective at the date. Changes in the bid prices are recorded in net gain on operations with precious metals.

Allowance for impairment losses under IAS 39

Assets carried at amortized cost

The Group accounts for impairment losses of financial assets that are not carried at fair value when there is objective evidence that a financial asset or group of financial assets is impaired. The impairment losses are measured as the difference between carrying amounts and the present value of expected future cash flows, including amounts recoverable from guarantees and collateral, discounted at the financial asset's original effective interest rate. Such impairment losses are not reversed unless if in a subsequent period the amount of the impairment loss decreases and the decrease can be related objectively to an event occurring after the impairment was recognized, such as recoveries, in which case the previously recognized impairment loss is reversed by adjusting an allowance account.

For financial assets carried at cost the impairment losses are measured as the difference between the carrying amount of the financial asset and the present value of estimated future cash flows discounted at the current market rate of return for a similar financial asset. Such impairment losses are not reversed.

Available-for-sale financial assets

If an available-for-sale asset is impaired, a consolidated amount comprising the difference between its cost (net of any principal payment and amortization) and its current fair value, less any impairment loss previously recognized in the consolidated income statement, is transferred from equity to the consolidated income statement. Reversals of impairment losses in respect of equity instruments classified as available-for-sale are not recognized in the consolidated income statement. Reversals of impairment losses on debt instruments are reversed through the consolidated income statement if the increase in fair value of the instrument can be objectively related to an event occurring after the impairment loss were recognized in the consolidated income statement.

The determination of impairment losses is based on an analysis of the risk assets and reflects the amount which, in the judgment of management, is adequate to provide for losses incurred. Provisions are made as a result of an individual appraisal of risk assets for financial assets that are individually significant, and an individual or collective assessment for financial assets that are not individually significant.

The change in impairment losses is charged to profit either through allowance account (financial assets that are carried at amortized cost) or direct write-off (financial assets carried at cost). The total of the impairment losses is deducted in arriving at assets as shown in the consolidated statement of financial position. Factors that the Group considers in determining whether it has objective evidence that an impairment loss has been incurred include information about the debtors' or issuers' liquidity, solvency and business and financial risk exposures, levels of and trends in delinquencies for similar financial assets, national and local economic trends and conditions, and the fair value of collateral and guarantees. These and other factors may, either individually or taken together, provide sufficient objective evidence that an impairment loss has been incurred in a financial asset or group of financial assets.

It should be understood that estimates of losses involve an exercise of judgment. While it is possible that in particular periods the Group may sustain losses which are substantial relative for impairment losses, it is the judgment of management that the impairment losses are adequate to absorb losses incurred on risk assets, at the reporting date.

Information on impairment assessment under IFRS 9 is presented in Note 30.

Investment properties

Investment property comprises land or buildings, which are held in order to earn rentals or for capital appreciation or both, and which are not occupied by the companies in the Group or otherwise held for sale. Property held under operating lease is classified as investment property if, and only if, it meets the definition of an investment property. Investment property is carried at fair value. Fair value is based on active market prices, adjusted, if necessary, for any difference in the nature, location or condition of the property. If this information is not available, the Group uses alternative valuation methods such as discounted cash flow projections. Changes in the fair value of investment property are recorded in the income statement.

Premises, equipment and intangible assets

Property, equipment and intangible assets are carried at historical cost less accumulated depreciation and amortization and any recognized impairment loss. Depreciation on assets under construction and those not placed in service commences from the date the assets are ready for their intended use.

Depreciation of property, equipment and amortization of intangible assets is charged on their historical cost and is designed to write off assets over their useful lives. It is calculated on a straight line basis at the following annual rates:

Building	3.3%
Furniture and equipment	25%
Computers	25%
Vehicles	15%
Other equipment	20%
Intangible assets	10%

The carrying amounts of property, equipment and intangible assets are reviewed at each reporting date to assess whether they are recorded in excess of their recoverable amounts, and where the carrying values exceed the estimated recoverable amounts, the assets are written down to their recoverable amounts. Impairment is recognized in the respective period and is included in operating expenses. After the recognition of an impairment loss the depreciation charge for property and equipment is adjusted in future periods to allocate the assets' revised carrying value, less its residual value (if any), on a systematic basis over its remaining useful life.

Provisions

Provisions are recognized when the Group 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 obligation can be made.

Taxation

Income tax expense comprises current and deferred taxation. Income tax expense for the current period is determined on the basis of the taxable profit received in the year. Taxable profit differs from net profit as reported in the income statement because it excludes items of income or expense that are taxable or deductible in other years and it further excludes items that are never taxable or deductible. The Group's current tax expense is calculated using tax rates that have been enacted during the reporting period.

Deferred tax is reported using the balance sheet liability method and represents income tax assets and liabilities on the temporary difference between the carrying value of assets and liabilities and the respective tax accounting data used to arrive at the taxable profit. Deferred tax liabilities are generally recognized for all taxable temporary differences and deferred tax assets are recognized to the extent that it is probable that taxable profits will be available against which the respective deferred tax assets can be utilized. Such assets and liabilities are not recognised if the temporary difference arises from goodwill or from the initial recognition (other than in a business combination) of other assets and liabilities in transactions that affect neither the tax profit nor the accounting profit. Deferred tax liabilities are recognised for taxable temporary differences arising on investments in subsidiaries and associates, and interests in joint ventures, except where the Group is able to control the reversal of the temporary difference and it is probable that the temporary difference will not reverse in the foreseeable future. Deferred tax assets arising from deductible temporary differences associated with such investments and interests are only recognized to the extent that it is probable that there will be sufficient taxable profits against which to utilize the benefits of the temporary differences and they are expected to reverse in the foreseeable future.

The carrying value of deferred tax assets is reviewed at each reporting date and reduced to the extent that it is no longer probable that a related tax benefit will be realized sufficient for full or partial recovery of the asset.

Deferred tax assets and liabilities are offset by the Group with the resulting difference reported in the financial statements if:

- The Group has a legally enforceable right to set off the current tax assets and current tax liabilities; and
- Deferred tax assets and deferred tax liabilities relate to income taxes levied by the same tax authority on the same taxpayer.

Deferred tax is calculated at the tax rates that are expected to apply in the period when the liability is settled or the asset realized. Deferred tax is charged or credited in the consolidated income statement, except when it relates to items charged or credited directly to equity, in which case the deferred tax is also dealt with in equity.

Amounts due to banks and customer accounts

Amounts due to banks and customer accounts are initially recognized at fair value. Subsequently amounts due are stated at amortized cost and any difference between carrying and redemption value is recognized in the consolidated income statement over the period of the borrowings using the effective interest method.

Contingencies

Contingent liabilities are not recognized in the consolidated 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 consolidated statement of financial position but disclosed when an inflow of economic benefits is probable.

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 recognised as additional paid-in capital.

Dividends on ordinary shares are recognized in equity as a reduction in the period in which they are declared. Dividends that are declared after the reporting date are treated as a subsequent event under International Accounting Standard 10 "Events after the reporting period" ("IAS 10") and disclosed accordingly.

Retirement and other benefit obligations

In accordance with the requirements of the legislation of the Republic of Azerbaijan, the Group withholds amounts of pension contributions from employee salaries and pays them to the state pension fund. Such expense is charged in the period the related salaries are earned. Upon retirement all retirement benefit payments are made by the state pension fund. The Group does not have any pension arrangements separate from the state pension system of Azerbaijan, which requires current contributions by employer calculated as a percentage of current gross salary payments. In addition, the Group has no post-retirement benefits or other significant compensated benefits requiring accrual.

Recognition of income and expenses

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

Interest and similar revenue and expense

From 1 January 2018, the Group calculates interest revenue on debt financial assets measured at amortized cost or at FVOCI by applying the EIR to the gross carrying amount of financial assets other than credit-impaired assets (before 1 January 2018: by applying EIR to the amortized cost of financial assets). EIR is the rate that exactly discounts estimated future cash payments or receipts through the expected life of the financial instrument or a shorter period, where appropriate, to the net carrying amount of the financial asset or financial liability. The calculation takes into account all contractual terms of the financial instrument (for example, prepayment options) and includes any fees or incremental costs that are directly attributable to the instrument and are an integral part of the effective interest rate, but not future credit losses. The carrying amount of the financial asset or financial liability is adjusted if the Group revises its estimates of payments or receipts. The adjusted carrying amount is calculated based on the original effective interest rate and the change in carrying amount is recorded as interest revenue or expense.

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

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

Interest revenue on all financial assets at FVPL is recognised using the contractual interest rate.

Fee and commission income

The Group 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

Fees earned for the provision of services over a period of time are accrued over that period. These fees include commission income on guarantees and letters of credit. 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 recognised as an adjustment to the effective interest rate on the loan.

Fee income earned at a point in time

Fees arising from settlement and cash operations are recognized upon completion of the underlying transactions. Each cash operation and settlement operation is treated as a separate performance obligation.

Foreign currency translation

Monetary assets and liabilities denominated in foreign currencies are translated into Azerbaijan Manats at the appropriate spot rates of exchange ruling at the reporting date. Foreign currency transactions are accounted for at the exchange rates prevailing at the date of the transaction. Profits and losses arising from these translations are included in net gain on foreign exchange operations.

Rates of exchange

The exchange rates at the year end used by the Group in the preparation of the consolidated financial statements are as follows:

31 December 2018	31 December 2017
USD 1 - AZN 1.7000	USD 1 - AZN 1.7001
EUR 1 = AZN 1.9468	EUR 1 = AZN 2.0307
GBP 1 = AZN 2.1529	GBP 1 = AZN 2.2881
RUR 1 = AZN 0.0245	RUR 1 = AZN 0.0295

Offset of financial assets and liabilities

Financial assets and liabilities are offset and reported net on the consolidated statement of financial position when the Group has a legally enforceable right to set off the recognized amounts and the Group intends either to settle on a net basis or to realize the asset and settle the liability simultaneously. In accounting for a transfer of a financial asset that does not qualify for derecognition, the Group does not offset the transferred asset and the associated liability.

4. Adoption of new or revised standards and interpretations

Certain new standards and interpretations became effective for the Group from 1 January 2018. The nature and effect of the changes as a result of adoption of these new accounting standards are described below.

IFRS 9 Financial Instruments

IFRS 9 replaces IAS 39 *Financial Instruments: Recognition and Measurement* for annual periods on or after 1 January 2018. The Bank has not restated comparative information for 2017 for financial instruments in the scope of IFRS 9. Therefore, the comparative information for 2017 is reported under IAS 39 and is not comparable to the information presented for 2018. Differences arising from the adoption of IFRS 9 have been recognised directly in retained earnings as of 1 January 2018 and are disclosed below.

(a) Classification and measurement

Under IFRS 9, all debt financial assets that do not meet a "solely payment of principal and interest" (SPPI) criterion, are classified at initial recognition as fair value through profit or loss (FVPL). Under this criterion, debt instruments that do not correspond to a "basic lending arrangement", such as instruments containing embedded conversion options or "non-recourse" loans, are measured at FVPL. For debt financial assets that meet the SPPI criterion, classification at initial recognition is determined based on the business model, under which these instruments are managed:

- Instruments that are managed on a "hold to collect" basis are measured at amortised cost;
- Instruments that are managed on a "hold to collect and for sale" basis are measured at fair value through other comprehensive income (FVOCI);
- Instruments that are managed on other basis, including trading financial assets, will be measured at FVPL.

Equity financial assets are required to be classified at initial recognition as FVPL unless an irrevocable designation is made to classify the instrument as FVOCI. For equity investments classified as FVOCI, all realised and unrealised gains and losses, except for dividend income, are recognised in other comprehensive income with no subsequent reclassification to profit and loss.

The classification and measurement of financial liabilities remains largely unchanged from the current IAS 39 requirements.

(b) Impairment

The adoption of IFRS 9 has fundamentally changed the Group's accounting for loan impairment by replacing IAS 39 incurred loss approach with a forward-looking expected credit loss (ECL) approach. From 1 January 2018, the Group has been recording the allowance for expected credit losses for all loans and other debt financial assets not held at FVPL, together with loan commitments and financial guarantee contracts. Equity instruments are not subject to impairment under IFRS 9.

The allowance is based on the ECLs associated with the probability of default in the next twelve months unless there has been a significant increase in credit risk since origination. If the financial asset meets the definition of purchased or originated credit impaired (POCI), the allowance is based on the change in the ECLs over the life of the asset. Details of the Group's impairment method are disclosed in Note 30. The quantitative impact of applying IFRS 9 as at 1 January 2018 is disclosed in section (c) below.

(c) Effect of transition to IFRS 9

The following tables set out the impact of adopting IFRS 9 on the statement of financial position and retained earnings as at 1 January 2018 including the effect of replacing IAS 39 incurred credit loss calculations with IFRS 9 ECL.

A reconciliation between the carrying amounts under IAS 39 to the balances reported under IFRS 9 as at 1 January 2018 is as follows:

	IAS 39 measurement		Re-measurement	IFRS 9	
Financial assets	**Category**	**Amount**	**ECL**	**Amount**	**Category**
Cash and cash equivalents	L&R[1]	107,085,013	-	107,085,013	Amortised cost
Amounts due from credit institutions	L&R	62,232,884	413,735	62,646,619	Amortised cost
Loans to customers	L&R	1,263,204,930	7,961,997	1271,166,927	Amortised cost
Investment securities – amortised cost	HTM[2]	236,644,596	(160,137)	236,484,459	Amortised cost
Investment securities – equity securities at FVOCI	AFS[3]	179,650	-	179,650	FVOCI (equity)
Other financial assets		24,060,879	-	24,060,879	
Total financial assets		**1,693,407,952**	**8,215,595**	**1,701,623,547**	
Non-financial liabilities					
Provisions		203,376	(67,139)	136,237	
Deferred tax liabilities		1,457,705	1,656,547	3,114,252	
Total liabilities		**1,661,081**	**1,589,408**	**3,250,489**	

[1] L&R: Loans and receivables.

[2] HTM: Held-to-maturity.

[3] AFS: Available-for-sale.

The impact of transition to IFRS 9 on retained earnings is as follows:

	Retained earnings
Closing balance under IAS 39 (31 December 2017)	15,813,360
Recognition of IFRS 9 ECLs	8,282,735
Deferred tax in relation to the above	(1,656,547)
Restated opening balance under IFRS 9 (1 January 2018)	**22,439,548**
Total change in equity due to adopting IFRS 9	**6,626,188**

The following table reconciles the aggregate opening loan loss allowances under IAS 39 and provisions for loan commitments and financial guarantee contracts in accordance with IAS 37 *Provisions Contingent Liabilities and Contingent Assets* to the ECL allowances under IFRS 9.

	Loan loss allowance/ provision under IAS 39 / IAS 37 at 31 December 2017	***Remeasurement under IFRS 9***	***ECL under IFRS 9 at 1 January 2018***
Impairment allowance for			
Loans and receivables at amortised cost	(111,837,455)	7,961,997	(103,875,458)
Amounts due from credit institutions	(417,914)	413,735	(4,179)
Investment securities at amortised cost	-	(160,137)	(160,137)
	(112,255,369)	**8,215,595**	**(104,039,773)**
Credit related commitments and performance guarantees	(203,376)	67,139	(136,237)
	(112,458,745)	**8,282,735**	**(104,176,010)**

IFRS 15 Revenue from Contracts with Customers

IFRS 15, issued in May 2014, and amended in April 2016, establishes a five-step model to account for revenue arising from contracts with customers. Under IFRS 15, revenue is recognised at an amount that reflects the consideration to which an entity expects to be entitled in exchange for transferring goods or services to a customer. However, the standard does not apply to revenue associated with financial instruments and leases, and therefore, does not impact the majority of the Group's revenue including interest income, gains/(losses) on operations with securities, lease income which are covered by IFRS 9 *Financial Instruments*. As a result, the majority of the Group's income are not impacted by the adoption of this standard.

The following amended standards became effective for the Group from 1 January 2018, but did not have any material impact on the Group:

- ***Amendments to IFRS 2 "Share-based Payment"*** (issued on 20 June 2016 and effective for annual periods beginning on or after 1 January 2018).
- ***Applying IFRS 9 "Financial Instruments" with IFRS 4 "Insurance Contracts" – Amendments to IFRS 4*** (issued on 12 September 2016 and effective, depending on the approach, for annual periods beginning on or after 1 January 2018 for entities that choose to apply temporary exemption option, or when the entity first applies IFRS 9 for entities that choose to apply the overlay approach).
- ***Annual Improvements to IFRSs 2014-2016 cycle – Amendments to IFRS 1 and IAS 28*** (issued on 8 December 2016 and effective for annual periods beginning on or after 1 January 2018).
- ***IFRIC 22 – "Foreign Currency Transactions and Advance Consideration"*** (issued on 8 December 2016 and effective for annual periods beginning on or after 1 January 2018).
- ***Transfers of Investment Property – Amendments to IAS 40*** (issued on 8 December 2016 and effective for annual periods beginning on or after 1 January 2018).

New Accounting Pronouncements

Certain new standards and interpretations have been published that become effective for the accounting periods beginning on or after 1 January 2019 or later periods and which are relevant to the Group but not early adopted by the Group.

IFRS 16 Leases (issued In January 2016 and effective for the annual periods beginning on or after 1 January 2019). IFRS 16 results in lessees accounting for most leases within the scope of the standard in a manner similar to the way in which finance leases are currently accounted for under IAS 17 *Leases*. Lessees will recognise a 'right of use' asset and a corresponding financial liability on the balance sheet. The asset will be amortized over the length of the lease and the financial liability measured at amortized cost. Lessor accounting remains substantially the same as in IAS 17 *Leases*.

Long-term Interests in Associates and Joint Ventures - Amendments to IAS 28 (issued on 12 October 2017 and effective for annual periods beginning on or after 1 January 2019). The amendments clarify that reporting entities should apply IFRS 9 to long-term loans, preference shares and similar instruments that form part of a net investment in an equity method investee before they can reduce such carrying value by a share of loss of the investee that exceeds the amount of investor's interest in ordinary shares.

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.

Sale or Contribution of Assets between an Investor and its Associate or Joint Venture - Amendments to IFRS 10 and IAS 28 (issued in September 2014 with latest changes on 15 December 2015; effective date is not set). The amendments address the acknowledged inconsistency between the requirements in IFRS 10 and IAS 28 in dealing with the loss of control of a subsidiary that is contributed to an associate or a joint venture. The amendments clarify that an investor recognizes a full gain or loss on the sale or contribution of assets that constitute a business, as defined in IFRS 3, between an investor and its associate or joint venture. The gain or loss resulting from the re- measurement at fair value of an investment retained in a former subsidiary is recognized only to the extent of unrelated investors' interests in that former subsidiary.

Described above, the new standards and interpretations are not expected to significantly affect the Group's financial statements.

5. Net interest income

Net interest income comprise:

	Year ended 31 December 2018	Year ended 31 December 2017
Interest income comprises		
Interest on loans to customers	85,895,081	86,539,186
Interest on debt securities	14,831,174	8,197,263
Interest on due from banks	7,780,398	5,029,888
Interest on guarantees	736,411	297,571
Interest on other operations	156,630	66,691
Total interest income on financial assets recorded at amortized cost	109,399,694	100,130,599
Interest expense comprises:		
Interest on customer accounts	(15,663,157)	(17,992,889)
Interest on due to banks and government agencies	(7,494,861)	(7,559,838)
Total interest expense on financial assets recorded at amortized cost	(23,158,018)	(25,552,727)
Net interest income before provision for impairment losses on interest bearing assets	**86,241,676**	**74,577,872**

6. Credit loss expense and other impairment and provisions

The movements in credit loss expense on interest earning assets were as follows:

	Forfeiting	Investment securities	Due from banks	Loans to customers	Total
31 December 2016	**(133,026)**	**-**	**(906,310)**	**(105,592,919)**	**(106,632,255)**
(Provision) / recovery of provision	41,227	-	488,396	(26,211,474)	(25,681,851)
Write-off of assets	-	-	-	19,966,938	19,966,938
31 December 2017	**(91,799)**	**-**	**(417,914)**	**(111,837,455)**	**(112,347,168)**
Impact of adopting IFRS 9	-	(160,137)	413,735	7,961,997	8,215,595
Restated opening balance under IFRS 9	**(91,799)**	**(160,137)**	**(4,179)**	**(103,875,458)**	**(104,131,573)**
(Provision) / recovery of provision	91,799	74,346	(128,137)	(24,931,120)	(24,893,112)
Write-off of assets	-	-	-	10,531,689	10,531,689
31 December 2018	**-**	**(85,791)**	**(132,316)**	**(118,274,889)**	**(118,492,996)**

The movements in provision for impairment losses on guarantees and other commitments were as follows:

	Guarantees and other commitments
31 December 2016	**(98,340)**
Provision	(105,036)
31 December 2017	**(203,376)**
Impact of adopting IFRS 9	67,139
Restated opening balance under IFRS 9	**(136,237)**
Recovery of provision	53,171
Write-off	21,363
31 December 2018	**(61,703)**

7. Fee and commission income and expense

Fee and commission income and expense comprise:

	Year ended 31 December 2018	Year ended 31 December 2017
Fee and commission income:		
Plastic cards operations	1,647,636	1,489,698
Settlements	1,622,754	1,459,167
Forfeiting	1,514,622	2,568,866
Cash operations	1,425,163	1,035,104
Foreign exchange operations	882,441	1,186,060
Letters of credit	99,734	7,295
Guarantee letters	61,310	39,439
Other	309,985	211,022
Total fee and commission income	**7,563,645**	**7,996,651**
Fee and commission expense:		
Plastic cards operations	(1,491,476)	(1,333,269)
Settlements	(659,360)	(404,159)
Cash operations	(199,130)	(158,017)
Letters of credit	(55,353)	(2,858)
Broker operationst	(5,348)	(46,817)
Other	(775,206)	(373,344)
Total fee and commission expense	**(3,185,873)**	**(2,318,464)**
Net fee and commission income	**4,377,772**	**5,678,187**

8. Net gain on foreign exchange operations

Net gain on foreign exchange operations comprise:

	Year ended 31 December 2018	Year ended 31 December 2017
Dealing differences, net	2,185,977	4,306,705
Translation differences, net	(297,371)	(1,133,068)
Total net gain on foreign exchange operations	**1,888,606**	**3,173,637**

9. Net (loss) / gain on precious metals operations

Net (loss) / gain on precious metals operations comprise:

	Year ended 31 December 2018	Year ended 31 December 2017
Net gain on precious metals operations	4,211	10,308
Translation difference on precious metals	(215,416)	1,209,321
Total net (loss) / gain on precious metals operations	**(211,205)**	**1,219,629**

10. Personnel, general and administrative expenses

Personnel, general and administrative expenses comprises:

	Year ended 31 December 2018	Year ended 31 December 2017
Salaries and bonuses	(17,497,906)	(12,532,796)
Social security costs	(3,741,639)	(2,772,140)
Other employee related expenses	(90,987)	(130,020)
Total personnel expenses	**(21,330,532)**	**(15,434,956)**
Payments to the Deposit Insurance Fund of the Republic of Azerbaijan	(3,758,078)	(3,806,212)
Operating leases	(1,349,367)	(1,346,054)
Taxes, other than income tax	(1,138,598)	(815,796)
Membership fees	(1,154,379)	(675,118)
Security expenses	(990,763)	(761,886)
Repairs and maintenance expenses	(787,629)	(622,311)
Professional services fees	(752,023)	(305,840)
Advertising and marketing expenses	(650,228)	(609,486)
Insurance	(577,516)	(548,412)
Transportation and business trip expenses	(470,639)	(376,476)
Communications	(395,729)	(755,870)
Utilities	(341,921)	(322,203)
Entertainment	(269,276)	(186,888)
Stationery expenses	(222,194)	(242,262)
Other expenses	(1,005,617)	(740,300)
Total general and administrative expenses	**(13,863,957)**	**(12,115,114)**

11. Income taxes

The Group provides for taxes based on the tax accounts maintained and prepared in accordance with the tax regulations of countries where the Group and its subsidiaries operate and which may differ from International Financial Reporting Standards.

The Group is subject to certain permanent tax differences due to non-tax deductibility of certain expenses and a tax free regime for certain income. The statutory income tax rate is 20%.

Deferred taxes reflect the net tax effects of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for tax purposes.

Temporary differences as at 31 December 2018 and 2017 relate mostly to different methods of income and expense recognition as well as to recorded values of certain assets.

Temporary differences as at 31 December 2018 and 2017 comprise:

	31 December 2018	31 December 2017
Deductible temporary differences:		
Allowance for loan impairment	19,188,248	9,313,552
Other liabilities	3,383,366	2,502,887
Amortization	585,880	453,314
Investment securities	85,790	-
Other assets	-	107,055
Total deductible temporary differences	23,243,284	12,376,808
Taxable temporary differences:		
Depreciation	(12,423,595)	(11,247,653)
Precious metals	(8,142,647)	(8,417,680)
Provision for impairment losses on other operations	(336,959)	-
Amounts due from credit institutions	(107,645)	-
Other assets	(14,172,038)	-
Total deductible temporary differences	(35,182,884)	(19,665,333)
Net deferred (taxable) / deductible temporary differences	(11,939,600)	(7,288,525)
Net deferred tax (liability) / asset at the statutory tax rate (20%)	(2,387,920)	(1,457,705)
Net deferred tax (liability) / asset	**(2,387,920)**	**(1,457,705)**

Relationships between tax expenses and accounting profit for the years ended 31 December 2018 and 2017 are explained as follows:

	Year ended 31 December 2018	Year ended 31 December 2017
Profit before income tax	**31,579,667**	**20,990,723**
Tax at the statutory tax rate of 20%	6,315,933	4,198,145
Tax effect of permanent differences	38,054	(149,580)
Income tax expense	**6,353,987**	**4,048,565**
Current income tax expense	7,080,319	3,799,798
Deferred income tax expense / (benefit)	(726,332)	248,767
Income tax expense	**6,353,987**	**4,048,565**

Deferred income tax liability	31 December 2018	31 December 2017
Beginning of the period	**(1,457,705)**	**(1,208,938)**
Effect of adoption of IFRS 9	(1,656,547)	-
Change in the income tax assets for the period charged to profit	726,332	(248,767)
End of the period	**(2,387,920)**	**(1,457,705)**

12. Earnings per share

The earnings per share are calculated as follows:

	Year ended 31 December 2018	Year ended 31 December 2017
Profit:		
Net profit for the year	25,221,584	16,940,080
Weighted average number of ordinary shares for basic earnings per share	3,630,300	3,630,300
Earnings per share – basic and diluted (AZN)	**6.948**	**4.666**

13. Cash and cash equivalents

Cash and cash equivalents comprise:

	31 December 2018	31 December 2017
Cash on hand	42,947,648	36,056,016
Correspondent accounts with the Central Bank of Azerbaijan Republic	40,119,798	7,708,702
Correspondent accounts with other banks	85,595,281	53,308,212
Time deposits with Central Bank of Azerbaijan Republic up to 15 days	109,546,785	10,012,083
Total cash and cash equivalents	**278,209,512**	**107,085,013**

As at 31 December 2018 and 2017 accrued interest income included in cash and cash equivalents amounted to AZN 265,121 and AZN 12,083, respectively.

For the purpose of ECL measurement cash and cash equivalent balances are included in Stage 1. The ECL for these balances represents an insignificant amount, therefore the Group did not create any credit loss allowance for cash and cash equivalents.

14. Amounts due from credit institutions

Amounts due from credit institutions comprise:

	31 December 2018	31 December 2017
Loans and time deposits with other banks	40,890,716	36,586,982
Obligatory reserve with the Central Bank of Azerbaijan Republic	10,156,520	8,572,410
Restricted deposits	15,525,045	17,491,406
	66,572,281	**62,650,798**
Less: allowance for impairment	(132,316)	(417,914)
Total amounts due from credit institutions	**66,439,965**	**62,232,884**

As at 31 December 2018 and 2017 accrued interest income included in due from credit institutions amounted to AZN 63,054 and AZN 10,778, respectively.

As at 31 December 2018 and 2017 the Bank had restricted deposits blocked in support of guarantees issued and plastic cards operations and money transfers totaling AZN 15,525,045 and AZN 17,491,406, respectively.

An analysis of changes in gross carrying value and corresponding ECL allowance on amounts due from credit institutions during the year ended 31 December 2018 is as follows:

	Stage 1	*Stage 2*	*Stage 3*	*Total*
Gross carrying value as at 1 January 2018	**62,650,798**	-	-	**62,650,798**
New assets originated	32,696,157	-	-	**32,696,157**
Assets repaid				
- Principal	*(27,015,195)*	-	-	***(27,015,195)***
- Interest	*(292,941)*	-	-	***(292,941)***
Unwinding of discount	347,318	-	-	**347,318**
Amounts written off	-	-	-	-
Foreign exchange adjustments	(1,813,856)	-	-	**(1,813,856)**
At 31 December 2018	**66,572,281**	-	-	**66,572,281**

	Stage 1	*Stage 2*	*Stage 3*	*Total*
ECL as at 1 January 2018	**(4,179)**	-	-	**(4,179)**
New assets originated	(130,702)	-	-	**(130,702)**
Assets repaid				
- Principal	*2,640*	-	-	***2,640***
- Interest	*4,931*	-	-	***4,931***
Unwinding of discount	(4,932)	-	-	**(4,932)**
Changes to models and inputs used for ECL calculations	(235)	-	-	**(235)**
Amounts written off	-	-	-	-
Foreign exchange adjustments	161	-	-	**161**
At 31 December 2018	**(132,316)**	-	-	**(132,316)**

Movements in allowances for impairment for the year ended 31 December 2017 and the impact of adopting IFRS 9 are disclosed in Note 6.

15. Loans to customers

Loans to customers comprise:

	31 December 2018	31 December 2017
Loans to corporate customers	1,242,821,009	1,166,668,374
Loans to individuals	207,664,914	208,374,011
Gross loans to customers at amortised cost	**1,450,485,923**	**1,375,042,385**
Less allowance for impairment	(118,274,889)	(111,837,455)
Total loans to customers at amortised cost	**1,332,211,034**	**1,263,204,930**

As at 31 December 2018 and 2017 accrued interest income included in loans to customers amounted to AZN 53,889,819 and AZN 52,427,677, respectively.

An analysis of changes in the gross carrying value and corresponding ECL in relation to loans to corporate customers during the year ended 31 December 2018 is as follows:

Corporate customers	*Stage 1*	*Stage 2*	*Stage 3*	*Total*
Gross carrying value as at 1 January 2018	**757,673,714**	**2,561,093**	**406,433,567**	**1,166,668,374**
New assets originated	544,985,632	-	32,286,590	**577,272,222**
Assets repaid				
- Principal	*(342,101,160)*	*(115,746)*	*(164,722,992)*	***(506,939,898)***
- Interest	*(42,192,141)*	*(227,812)*	*(15,069,549)*	***(57,489,502)***
Transfers to Stage 1	-	-	-	-
Transfers to Stage 2	-	-	-	-
Transfers to Stage 3	(479,809)	(2,449,447)	2,929,256	-
Unwinding of discount	42,560,220	232,056	24,731,296	**67,523,572**
Recoveries	-	-	-	-
Amounts written off	-	-	(3,133,376)	**(3,133,376)**
Foreign exchange adjustments	(734,986)	(144)	(345,253)	**(1,080,383)**
At 31 December 2018	**959,711,470**	**-**	**283,109,539**	**1,242,821,009**

Corporate customers	*Stage 1*	*Stage 2*	*Stage 3*	*Total*
ECL as at 1 January 2018	**(719,352)**	**(155,117)**	**(62,902,770)**	**(63,777,239)**
New assets originated	(390,731)	-	(2,322,827)	**(2,713,558)**
Assets repaid				
- Principal	*167,622*	*8,625*	*13,451,559*	***13,627,806***
- Interest	*61,664*	*15,417*	*3,244,562*	***3,321,643***
Transfers to Stage 1	-	-	-	-
Transfers to Stage 2	-	-	-	-
Transfers to Stage 3	34,735	166,661	(201,396)	-
Impact on period end ECL of exposures transferred between stages during the period	(32,155)	(19,702)	-	**(51,857)**
Unwinding of discount	(62,904)	(15,894)	(9,489,100)	**(9,567,898)**
Changes to models and inputs used for ECL calculations	79,378	-	(36,800,494)	**(36,721,116)**
Recoveries	-	-	-	-
Amounts written off	-	-	3,133,376	**3,133,376**
Foreign exchange adjustments	377	10	25,800	**26,187**
At 31 December 2018	**(861,366)**	**-**	**(91,861,290)**	**(92,722,656)**

An analysis of changes in the gross carrying value and corresponding ECL in relation to loans to individuals during the year ended 31 December 2018 is as follows:

Individuals	*Stage 1*	*Stage 2*	*Stage 3*	*Total*
Gross carrying value as at 1 January 2018	**132,634,406**	**2,655,176**	**73,084,429**	**208,374,011**
New assets originated	213,984,297	105,598	39,127	**214,129,022**
Assets repaid				
- Principal	*(179,542,691)*	*(508,322)*	*(28,243,778)*	***(208,294,791)***
- Interest	*(10,310,440)*	*(195,595)*	*(6,390,102)*	***(16,896,137)***
Transfers to Stage 1	1,550,776	(1,380,010)	(170,766)	**-**
Transfers to Stage 2	(430,350)	430,350	-	**-**
Transfers to Stage 3	(107,298)	(681,157)	788,455	**-**
Unwinding of discount	10,356,162	184,503	7,830,844	**18,371,509**
Recoveries				
Amounts written off	-	-	(7,398,313)	**(7,398,313)**
Foreign exchange adjustments	(3,135)	(5)	(617,247)	**(620,387)**
At 31 December 2018	**168,131,727**	**610,538**	**38,922,649**	**207,664,914**

Individuals	*Stage 1*	*Stage 2*	*Stage 3*	*Total*
ECL as at 1 January 2018	**(206,627)**	**(403,428)**	**(39,488,164)**	**(40,098,219)**
New assets originated	(214,826)	(80)	(3,672)	**(218,578)**
Assets repaid				
- Principal	*99,206*	*29,336*	*11,531,635*	***11,660,177***
- Interest	*58,629*	*19,375*	*4,747,502*	***4,825,506***
Transfers to Stage 1	(16,410)	15,268	1,142	**-**
Transfers to Stage 2	93,670	(93,670)	-	**-**
Transfers to Stage 3	29,181	198,466	(227,647)	**-**
Impact on period end ECL of exposures transferred between stages during the period	(131,412)	150,969	50,477	**70,034**
Unwinding of discount	(327,260)	(7,383)	(5,700,042)	**(6,034,685)**
Changes to models and inputs used for ECL calculations	(232,581)	(11,826)	(3,288,479)	**(3,532,886)**
Recoveries	-	-	-	**-**
Amounts written off	-	-	7,398,313	**7,398,313**
Foreign exchange adjustments	57	3	378,045	**378,105**
At 31 December 2018	**(848,373)**	**(102,970)**	**(24,600,890)**	**(25,552,233)**

A reconciliation of the allowance for impairment of loans to customers by class during the year ended 31 December 2017 is as follows:

	Corporate loans	**Individuals**	**Total**
At 1 January 2017	**(75,173,261)**	**(30,419,658)**	**(105,592,919)**
Charge for the year	(14,349,915)	(11,861,559)	(26,211,474)
Amounts written off	18,428,445	1,538,493	19,966,938
At 31 December 2017	**(71,094,731)**	**(40,742,724)**	**(111,837,455)**

Impact of adopting IFRS 9 for the year ended 31 December 2017 are disclosed in Note 6.

As at 31 December 2017 loans to customers included loans in amount of AZN 174,807,381 that were individually determined to be impaired.

Loans are made in the following industry sectors:

Analysis by industry	**31 December 2018**	**31 December 2017**
Construction	364,751,270	494,271,135
Telecommunication	226,706,489	186,561,702
Individuals	207,664,914	208,374,011
Energy	180,568,059	15,405,739
Agriculture	129,472,169	122,263,196
Mining	126,734,433	148,007,306
Manufacturing	84,056,932	51,339,531
Trading	76,525,532	99,786,533
Other	54,006,125	49,033,232
	1,450,485,923	1,375,042,385
Less allowance for impairment	(118,274,889)	(111,837,455)
Total loans to customers	**1,332,211,034**	**1,263,204,930**

Loans to individuals comprise the following products:

	31 December 2018	**31 December 2017**
Mortgage loans	116,098,553	113,570,814
Consumer loans	55,765,196	30,086,850
Business loans	32,023,875	62,450,937
Auto loans	3,101,550	1,699,899
Credit cards	675,740	565,511
	207,664,914	208,374,011
Less allowance for impairment	(25,552,233)	(40,742,724)
Total loans to individuals	**182,112,681**	**167,631,287**

The table below summarizes the amount of loans secured by collateral, rather than the fair value of the collateral itself:

	31 December 2018	**31 December 2017**
Loans collateralized by real estate	668,513,749	645,878,033
Loans collateralized by cash	154,564,618	159,231,827
Loans collateralized by equipment	150,847,270	202,821,930
Loans collateralized by guarantees	93,991,980	135,471,967
Loans collateralized by vehicles	3,674,389	1,849,807
Loans collateralized by trade receivable	1,865,015	12,316,019
Unsecured loans	377,028,902	217,472,802
	1,450,485,923	1,375,042,385
Less allowance for impairment	(118,274,889)	(111,837,455)
Total loans to customers	**1,332,211,034**	**1,263,204,930**

As at 31 December 2018 and 2017 the Bank granted 11 and 11 loans totaling AZN 786,098,661 and AZN 776,255,300, respectively, which individually exceeded 10% of the Group's equity.

As at 31 December 2018 and 2017 loans to customers included loans in amount of AZN 261,271,476 and AZN 335,129,233, respectively, whose terms have been renegotiated.

As at 31 December 2018 and 2017, 61% and 60% of total amount of loans to customers are given to 14 and 12 entities, respectively.

A significant amount of loans (100% of loans to customers) is granted to companies operating in the Republic of Azerbaijan, which represents significant geographical concentration in one region.

16. Forfeiting

Forfeiting comprise:

	31 December 2018	31 December 2017
Forfeiting operations with customers	-	4,589,966
Less allowance for impairment losses	-	(91,799)
Total forfeiting	**-**	**4,498,167**

Movements in allowances for impairment for the year ended 31 December 2017 are disclosed in Note 6.

17. Investment securities

Investment securities comprise:

	31 December 2018	31 December 2017
Equity securities at FVOCI	447,258	179,650
Debt securities at amortised cost	165,074,412	236,644,596
Total investment securities	**165,521,670**	**236,824,246**

As at 31 December 2018 and 2017 accrued interest income included in investments securities amounted to AZN 1,057,578 and AZN 1,303,289, respectively.

Equity securities at FVOCI	**Share %**	**31 December 2018**	**Share %**	**31 December 2017**
Azerbaijan Credit Bureau LLC	12.5	250,000	-	-
Baku Stock Exchange CJSC	4.76	135,000	4.76	135,000
Millikart LTD	1	40,000	1	40,000
Boradigah Cay-2 OJSC	2.55	17,800		-
SWIFT SCRL		4,458		4,650
Total equity securities		**447,258**		**179,650**

Debt securities at amortised cost	**Coupon rate**	**31 December 2018**	**Coupon rate**	**31 December 2017**
Notes issued by Central Bank of Azerbaijan Republic	8%	122,419,900	15%	194,137,077
Bonds issued by SOCAR	5%	27,448,641	5%	27,450,256
Eurobonds issued by CJSC Southern Gas Corridor (SGC)	7%	14,903,551	7%	15,019,357
Bonds issued by Ministry of Finance of the Republic of Azerbaijan	10%	368,110	15%	37,906
Notes issued by other organisations	12%	20,000		-
		165,160,202		236,644,596
Less: allowance for impairment		(85,790)		-
Total debt securities		**165,074,412**		**236,644,596**

An analysis of changes in the gross carrying values and associated ECLs in relation to debt securities at amortized cost is as follows:

Debt securities at amortised cost	*Central Bank of the AR*	*SOCAR*	*SGC and others*	*Total*
Gross carrying value as at 1 January 2018	**194,137,077**	**27,450,256**	**15,057,263**	**236,644,596**
New assets originated or purchased	1,901,984,207	-	12,294,985	**1,914,279,192**
Assets repaid				
- *Principal*	(1,973,450,863)	-	(5,586,845)	**(1,979,037,708)**
- *Interest*	(12,833,014)	(1,358,490)	(974,695)	**(15,166,199)**
Assets sold	-	-	(6,388,351)	**(6,388,351)**
Unwinding of discount (recognised in interest income)	12,582,493	1,358,486	890,195	**14,831,174**
Amounts written off	-	-	-	
Foreign exchange adjustments	-	(1,611)	(891)	**(2,502)**
At 31 December 2018	**122,419,900**	**27,448,641**	**15,291,661**	**165,160,202**

Debt securities at amortised cost	*Central Bank of the AR*	*SOCAR*	*SGC and others*	*Total*
ECLs as at 1 January 2018	**(19,687)**	**(122,923)**	**(17,527)**	**(160,137)**
New assets originated or purchased	(192,423)	-	(13,432)	**(205,855)**
Assets repaid				
- *Principal*	199,653	-	5,881	**205,534**
- *Interest*	1,298	3,137	662	**5,097**
Assets sold	-	-	7,580	**7,580**
Unwinding of discount (recognised in interest revenue)	(1,273)	(3,137)	(614)	**(5,024)**
Changes to models and inputs used for ECL calculations	47	59,527	7,434	**67,008**
Amounts written off	-	-	-	**-**
Foreign exchange adjustments	-	4	3	**7**
At 31 December 2018	**(12,385)**	**(63,392)**	**(10,013)**	**(85,790)**

All balances of investment securities are allocated to Stage 1.

Movements in allowances for impairment for the year ended 31 December 2017 and the impact of adopting IFRS 9 are disclosed in Note 6.

In 2018, the Group received dividends of AZN 24,000 from Baku Stock Exchange CJSC which was recorded in the consolidated statement as other income.

18. Premises, equipment and intangible assets

	Land	Buildings	Computers	Vehicles	Furniture & Equipment	Other Equipment	Construction in progress	Total Premises & Equipment	Intangible Assets	Total
Cost at 31 December 2016	1,095,138	73,675,455	4,739,624	4,312,835	11,266,258	1,052,433	759,131	**96,900,874**	3,459,851	**100,360,725**
Additions	-	1,484	161,724	2,722,593	1,070,699	448,553	204,018	**4,609,071**	135,091	**4,744,162**
Disposals	-	-	(20,686)	(860,500)	(39,689)	(8,142)	(1,970)	**(930,987)**	-	**(930,987)**
Transfers	-	710,151	-	-	-	-	(710,151)	**-**	-	**-**
Cost at 31 December 2017	1,095,138	74,387,090	4,880,662	6,174,928	12,297,268	1,492,844	251,028	**100,578,958**	3,594,942	**104,173,900**
Additions	-	1,046	195,765	1,096,438	1,001,162	63,231	555,691	**2,913,333**	325,340	**3,238,673**
Disposals	-	-	(3,109)	(301,180)	(22,656)	-	-	**(326,945)**	-	**(326,945)**
Transfers	-	66,403	-	-	-	-	(66,403)	**-**	-	**-**
Cost at 31 December 2018	1,095,138	74,454,539	5,073,318	6,970,186	13,275,774	1,556,075	740,316	**103,165,346**	3,920,282	**107,085,628**
Accumulated Depreciation at 31 December 2016	-	(12,225,677)	(3,629,294)	(3,316,136)	(8,820,719)	(721,594)	-	**(28,713,420)**	(1,716,932)	**(30,430,352)**
Charge for the year	-	(2,455,740)	(310,040)	(571,875)	(1,122,170)	(68,558)	-	**(4,528,383)**	(326,040)	**(4,854,423)**
Disposals	-	-	20,673	809,042	39,624	8,142	-	**877,481**	-	**877,481**
Transfers	-	-	-	-	-	-	-	**-**	-	**-**
Accumulated Depreciation at 31 December 2017	-	(14,681,417)	(3,918,661)	(3,078,969)	(9,903,265)	(782,010)	-	**(32,364,322)**	(2,042,972)	**(34,407,294)**
Charge for the year	-	(2,476,522)	(253,484)	(655,690)	(992,123)	(135,009)	-	**(4,512,828)**	(365,655)	**(4,878,483)**
Disposals	-	-	3,109	257,750	22,656	-	-	**283,515**	-	**283,515**
Transfers	-	-	-	-	-	-	-	**-**	-	**-**
Accumulated Depreciation at 31 December 2018	-	(17,157,939)	(4,169,036)	(3,476,909)	(10,872,732)	(917,019)	-	**(36,593,635)**	(2,408,627)	**(39,002,262)**
NBV at 31 December 2017	**1,095,138**	**59,705,673**	**962,001**	**3,095,959**	**2,394,003**	**710,834**	**251,028**	**68,214,636**	**1,551,970**	**69,766,606**
NBV at 31 December 2018	**1,095,138**	**57,296,600**	**904,282**	**3,493,277**	**2,403,042**	**639,056**	**740,316**	**66,571,711**	**1,511,655**	**68,083,366**

19. Investment properties

Investment properties comprise:

	31 December 2018	31 December 2017
Investment property at fair value at beginning of the year	6,825,306	6,783,500
Fair value gains	201,940	41,806
Investment properties at fair value at end of the year	7,027,246	6,825,306

The fair value of investment property as at 31 December 2018 was determined on 19 March 2019 by AIS Azintellektservice, who holds a recognized professional qualification. The basis used for the appraisal was market value.

	Year ended 31 December 2018	Year ended 31 December 2017
Rental income derived from investment properties	**359,368**	**359,029**
Direct operating expenses arising from investment property that generated rental income	(322,192)	(296,052)
Direct operating expenses arising from investment property that did not generate rental income	(15,682)	(15,569)
	21,494	**47,408**

20. Other assets

Other assets comprise:

	31 December 2018	31 December 2017
Other financial assets		
Settlements on money transfers and plastic cards	3,846,188	4,257,246
Accrued interests on other operations	20,447	-
Other non-financial assets		
Collateral repossessed	60,716,298	27,123,491
Deferred expenses	777,336	913,771
Prepaid operating leases	538,602	623,253
Prepayments and receivables on other transactions	494,123	1,482,539
Prepayments for purchase of property and equipment	217,860	160,719
Prepaid operating taxes	218,584	3,362,809
Prepayments for purchases of intangible assets	181,818	359,363
Other	231,800	38,823
	67,243,056	38,322,014
Less: Provision for impairment of other non-financial assets	(7,976,732)	(11,299,624)
Total other assets	**59,266,324**	**27,022,390**

The movements in provision for impairment losses on other non-financial assets were as follows:

	Other non-financial assets
31 December 2016	**(4,685,784)**
Provision	(6,613,840)
31 December 2017	**(11,299,624)**
Recovery of provision	3,039,742
Write-off	283,150
31 December 2018	(7,976,732)

21. Amounts due to banks and government agencies

Amounts due to banks and government agencies comprise:

	31 December 2018	**31 December 2017**
Amount due to the National Fund for Support of Entrepreneurship	127,381,325	114,122,893
Long-term deposits from banks	103,800,00	85,005,000
Short-term deposits from banks	-	10,200,600
Amount due to Azerbaijan Mortgage Fund	57,561,707	53,584,891
Amount due to State Oil Company of Azerbaijan Republic	34,684,907	33,883,773
Loans from the Central Bank of Azerbaijan Republic	24,091,778	31,491,778
Correspondent accounts of other banks	20,617,783	25,645,162
Amount due to the National Depository Center	8,020,133	2,708,699
Total amounts due to banks and government agencies	**376,157,633**	**356,642,796**

As at 31 December 2018 and 2017 accrued interest expense included in due to banks and government agencies amounted to AZN 234,280 and AZN 209,016, respectively.

22. Customer accounts

Customer accounts comprise:

	31 December 2018	**31 December 2017**
Time deposits	859,949,574	949,788,266
Repayable on demand	475,085,212	233,668,214
Total customer accounts	**1,335,034,786**	**1,183,456,480**

As at 31 December 2018 and 2017 accrued interest expense included in customer accounts amounted to AZN 775,553 and AZN 763,978, respectively.

As at 31 December 2018 and 2017 customer accounts amounting to AZN 1,004,262,036 and AZN 915,087,508 were due to 16 and 14 customers representing a significant concentration, being approximately 75% and 77%, respectively.

An analysis of customer accounts by economic sector follows:

	31 December 2018	31 December 2017
Individuals	734,096,585	780,877,314
Investing	245,735,318	177,452,950
Energy	143,107,979	72,988,268
Transport and communication	67,064,753	65,733,577
Insurance	44,913,408	47,555,189
Trade	31,706,733	8,994,600
Construction	29,493,369	4,907,531
Manufacturing	18,178,382	5,422,041
Agriculture	6,941,275	16,133,288
State institutions	6,040,272	1,168,243
Other	7,756,712	2,223,479
Total customer accounts	**1,335,034,786**	**1,183,456,480**

23. Other liabilities

Other liabilities comprise:

	31 December 2018	31 December 2017
Other financial liabilities		
Settlements on money transfers and plastic cards	1,768,468	1,583,012
Professional fees payable	107,262	53,100
Accrued expenses	76,254	85,443
Other non-financial liabilities		
Payables to the employees	3,276,740	2,450,423
Payables to the Deposit Insurance Fund	880,254	948,823
Taxes other than income tax	733,992	549,041
Deferred revenue	32,229	1,570,283
Other	212,372	324,221
Total other liabilities	**7,087,571**	**7,564,346**

24. Share capital

As at 31 December 2018 and 2017 the Banks's authorized, issued and fully paid capital amounted to AZN 225,078,600 comprising of 3,630,300 ordinary shares with a par value of AZN 62 per ordinary share. Each share entitles one vote to the shareholder.

Movements in ordinary shares outstanding, issued and fully paid were as follows:

	Nominal price of one share	Number of ordinary shares	Share capital AZN
31 December 2016	**58.30**	**3,630,300**	**211,646,490**
Capitalization of retained earnings	3.70	-	13,432,110
31 December 2017	**62.00**	**3,630,300**	**225,078,600**
Increase in share capital	-	-	-
31 December 2018	**62.00**	**3,630,300**	**225,078,600**

On 25 September 2018 Shareholders of the Bank declared dividends in the amount of AZN 5,989,995 on ordinary shares which was paid as at 31 December 2018.

25. Commitments and contingencies

In the normal course of business, the Group is a party to financial instruments with off-balance sheet risk in order to meet the needs of its customers. These instruments, involving varying degrees of credit risk, are not reflected in the consolidated statement of financial position.

As at 31 December 2018 and 2017, the Group's commitments and contingencies comprised the following:

	31 December 2018	31 December 2017
Credit related commitments		
Unused credit lines	192,524,895	58,656,136
Letters of credit	1,701,816	10,399,073
Financial guarantees	22,029,552	11,819,153
	216,256,263	**80,874,362**
Operating lease commitments		
Not later than 1 year	296,874	296,874
Later than 1 year but not later than 5 years	1,187,497	1,187,497
Later than 5 years	219,809	516,683
	1,704,180	**2,001,054**
Performance guarantees	**24,322,271**	**13,893,396**
Commitments and contingencies before deducting collateral and provision	**242,282,714**	**96,768,812**
Less: provisions for ECL for credit related commitments	(61,703)	(203,376)
Less: cash held as security against letters of credit and guarantees	(21,896,159)	(24,336,841)
Commitments and contingencies	**220,324,852**	**72,228,595**

An analysis of changes in the ECL allowance during the year ended 31 December 2018 is as follows: .

	Stage 1	*Stage 2*	*Stage 3*	*Total*
ECL as at 1 January 2018	**(19,843)**	**(4)**	**(116,390)**	**(136,237)**
New exposures	(6,663)	-	-	**(6,663)**
Amounts paid	16,077	-	223	**16,300**
Expired exposures	275	4	64,276	**64,555**
Transfers to Stage 1	-	-	-	**-**
Transfers to Stage 2	-	-	-	**-**
Transfers to Stage 3	427	-	(427)	**-**
Changes to models and inputs used for ECL calculations	(85)	-	(20,936)	**(21,021)**
Amounts written off			21,363	**21,363**
At 31 December 2018	**(9,812)**	**-**	**(51,891)**	**(61,703)**

Movements in allowances for impairment for the year ended 31 December 2017 and the impact of adopting IFRS 9 are disclosed in Note 6.

Capital commitments – The Group had no material commitments for capital expenditures outstanding as at 31 December 2018.

Legal proceedings - From time to time and in the normal course of business, claims against the Group are received from customers and counterparties. Management is of the opinion that no material unaccrued losses will be incurred and accordingly no provision has been made in these consolidated financial statements.

Taxes - Azerbaijan commercial legislation and tax legislation in particular may give rise to varying interpretations and amendments. In addition, as management's interpretation of tax legislation may differ from that of the tax authorities, transactions may be challenged by the tax authorities, and as a result the Group may be assessed additional taxes, penalties and interest. Tax years remain open to review by the tax authorities for three years. Management believes that the Group has already made all tax payments that are due, and therefore no provisions have been made in these consolidated financial statements for any potential liabilities.

Pensions and retirement plans - Employees receive pension benefits from the Republic of Azerbaijan in accordance with the laws and regulations of the country. As at 31 December 2018 the Group was not liable for any supplementary pensions, post-retirement health care, insurance benefits, or retirement indemnities to its current or former employees.

Operating environment - The Group's principal business activities are within Azerbaijan. Laws and regulations affecting the business environment in Azerbaijan are subject to rapid changes and the Group's assets and operations could be at risk due to negative changes in the political and business environment.

26. Transactions with related parties

Related parties or transactions with related parties in the Group, as defined by IAS 24 "Related party disclosures", represent:

(a) Parties that directly, or indirectly through one or more intermediaries: control, or are controlled by, or are under common control with, the Group (this includes parents, subsidiaries and fellow subsidiaries); have an interest in the Group that gives then significant influence over the Group; and that have joint control over the Group;

(b) Associates – enterprises in which the Group has significant influence and which is neither a subsidiary nor a joint venture of the investor;

(c) Members of key management personnel of the Group or its parent;

(d) Close members of the family of any individuals referred to in (a) or (c);

(e) Parties that are entities controlled, jointly controlled or significantly influenced by, or for which significant voting power in such entity resides with, directly or indirectly, any individual referred to in (c) or (d).

In considering each possible related party relationship, attention is directed to the substance of the relationship, and not merely the legal form. The Group had the following transactions outstanding as at 31 December 2018 and 2017 with related parties:

	31 December 2018		31 December 2017	
	Related party transactions	**Total category as per financial statements caption**	**Related party transactions**	**Total category as per financial statements caption**
Loans to customers		1,450,485,923		1,375,042,385
- shareholders and entities in which a substantial interest is owned by shareholders of the Group	-		*54,574,685*	
- key management personnel of the entity	*803,950*		*770,353*	
Allowance for impairment losses		(118,274,889)		(111,837,455)
- shareholders and entities in which a substantial interest is owned by shareholders of the Group	-		*(1,051,272)*	
- key management personnel of the entity	*(1,385)*		*(7,283)*	
Customer accounts		1,335,034,786		1,183,456,480
- shareholders and entities in which a substantial interest is owned by shareholders of the Group	*54,365,749*		*83,871,364*	
- key management personnel of the entity	*1,422,576*		*1,141,950*	
Guarantees issued		46,351,823		25,712,549
- shareholders and entities in which a substantial interest is owned by shareholders of the Group	*612,010*		*612,010*	
Unused loan commitments		192,524,895		58,656,136
- shareholders and entities in which a substantial interest is owned by shareholders of the Group	-		17,911,990	
- key management personnel of the entity	*142,702*		*89,516*	

Included in the consolidated income statement for the years ended 31 December 2018 and 2017 are the following amounts which arose due to transactions with related parties:

	Year ended 31 December 2018		Year ended 31 December 2017	
	Related party transactions	**Total category as per financial statements caption**	**Related party transactions**	**Total category as per financial statements caption**
Interest income		109,399,694		100,130,599
- shareholders and entities in which a substantial interest is owned by shareholders of the Group	*-*		*3,623,609*	
- key management personnel of the entity	*77,519*		*66,677*	
Interest expense		(23,158,018)		(25,552,727)
- shareholders and entities in which a substantial interest is owned by shareholders of the Group	*(1,778,203)*		*(1,620,214)*	
- key management personnel of the entity	*(12,730)*		*(17,146)*	
Fee and commission income		7,563,645		7,996,651
- shareholders and entities in which a substantial interest is owned by shareholders of the Group	*11,851*		*114,631*	
- key management personnel of the entity	*232*		*1,097*	
Other income		954,049		1,104,813
- shareholders and entities in which a substantial interest is owned by shareholders of the Group	*438,792*		*420,792*	
General and administrative expenses		(13,863,957)		(12,115,114)
- shareholders and entities in which a substantial interest is owned by shareholders of the Group	*(598,937)*		*(607,363)*	

	Year ended 31 December 2018		Year ended 31 December 2017	
	Related party transactions	**Total category as per financial statements caption**	**Related party transactions**	**Total category as per financial statements caption**
Key management personnel compensation:				
short-term employee benefits	1,739,249	21,330,532	443,037	15,434,956

27. Fair value of financial instruments

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

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

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

	Level 1	Level 2	Level 3	31 December 2018 Total
Assets measured at fair value				
Investment securities	-	447,258	-	447,258
Investment property	-	7,027,246	-	7,027,246
Assets for which fair values are disclosed				
Cash and cash equivalents	168,662,727	-	109,546,785	278,209,512
Precious metals	14,989,411	-	-	14,989,411
Amounts due from credit institutions	24,441,524	-	41,998,441	66,439,965
Loans to customers	-	-	1,332,211,034	1,332,211,034
Investment securities	-	-	165,074,412	165,074,412
Other assets	-	-	3,846,188	3,846,188
Assets	**208,093,662**	**7,474,504**	**1,652,676,860**	**1,868,245,026**
Liabilities for which fair values are disclosed				
Amounts due to banks and government agencies	-	-	376,157,633	376,157,633
Customer accounts	475,085,212	-	859,949,574	1,335,034,786
Other liabilities	-	-	1,768,468	1,768,468
Liabilities	**475,085,212**	**-**	**1,237,875,675**	**1,712,960,887**

	Level 1	Level 2	Level 3	31 December 2017 Total
Assets measured at fair value				
Investment securities	-	179,650	-	179,650
Investment property	-	6,825,306	-	6,825,306
Assets for which fair values are disclosed				
Cash and cash equivalents	97,072,930	-	10,012,083	107,085,013
Precious metals	15,305,466	-	-	15,305,466
Amounts due from credit institutions	25,861,881	-	36,371,003	62,232,884
Loans to customers	-		1,263,204,930	1,263,204,930
Investment securities	-		236,644,596	236,644,596
Forfeiting			4,498,167	4,498,167
Other assets	-		4,257,246	4,257,246
Assets	**138,240,277**	**7,004,956**	**1,554,988,025**	**1,700,233,258**
Liabilities for which fair values are disclosed				
Amounts due to banks and government agencies	-	-	356,642,796	356,642,796
Customer accounts	233,668,214	-	949,788,266	1,183,456,480
Other liabilities	-	-	1,583,012	1,583,012
Liabilities	**233,668,214**	**-**	**1,308,014,074**	**1,541,682,288**

The fair value of financial assets and liabilities compared with the corresponding carrying amount in the consolidated statement of financial position of the Group is presented below:

	31 December 2018		31 December 2017	
	Carrying amount	**Fair value**	**Carrying amount**	**Fair value**
Cash and cash equivalents	278,209,512	278,209,512	107,085,013	107,085,013
Precious metals	14,989,411	14,989,411	15,305,466	15,305,466
Amounts due from credit institutions	66,439,965	66,439,965	62,232,884	62,232,884
Loans to customers	1,332,211,034	1,332,211,034	1,263,204,930	1,263,204,930
Investment securities	165,521,670	165,521,670	236,824,246	236,824,246
Other financial assets	3,846,188	3,846,188	4,257,246	4,257,246
Amounts due to banks and government agencies	376,157,633	376,157,633	356,642,796	356,642,796
Customer accounts	1,335,034,786	1,335,034,786	1,183,456,480	1,183,456,480
Other financial liabilities	1,768,468	1,768,468	1,583,012	1,583,012

The fair value of equity securities included in investment securities cannot be measured reliably. As at 31 December 2018 and 2017 the cost of them was AZN 447,258 and AZN 179,650, respectively. Since these shares are not publicly traded and the range of reasonable fair value estimates is significant, it is not possible to estimate their fair value.

Valuation techniques and assumptions

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

Assets for which fair value approximates carrying value

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

Investment securities

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

Financial assets and financial liabilities carried at amortized cost

The fair value of unquoted instruments, loans to customers, customer deposits, amounts due from credit institutions and amounts due to banks and government organizations and other financial assets and liabilities, obligations under finance leases is estimated by discounting future cash flows using rates currently available for debt on similar terms, credit risk and remaining maturities.

28. Regulatory matters

Quantitative measures established by regulation to ensure capital adequacy require the Group to maintain minimum amounts and ratios (as set forth in the table below) of total (10%) and tier 1 capital (5%) to risk weighted assets.

As at 31 December 2018 the Group's total capital amount for Capital Adequacy purposes was AZN 267,440,648 and tier 1 capital amount was AZN 265,348,129 with ratios of 15% and 15%, respectively.

As at 31 December 2017 the Group's total capital amount for Capital Adequacy purposes was AZN 256,100,240 and tier 1 capital amount was AZN 239,448,701 with ratios of 15% and 14%, respectively.

In addition, the Group has to maintain a statutory capital adequacy ratio based on the Central Bank of Azerbaijan Republic requirements. During the years ended 31 December 2018 and 2017 the Group was in compliance with the minimum capital requirements imposed by the Central Bank of Azerbaijan Republic.

29. Capital management

The Group manages its capital to ensure that entities in the Group will be able to continue as a going concern while maximising the return to stakeholders through the optimisation of the debt and equity balance.

The Management Board reviews the capital structure on a semi-annual basis. As a part of this review, the Board considers the cost of capital and the risks associated with each class of capital. Based on recommendations of the Board, the Group balances its overall capital structure through the payment of dividends, new share issues as well as the issue of new debt or the redemption of existing debt.

The Group's overall capital risk management policy remains unchanged from 2017.

30. Risk management policies

Management of risk is fundamental to the banking business and is an essential element of the Group's operations. The main risks inherent to the Group's operations are those related to credit exposures, liquidity and market movements in interest rates and foreign exchange rates. A description of the Group's risk management policies in relation to those risks follows. The Group manages the following risks:

Credit risk

Credit risk is the risk that the Group will incur a loss because its customers, clients or counterparties failed to discharge their contractual obligations. The Group 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 Group 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. The credit quality review process allows the Group to assess the potential loss as a result of the risks to which it is exposed and take corrective action.

Derivative financial instruments

Credit risk arising from derivative financial instruments is, at any time, limited to those with positive fair values, as recorded in the consolidated statement of financial position.

Credit-related commitments risks

The Group makes available to its customers guarantees which may require that the Group make payments on their behalf. Such payments are collected from customers based on the terms of the letter of credit. They expose the Bank to similar risks to loans and these are mitigated by the same control processes and policies.

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

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

Impairment assessment

From 1 January 2018, the Group calculates ECL based on several probability-weighted scenarios to measure the expected cash shortfalls, discounted at an approximation to the EIR. A cash shortfall is the difference between the cash flows that are due to an entity in accordance with the contract and the cash flows that the entity expects to receive. The mechanics of the ECL calculations are outlined below and the key elements are as follows:

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

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

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

Stage 1:	When loans are first recognised, the Group recognises an allowance based on 12mECL. Stage 1 loans also include facilities where the credit risk has improved and the loan has been reclassified from Stage 2 and Stage 3.
Stage 2:	When a loan has shown a significant increase in credit risk since origination, the Group records an allowance for the LTECL
Stage 3:	Loans considered credit-impaired. The Group records an allowance for the LTECL.
POCI:	Purchased or originated credit impaired (POCI) assets are financial assets that are credit impaired on initial recognition. POCI assets are recorded at fair value at original recognition and interest income is subsequently recognised based on a credit-adjusted EIR. ECL are only recognised or released to the extent that there is a subsequent change in the expected credit losses.

Definition of default and cure

A financial instrument impairment event is determined at the borrower level for all portfolios except for the retail borrowers' portfolio. For retail borrowers, the impairment event is determined at the financial instrument level. The Group considers a financial asset to be in default when:

- More than 90 calendar days of overdue debt at the reporting date for all segments except transactions with financial institutions and issuers of securities;
- More than 7 working days of overdue debt at the reporting date for transactions with financial institutions and issuers of securities;
- The counterparty / issuer was declared bankrupt by the court, or the court introduced bankruptcy procedures in relation to the borrower. This criterion applies to all portfolios with the exception of the portfolio of retail borrowers;
- Assignment of a regulatory quality category 4 or 5 to the contract at the reporting date;
- Default / forced restructuring due to the financial difficulties of the borrower (applicable except for transactions with financial institutions and securities). Default / forced restructuring refers to a change in the terms of a contract recognized as a forced restructuring by the Group, which are a consequence of the borrower's inability to perform the obligations specified in the contract, and are caused by a deterioration in the credit quality of the borrower;
- Revocation of the license and the introduction of an interim administration (applicable to financial institutions and issuers of securities).

If there is evidence that there is no longer a significant increase in credit risk relative to initial recognition, then the loss allowance on an instrument returns to being measured as 12-month ECL. Some qualitative indicators of an increase in credit risk, such as delinquency of forbearance, may be indicative of an increased risk of default that persists after the indicator itself has ceased to exist. In these cases, the Group determines a probation period during which the financial asset is required to demonstrated good behavior to provide evidence that its credit risk has declined sufficiently. Probation criteria for recovery and transfer of financial instruments to Stage 1 are as follows:

- No overdue debt (0 days overdue) for three consecutive reporting months for retail borrowers;
- No overdue debt or overdue indebtedness for twelve consecutive reporting months for corporate counterparties and individual entrepreneurs with annuity payments.

Generating the term structure of PD

The Group collects performance and default information about its credit risk by type of product as well as by borrower's segment. For some portfolios, information purchased from external credit reference agencies is also used.

The Group employs statistical models to analyze the data collected and generate estimates of the remaining lifetime PD of exposures and how these are expected to change as a result of the passage of time.

Treasury and interbank relationships

The Group's treasury and interbank relationships and counterparties comprise financial services institutions, banks, broker-dealers, exchanges and clearing-houses. For these relationships, the Group's credit risk department analyses publicly available information such as financial information and other external data, e.g., the external ratings, and assigns the internal rating, as shown in the table below.

Corporate and small business lending

For corporate loans, the borrowers are assessed by specialised credit risk employees of the Group. The credit risk assessment is based on a credit scoring model that takes into account various historical, current and forward-looking information such as:

- Historical financial information together with forecasts and budgets prepared by the client. This financial information includes realised and expected results, solvency ratios, liquidity ratios and any other relevant ratios to measure the client's financial performance. Some of these indicators are captured in covenants with the clients and are, therefore, measured with greater attention.
- Any publicly available information on the clients from external parties. This includes external rating grades issued by rating agencies, independent analyst reports, publicly traded bond prices or press releases and articles.
- Any other objectively supportable information on the quality and abilities of the client's management relevant for the company's performance.

The complexity and granularity of the rating techniques varies based on the exposure of the Group and the complexity and size of the customer. Some of the less complex small business loans are rated within the Group's models for retail products.

Consumer lending and residential mortgages

Consumer lending comprises unsecured personal loans, credit cards and overdrafts. These products along with residential mortgages and some of the less complex small business lending are rated by an automated scorecard tool primarily driven by debt to income (DTI), loan to value (LTV) and payment to income (PTI) ratios.

The Group's internal credit rating grades are as follows:

Internal rating grade	*International external rating agency (Fitch) rating*	*Internal rating description*	*Lifetime PD*
	AA+ to AAA		
	AA		
>13	A+ to AA-	High grade	0-0.06%
	A-		
	BBB+		
	BBB		
	BBB-		
8-13	BB+	Standard grade	0.06-0.45%
	BB to BB		
	B- to B+		
4-8	CCC	Sub-standard grade	0.45-100%
	CCC-		
<4	D	Impaired	100%

Measurement of ECL

The key inputs into the measurement of ECL are the term structure of the following variables:

- probability of default (PD);
- loss given default (LGD);
- exposure at default (EAD).

ECL for exposures in Stage 1 is calculated by multiplying the 12-month PD by LGD and EAD. Lifetime ECL is calculated by multiplying the lifetime PD by LGD and EAD.

The methodology of estimating PDs is discussed above under the heading "Generating the term structure of PD".

The Bank estimates LGD parameters based on the history of recovery rates of claims against defaulted counterparties. The LGD models consider repayments of principal and interest amounts for defaulted customers in each segment. In corporate portfolio, recovery amounts are computed on a customer base, while it in credit cards and consumer loan portfolios it is calculated on a contract level. They are calculated on a discounted cash flow basis using first available contractual rate as the discounting factor, as it is considered as the best proxy of effective interest rate at origination. For mortgage loans, haircut was applied to the collaterals.

EAD represents the expected exposure in the event of a default. The Bank derives the EAD from the current exposure to the counterparty and potential changes to the current amount allowed under the contract and arising from amortization. The EAD of a financial asset is its gross carrying amount at the time of default. For lending commitments, the EAD is potential future amounts that may be drawn under the contract, which are estimated based on historical observations.

As described above, and subject to using a maximum of a 12-month PD for Stage 1 financial assets, the Bank measures ECL considering the risk of default over the maximum contractual period (including any borrower's extension options) over which it is exposed to credit risk, even if, for credit risk management purposes, the Bank considers a longer period. The maximum contractual period extends to the date at which the Bank has the right to require repayment of an advance or terminate a loan commitment.

Significant increase in credit risk

The Group assesses whether credit risk has increased significantly since initial recognition at each reporting period. Determining whether an increase in credit risk is significant depends on the characteristics of the financial instrument and the borrower, and the geographical region. What is considered significant will differ for different types of lending, in particular between corporate and retail.

As a general indicator, credit risk of a particular exposure is deemed to have increased significantly since initial recognition if, based on the Group's qualitative criteria:

- the presence of the fact of overdue debt for 31-90 days for all segments except transactions with financial institutions and issuers of securities;
- the presence of the fact of debt overdue by 1-7 working days for transactions with financial institutions and issuers of securities;
- the presence of the fact of overdue debt more than 90 days under other agreements of the borrower for the retail portfolio;
- reduction of financial support from the parent company or another affiliated enterprise;
- the Group receives reliable negative information about products issued to the borrower.

Days past due are determined by counting the number of days since the earliest elapsed due date in respect of which full payment has not been received. Due dates are determined without considering any grace period that might be available to the borrower.

Quantitative criteria (are applied only in the presence of external ratings):

- The relative change in the external rating at the reporting date compared to the external rating at the recognition date according to the criteria given in table below.

Criteria for determining a significant increase in credit risk depending on the value of the external rating upon initial recognition.

	Counterparty external rating at initial recognition			**Significant increase in credit risk assigned:**
	Moody's	**Fitch**	**S&P**	
1	AAA	AAA	AAA	Low credit risk: criterion is not applied
2	Aa1	AA+	AA+	
3	Aa2	AA	AA	
4	Aa3	AA-	AA-	
5	A1	A+	A+	
6	A2	A	A	
7	A3	A-	A-	
8	Baa1	BBB+	BBB+	
9	Baa2	BBB	BBB	
10	Baa3	BBB-	BBB-	
11	Ba1	BB+	BB+	Decrease of rating by 2 notches
12	Ba2	BB	BB	
13	Ba3	BB-	BB-	
14	B1	B+	B+	Decrease of rating by 1 notch
15	B2	B	B	
16	B3	B-	B-	
17	Caa1	CCC-C	CCC-C	
18	Caa2			
19	Caa3			
20	Ca-C			
21	D	D	D	

Forward-looking information and multiple economic scenarios

In its ECL models, the Group relies on a broad range of forward looking information as economic inputs, such as:

- Real GDP;
- Consumer Price Index;
- Oil price;

The Group formulates one economic scenario: a base case. The base case is aligned with information used by the Group for other purposes such as strategic planning and budgeting. The historical data of defaults use the statistics of CBAR on the share of overdue loans in total loans to individuals in the banking system. The assessment of the impact of macroeconomic information should be made at least on an annual basis.

The Group has identified and documented key drivers of credit risk and credit losses for the entire loan portfolio (including the securities portfolio, requirements for financial institutions), using an analysis of historical data, has estimated relationships between macro-economic variables and credit risk and credit losses.

The key driver is Real GDP growth forecast. The economic scenarios used as at 31 December 2018 included the following key indicators for the Republic of Azerbaijan for the years ending 31 December 2019 through 2023.

Years	**Real GDP growth rate**
2019	3.50%
2020	3.20%
2021	2.40%
2022	2.40%
2023	2.30%

Predicted relationships between the key indicator and default and loss rates on various portfolios of financial assets have been developed based on analyzing historical data over the past 5 years.

Credit quality per class of financial assets

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

	Note		High grade	Standard grade	Sub-standard grade	Impaired	Total
Cash and cash equivalents, except for cash on hand	13	Stage 1	231,398,126	3,855,063	8,675	-	**235,261,864**
Amount due from credit institutions	14	Stage 1	47,695,724	18,876,556	-	-	**66,572,281**
Loans to customers at amortised cost	15						
Loans to corporate customers		Stage 1	68,000,000	809,959,255	81,752,215	-	**959,711,470**
		Stage 2				-	**-**
		Stage 3	-	-	-	283,109,539	**283,109,539**
-Loans to individuals							
Auto loans		Stage 1	-	2,656,987	87,442	-	**2,744,429**
		Stage 2	-	-	1,021	-	**1,021**
		Stage 3	-	-	-	356,099	**356,099**
Consumer loans		Stage 1	-	43,724,224	495,986	-	**44,220,210**
		Stage 2	-	-	17,900	-	**17,900**
		Stage 3	-	-	-	11,527,086	**11,527,086**
Mortgage loans		Stage 1	-	53,140,826	56,878,936	-	**110,019,762**
		Stage 2	-	-	492,781	-	**492,781**
		Stage 3	-	-	-	5,586,010	**5,586,010**
Credit cards		Stage 1	14,417	514,978	-	-	**529,395**
		Stage 2	-	98,835	-	-	**98,835**
		Stage 3	-	-	-	32,946	**32,946**
Business loans		Stage 1	-	10,312,277	305,657	-	**10,617,934**
		Stage 2	-	-	-	-	**-**
		Stage 3	-	-	-	21,420,506	**21,420,506**
Investment securities							
- Debt securities at amortised cost	17	Stage 1	137,691,561	27,448,641	20,000	-	**165,160,202**
Letters of credit	25	Stage 1	-	1,701,816	-	-	**1,701,816**
Financial guarantees	25	Stage 1	-	22,029,552	-	-	**22,029,552**
Undrawn loan commitments	25	Stage 1	485,980	189,852,324	1,235,427	-	**191,573,730**
		Stage 2	-	1,165	-	-	**1,165**
		Stage 3	-	-	-	950,000	**950,000**
Total			**485,285,808**	**1,184,172,499**	**141,296,040**	**322,982,187**	**2,133,736,533**

The table below shows gross balances under IAS 39 as at 31 December 2017 based on the Group's internal credit rating system:

	Neither past due nor impaired					
	High grade	**Standard grade**	**Sub-standard grade**	**Past due but not impaired**	***Individually impaired***	**Total**
Cash and cash equivalents, except for cash on hand	42,100,798	28,782,291	145,908	-	-	**71,028,997**
Amount due from credit institutions	45,575,916	17,074,882	-	-	-	**62,650,798**
Loans to customers	-	607,961,487	592,236,859	36,658	174,807,381	**1,375,042,385**
Forfeiting	-	4,589,966	-	-	-	**4,589,966**
Investment securities	-	236,644,596	-	-	-	**236,644,596**
Total	**87,676,714**	**895,053,222**	**592,382,767**	**36,658**	**174,807,381**	**1,749,956,742**

The following table details the carrying value of assets that are impaired and the ageing of those that are past due but not impaired:

		Financial assets past due but not impaired				31 December 2017	
	Neither past due nor impaired	**0-3 months**	**3-6 months**	**6 months to 1 year**	**Greater than one year**	**Financial assets that have been impaired**	**Total**
Cash and cash equivalents, except for cash on hand	71,028,997	-	-	-	-	-	71,028,997
Amounts due from credit institutions	62,650,798	-	-	-	-	-	62,650,798
Loans to customers	1,200,198,346	14,441	21,735	217	265	174,807,381	1,375,042,385
Forfeiting	4,589,966	-	-	-	-	-	4,589,966
Investments available for sale	236,644,596	-	-	-	-	-	236,644,596
Total	**1,575,112,703**	**14,441**	**21,735**	**217**	**265**	**174,807,381**	**1,749,956,742**

Maximum Exposure

The Groups maximum exposure to credit risk varies significantly and is dependant on both individual risks and general market economy risks. The following table presents the maximum exposure to credit risk of financial assets and contingent liabilities. For financial assets the maximum exposure equals to a carrying value of those assets prior to any offset or collateral. For financial guarantees and other contingent liabilities the maximum exposure to credit risk is the maximum amount the Group would have to pay if the guarantee was called on or in the case of commitments, if the loan amount was called on.

				31 December 2018
	Maximum exposure	**Net exposure after offset**	**Collateral Pledged**	**Net exposure after offset and collateral**
Amounts due from credit institutions	66,439,965	66,439,965	-	66,439,965
Loans to customers	1,332,211,034	1,177,646,416	800,617,514	377,028,902
Investment securities	165,521,670	165,521,670	165,054,412	467,258

	31 December 2017			
	Maximum exposure	**Net exposure after offset**	**Collateral Pledged**	**Net exposure after offset and collateral**
Amounts due from credit institutions	62,232,884	62,232,884	-	62,232,884
Loans to customers	1,263,204,930	1,103,973,103	886,500,301	217,472,802
Investment securities	236,824,246	236,824,246	236,644,596	179,650
Forfeiting	4,498,167	4,498,167	-	4,498,167

Geographical concentration

The Assets and Liabilities Management Committee exercises control over the risk in the legislation and regulatory arena and assess its influence on the Group's activity. This approach allows the Group to minimize potential losses from the investment climate fluctuations in the Republic of Azerbaijan. The Group's Management Board sets up country limits, which mainly applies to banks of the Commonwealth of Independent States and Baltic countries.

The geographical concentration of assets and liabilities is set out below:

	The Republic of Azerbaijan	**CIS and other countries**	**OECD countries**	**31 December 2018 Total**
Assets				
Cash and cash equivalents	192,882,568	1,253,034	84,073,910	278,209,512
Precious metals	14,989,411	-	-	14,989,411
Amounts due from credit institutions	17,403,531	-	49,036,434	66,439,965
Loans to customers	1,332,211,034	-	-	1,332,211,034
Investment securities	165,517,212	-	4,458	165,521,670
Property and equipment	66,571,711	-	-	66,571,711
Investment property	7,027,246	-	-	7,027,246
Intangible assets	1,511,655	-	-	1,511,655
Other assets	59,136,082	-	130,242	59,266,324
Total assets	**1,857,250,450**	**1,253,034**	**133,245,044**	**1,991,748,528**
Liabilities				
Amounts due to banks and government agencies	376,157,633	-	-	376,157,633
Customer accounts	1,335,034,786	-	-	1,335,034,786
Provision for impairment losses on other operations	61,703	-	-	61,703
Current income tax liability	4,159,131	-	-	4,159,131
Deferred income tax liability	2,387,920	-	-	2,387,920
Other liabilities	7,005,810	11	81,750	7,087,571
Total liabilities	**1,724,806,983**	**11**	**81,750**	**1,724,888,744**
Net position	**132,443,467**	**1,253,023**	**133,163,294**	

	The Republic of Azerbaijan	CIS and other countries	OECD countries	31 December 2017 Total
Assets				
Cash and cash equivalents	54,479,452	815,417	51,790,144	107,085,013
Precious metals	15,305,466	-	-	15,305,466
Amounts due from credit institutions	8,589,242	-	53,643,642	62,232,884
Loans to customers	1,263,204,930	-	-	1,263,204,930
Forfeiting	4,498,167	-	-	4,498,167
Investment securities	236,819,596	-	4,650	236,824,246
Property and equipment	68,214,636	-	-	68,214,636
Investment property	6,825,306	-	-	6,825,306
Intangible assets	1,551,970	-	-	1,551,970
Other assets	26,921,654	25,979	74,757	27,022,390
Total assets	**1,686,410,419**	**841,396**	**105,513,193**	**1,792,765,008**
Liabilities				
Amounts due to banks and government agencies	356,642,796	-	-	356,642,796
Customer accounts	1,183,456,480	-	-	1,183,456,480
Provision for impairment losses on other operations	203,376	-	-	203,376
Current income tax liability	2,439,634	-	-	2,439,634
Deferred income tax liability	1,457,705	-	-	1,457,705
Other liabilities	7,511,890	6,914	45,542	7,564,346
Total liabilities	**1,551,711,881**	**6,914**	**45,542**	**1,551,764,337**
Net position	**134,698,538**	**834,482**	**105,467,651**	

Liquidity risk

Liquidity risk refers to the availability of sufficient funds to meet deposit withdrawals and other financial commitments associated with financial instruments as they actually fall due. In order to manage liquidity risk, the Group performs daily monitoring of expected future cash flows on clients' and banking operations, which is a part of the assets/liabilities management process. The Assets and Liabilities Management Committee sets limits on the minimum proportion of maturing funds available to meet deposit withdrawals and on the minimum level of interbank and other borrowing facilities that should be in place to cover withdrawals at unexpected levels of demand.

An analysis of the liquidity and interest rate risks is presented in the following table. The tables have been drawn up to detail:

(i) The remaining contractual maturity of non-derivative financial liabilities based on the undiscounted cash flows of financial liabilities (both interest and principal cash flows) based on the earliest date on which the Group can be required to pay, and

(ii) The expected maturity for non-derivative financial assets based on the undiscounted contractual maturities of the financial assets including interest that will be earned on those assets except where the Group anticipates that the cash flow will occur in a different period.

	Weighted average effective interest rate	Up to 1 month	1 month to 3 months	3 month to 1 year	1 year to 5 years	Over 5 years	Maturity undefined	31 December 2018 Total
Assets								
Cash and cash equivalents	6.95%	127,981,664	-	-	-	-	-	127,981,664
Amounts due from credit institutions	1.64%	-	-	36,237,662	4,590,000	-	-	40,827,662
Loans to customers	5.62%	111,756,896	7,957,862	226,196,622	574,526,861	407,854,380	-	1,328,292,621
Investment securities	7.23%	121,780,587	-	20,000	27,531,205	14,685,043	-	164,016,834
Total interest bearing assets at fixed rates		233,537,483	7,957,862	262,454,284	606,648,066	422,539,422	-	1,533,137,117
Cash and cash equivalents		150,227,848	-	-	-	-	-	150,227,848
Precious metals		14,989,411			-	-	-	14,989,411
Amounts due from credit institutions		63,054					25,549,249	25,612,303
Loans to customers		1,929,422	-	-	-	-	1,988,991	3,918,413
Investment securities		-	1,057,578	-	-	-	447,258	1,504,836
Other assets		3,866,635	231,800	-	52,739,566	-	-	56,838,001
		404,613,853	**9,247,240**	**262,454,284**	**659,387,632**	**422,539,422**	**27,985,498**	**1,786,227,929**
Liabilities								
Amounts due to banks and government agencies	2.19%	11,800,000	87,200,000	54,442,280	54,666,929	147,196,361	-	355,305,570
Customer accounts	1.74%	10,276,350	163,322,838	286,144,116	398,182,747	-	-	857,926,051
Total interest bearing liabilities at fixed rates		22,076,350	250,522,838	340,586,396	452,849,676	147,196,361	-	1,213,231,621
Amounts due to banks and government agencies		20,852,063	-	-	-	-	-	20,852,063
Customer accounts		460,547,388	-	1,069,254	200,000	-	15,292,093	477,108,735
Current income tax liability		-	-	4,159,131	-	-	-	4,159,131
Other liabilities		2,724,976	841,254	3,521,341	-	-	-	7,087,571
Guarantees issued		3,836,589	2,868,543	20,569,143	19,077,547	-	-	46,351,823
Letters of credit		1,377,600	324,216	-	-	-	-	1,701,816
Undrawn loan commitments		59,540	1,582,795	128,699,259	62,183,301	-	-	192,524,895
		511,474,505	**256,139,647**	**498,604,524**	**534,310,524**	**147,196,361**	**15,292,093**	**1,963,017,655**
Liquidity gap		(106,860,653)	(246,892,406)	(236,150,240)	125,077,108	275,343,061		
Interest sensitivity gap for fixed rate instruments		211,461,133	(242,564,976)	(78,132,112)	153,798,390	275,343,061		
Interest sensitivity gap		211,461,133	(242,564,976)	(78,132,112)	153,798,390	275,343,061		
Cumulative interest sensitivity gap		**211,461,133**	**(31,103,843)**	**(109,235,955)**	**44,562,435**	**319,905,496**		

	Weighted average effective interest rate	Up to 1 month	1 month to 3 months	3 month to 1 year	1 year to 5 years	Over 5 years	Maturity undefined	31 December 2017 Total
Assets								
Cash and cash equivalents	14.50%	10,000,000	-	-	-	-	-	10,000,000
Amounts due from credit institutions	0.29%	10,574,243	14,987,055	11,014,905	-	-	-	36,576,204
Loans to customers	6.06%	17,939,490	1,742,835	237,643,592	597,088,244	404,026,267	-	1,258,440,427
Investment securities	9.86%	193,333,032	-	-	27,170,998	14,837,277	-	235,341,308
Total interest bearing assets at fixed rates		221,846,765	16,729,890	248,658,498	624,259,243	418,863,544	-	1,530,357,939
Cash and cash equivalents		88,512,603	8,572,410	-	-	-	-	97,085,013
Precious metals		15,305,466	-	-	-	-	-	15,305,466
Amounts due from credit institutions		8,165,275				-	17,491,406	25,656,680
Loans to customers		3,005,030	-	-	-	-	1,759,473	4,764,503
Investment securities		804,045	499,244	-	-	-	179,650	1,482,939
Other assets		4,257,246	952,594	-	15,823,867	-	-	21,033,707
Forfeiting		-	1,164,520	3,425,445	-	-	-	4,589,966
		341,896,429	**27,918,658**	**252,083,943**	**640,083,110**	**418,863,544**	**19,430,529**	**1,700,276,212**
Liabilities								
Amounts due to banks and government agencies	2.36%	10,900,000	85,015,361	43,001,770	51,249,797	140,621,690	-	330,788,617
Customer accounts	1.64%	14,207,119	167,736,300	480,232,570	285,997,805	-	-	948,173,795
Total interest bearing liabilities at fixed rates		25,107,119	252,751,661	523,234,340	337,247,603	140,621,690	-	1,278,962,412
Amounts due to banks and government agencies		25,854,179	-	-	-	-	-	25,854,179
Customer accounts		220,665,997	-	-	-	870,000	13,746,689	235,282,686
Current income tax liability		-	2,439,634	-	-	-	-	2,439,634
Other liabilities		2,617,278	986,433	3,960,635	-	-	-	7,564,346
Guarantees issued		2,066,167	1,006,006	9,838,365	12,802,012	-	-	25,712,549
Letters of credit		-	42,503	10,356,570	-	-	-	10,399,073
Undrawn loan commitments		54,309	1,347,534	29,416,630	10,836,663	17,001,000	-	58,656,136
		276,365,048	**258,573,770**	**576,806,540**	**360,886,277**	**158,492,690**	**13,746,689**	**1,644,871,014**
Liquidity gap		65,531,381	(230,655,113)	(324,722,597)	279,196,833	260,370,854		
Interest sensitivity gap for fixed rate instruments		196,739,646	(236,021,772)	(274,575,842)	287,011,640	278,241,854		
Interest sensitivity gap		196,739,646	(236,021,772)	(274,575,842)	287,011,640	278,241,854		
Cumulative interest sensitivity gap		**196,739,646**	**(39,282,125)**	**(313,857,967)**	**(26,846,327)**	**251,395,527**		

Market Risk

Market risk covers interest rate risk, currency risk and other pricing risks to which the Group is exposed. There have been no changes as to the way the Group measures risk or to the risk it is exposed in 2017.

The Group is exposed to interest rate risks as entities in the Group borrow funds at both fixed and floating rates. The risk is managed by the Group maintaining an appropriate mix between fixed and floating rate borrowings.

The ALMC also manages interest rate and market risks by matching the Group's interest rate position, which provides the Group with a positive interest margin. The Department of Financial Control conducts monitoring of the Group's current financial performance, estimates the Group's sensitivity to changes in interest rates and its influence on the Group's profitability.

The majority of the Group's loan contracts and other financial assets and liabilities that bear interest are either variable or contain clauses enabling the interest rate to be changed at the option of the lender. The Group monitors its interest rate margin and consequently does not consider itself exposed to significant interest rate risk or consequential cash flow risk

Interest rate risk

The Group manages fair value interest rate risk through periodic estimation of potential losses that could arise from adverse changes in market conditions. The Department of Financial Control conducts monitoring of the Group's current financial performance, estimates the Group's sensitivity to changes in fair value interest rates and its influence on the Group's profitability.

The following table presents a sensitivity analysis of interest rate risk, which has been determined based on "reasonably possible changes in the risk variable". The level of these changes is determined by management and is contained within the risk reports provided to key management personnel.

Impact on profit before tax:

	As at 31 December 2018		As at 31 December 2017	
	Interest rate +1%	Interest rate -1%	Interest rate +1%	Interest rate -1%
Assets:				
Cash and cash equivalents	1,279,817	(1,279,817)	100,000	(100,000)
Amounts due from credit institutions	408,277	(408,277)	365,762	(365,762)
Loans to customers	13,282,926	(13,282,926)	12,584,404	(12,584,404)
Investment securities	1,640,168	(1,640,168)	2,353,413	(2,353,413)
Liabilities:				
Amounts due to banks and government agencies	(3,553,056)	3,553,056	(3,307,886)	3,307,886
Customer accounts	(8,579,260)	8,579,260	(9,481,738)	9,481,738
Net impact on profit before tax	**4,478,872**	**(4,478,872)**	**2,613,955**	**(2,613,955)**

Currency risk

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

The Management Board sets limits on the level of exposure by currencies. These limits also comply with the minimum requirements of the CBAR. The Group's exposure to foreign currency exchange rate risk is presented in the table below:

	AZN	USD	EUR	Other currencies	31 December 2018 Total
Assets					
Cash and cash equivalents	172,318,655	30,101,064	73,770,026	2,019,767	278,209,512
Precious metals				14,989,411	14,989,411
Amounts due from credit institutions	6,873,294	11,897,966	12,243,973	35,424,732	66,439,965
Loans to customers	257,192,027	1,025,730,529	49,288,478	-	1,332,211,034
Investment securities	123,165,020	42,352,192	4,458	-	165,521,670
Property and equipment	66,571,711	-	-	-	66,571,711
Investment property	7,027,246	-	-	-	7,027,246
Intangible assets	1,511,655	-	-	-	1,511,655
Other assets	58,631,019	444,587	190,718	-	59,266,324
Total assets	**693,290,627**	**1,110,526,338**	**135,497,653**	**52,433,910**	**1,991,748,528**
Liabilities					
Amounts due to banks and government agencies	255,239,850	120,915,846	1,398	539	376,157,633
Customer accounts	397,340,844	786,925,770	134,674,443	16,093,729	1,335,034,786
Provision for impairment losses on other operations	61,703	-	-	-	61,703
Current income tax liability	4,159,131	-	-	-	4,159,131
Deferred income tax liability	2,387,920	-	-	-	2,387,920
Other liabilities	5,045,187	1,118,222	924,157	5	7,087,571
Total liabilities	**664,234,635**	**908,959,838**	**135,599,998**	**16,094,273**	**1,724,888,744**
Net balance sheet position	**29,055,992**	**201,566,500**	**(102,345)**	**36,339,637**	

	AZN	USD	EUR	Other currencies	31 December 2017 Total
Assets					
Cash and cash equivalents	32,817,367	68,848,866	4,245,851	1,172,929	107,085,013
Precious metals	-	-	-	15,305,466	15,305,466
Amounts due from credit institutions	8,572,410	15,613	17,066,625	36,578,236	62,232,884
Loans to customers	414,965,542	802,783,804	45,455,584	-	1,263,204,930
Forfeiting	-	4,498,167	-	-	4,498,167
Investment securities	194,349,983	42,469,613	4,650	-	236,824,246
Property and equipment	68,214,636	-	-	-	68,214,636
Investment property	6,825,306	-	-	-	6,825,306
Intangible assets	1,551,970	-	-	-	1,551,970
Other assets	25,566,801	1,172,264	274,622	8,703	27,022,390
Total assets	**752,864,015**	**919,788,327**	**67,047,332**	**53,065,334**	**1,792,765,008**
Liabilities					
Amounts due to banks and government agencies	235,792,034	120,820,574	30,104	84	356,642,796
Customer accounts	358,584,898	742,093,601	66,711,378	16,066,603	1,183,456,480
Provision for impairment losses on other operations	203,376	-	-	-	203,376
Current income tax liability	2,439,634	-	-	-	2,439,634
Deferred income tax liability	1,457,705	-	-	-	1,457,705
Other liabilities	3,990,591	3,433,624	140,125	6	7,564,346
Total liabilities	**602,468,238**	**866,347,799**	**66,881,607**	**16,066,693**	**1,551,764,337**
Net balance sheet position	**150,395,777**	**53,440,528**	**165,725**	**36,998,641**	

Currency risk sensitivity

The following table details the Group's sensitivity to a 10% increase and decrease in the USD and Euro against the AZN. 10% is the sensitivity rate used when reporting foreign currency risk internally to key management personnel and represents management's assessment of the possible change in foreign currency exchange rates. The sensitivity analysis includes only outstanding foreign currency denominated monetary items and adjusts their translation at the end of the period for a 10% change in foreign currency rates. The sensitivity analysis includes external loans as well as loans to foreign operations within the Group where the denomination of the loan is in a currency other than the currency of the lender or the borrower.

	As at 31 December 2018		**As at 31 December 2017**	
	AZN / USD +10%	AZN / USD -10%	AZN / USD +10%	AZN / USD -10%
Impact on profit or loss	20,156,650	(20,156,650)	5,344,053	(5,344,053)

	As at 31 December 2018		**As at 31 December 2017**	
	AZN / EURO +10%	AZN / EURO -10%	AZN / EURO +10%	AZN / EURO -10%
Impact on profit or loss	(10,235)	10,235	16,573	(16,573)

Limitations of sensitivity analysis

The above tables demonstrate the effect of a change in a key assumption while other assumptions remain unchanged. In reality, there is a correlation between the assumptions and other factors. It should also be noted that these sensitivities are non-linear, and larger or smaller impacts should not be interpolated or extrapolated from these results.

The sensitivity analyses do not take into consideration that the Group's assets and liabilities are actively managed. Additionally, the financial position of the Group may vary at the time that any actual market movement occurs. For example, the Group's financial risk management strategy aims to manage the exposure to market fluctuations. As investment markets move past various trigger levels, management actions could include selling investments, changing investment portfolio allocation and taking other protective action. Consequently, the actual impact of a change in the assumptions may not have any impact on the liabilities, whereas assets are held at market value on the consolidated statement of financial position. In these circumstances, the different measurement bases for liabilities and assets may lead to volatility in shareholder equity.

Other limitations in the above sensitivity analyses include the use of hypothetical market movements to demonstrate potential risk that only represent the Group's view of possible near-term market changes that cannot be predicted with any certainty; and the assumption that all interest rates move in an identical fashion.

31. Events after the reporting period

On 11 February 2019 Shareholders of the Bank declared dividends in the amount of AZN 7,986,660 on ordinary shares which was paid on 5 March 2019.

On 1 April 2019 Shareholders of the Bank decided to increase share capital of the Bank in the amount of AZN 107,999,784.