

Consolidated financial statements

OJSC Xalq Bank and its subsidiaries
for the year ended 31 December 2019

with independent auditor's report

Open Joint Stock Company Xalq Bank

Table of Contents

Consolidated Financial Statements

Statement of management's responsibilities	1
Independent auditor's report	2
Consolidated statement of profit or loss.....	5
Consolidated statement of financial position.....	6
Consolidated statement of changes in equity	7
Consolidated statement of cash flows	8

Notes to the Consolidated Financial Statements

1. Background.....	10
2. Basis of presentation	11
3. Summary of significant accounting policies	11
4. Adoption of new or revised standards and interpretations	20
5. Net interest income	25
6. Credit loss expense and other impairment and provisions	25
7. Fee and commission income and expense	26
8. Net gain on foreign exchange operations	27
9. Net gain / (loss) on precious metals operations.....	27
10. Personnel, general and administrative expenses	27
11. Income taxes.....	28
12. Earnings per share.....	29
13. Cash and cash equivalents.....	29
14. Amounts due from credit institutions.....	30
15. Loans to customers.....	32
16. Investment securities	37
17. Premises, equipment and right-of-use assets	40
18. Investment properties	41
19. Intangible assets	41
20. Other assets.....	42
21. Amounts due to banks and government agencies.....	42
22. Customer accounts	43
23. Other liabilities.....	43
24. Share capital	44
25. Commitments and contingencies.....	44
26. Transactions with related parties	46
27. Fair value of financial instruments	48
28. Regulatory matters.....	50
29. Capital management.....	50
30. Risk management policies	51
31. Events after the reporting period.....	66

Statement of management's responsibilities for the preparation and approval of the consolidated financial statements for the year ended 31 December 2019

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 2019, 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 2019 were authorized for issue on 30 April 2020 by the Management Board.

Approved for issue and signed on behalf of the Management Board on 30 April 2020.


Chairman
Mr. Elkhan Aghayev




Chief Accountant
Mrs. Tamilla Asadova

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 2019, 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 2019, 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.



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



30 April 2020
Baku, the Republic of Azerbaijan

Open Joint Stock Company Xalq Bank

Consolidated statement of profit or loss for the year ended 31 December 2019 (in Azerbaijan manats)

	Notes	Year ended 31 December 2019	Year ended 31 December 2018
Interest income	5	110,720,135	109,399,694
Interest expense	5	(19,626,542)	(23,158,018)
Net interest income		91,093,793	86,241,676
Credit loss expense on interest bearing assets	6	(27,750,133)	(24,893,112)
Net interest income after credit loss expense		63,343,660	61,348,564
Net fee and commission income	7	5,300,948	4,377,772
Net gain on foreign exchange operations	8	6,873,521	1,888,606
Net gain / (loss) on precious metals operations	9	2,621,882	(211,205)
Gain on revaluation of investment property	18	277,791	201,940
Recovery of provision for impairment losses on non-interest bearing assets	20	258,801	3,039,742
Other income		1,873,524	954,049
Non-interest income		17,206,467	10,250,904
Personnel expenses	10	(24,201,913)	(21,555,829)
General and administrative expenses	10	(13,361,147)	(13,571,508)
Depreciation and amortisation	17,19	(6,230,398)	(4,945,635)
Recovery of provision for impairment losses on guarantees and other commitments	6	21,553	53,171
Non-interest expense		(43,771,905)	(40,019,801)
Profit before income tax		36,778,222	31,579,667
Income tax expense	11	(7,468,005)	(6,353,987)
Net profit for the year		29,310,217	25,225,680
Attributable to:			
- shareholders of the Bank		29,304,206	25,221,584
- non-controlling interest		6,011	4,096
		<u>29,310,217</u>	<u>25,225,680</u>
EARNINGS PER SHARE			
<i>Basic and diluted (AZN)</i>	12	<u>8.072</u>	<u>6.948</u>

Approved for issue and signed on behalf of the Management Board on 30 April 2020.





Chairman
Mr. Elkhan Aghayev

Chief Accountant
Mrs. Tamilla Asadova

Open Joint Stock Company Xalq Bank

Consolidated statement of financial position as at 31 December 2019
(in Azerbaijan manats)

	Notes	31 December 2019	31 December 2018
Assets			
Cash and cash equivalents	13	363,973,758	278,209,512
Precious metals		17,515,867	14,989,411
Amounts due from credit institutions	14	36,385,755	66,439,965
Loans to customers	15	1,766,799,111	1,332,211,034
Investment securities	16	110,161,296	165,521,670
Property, equipment and right-of-use assets	17	69,365,695	67,041,774
Investment properties	18	7,315,000	7,027,246
Intangible assets	19	2,034,792	1,511,655
Other assets	20	56,927,395	58,796,261
Total assets		2,430,478,669	1,991,748,528
Liabilities			
Amounts due to banks and government agencies	21	383,805,333	376,157,633
Customer accounts	22	1,636,351,672	1,335,034,786
Current income tax liability		306,531	4,159,131
Deferred income tax liability	11	1,144,632	2,387,920
Other liabilities	23	12,694,166	7,149,274
Total liabilities		2,034,302,334	1,724,888,744
Equity			
Share capital	24	364,772,544	225,078,600
Retained earnings		31,294,523	41,671,137
Non-controlling interest		109,268	110,047
Total equity		396,176,335	266,859,784
Total liabilities and equity		2,430,478,669	1,991,748,528

Approved for issue and signed on behalf of the Management Board on 30 April 2020.





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 2019 (in Azerbaijan manats)

	Share capital	Retained earnings	Non-controlling interest	Total equity
1 January 2018	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
Share capital increase	107,999,784	-	-	107,999,784
Capitalization of retained earnings	31,694,160	(31,694,160)	-	-
Dividends to shareholders of Bank	-	(7,986,660)	-	(7,986,660)
Total income for the year	-	29,304,206	6,011	29,310,217
Change in ownership interest in subsidiary	-	-	(6,790)	(6,790)
31 December 2019	364,772,544	31,294,523	109,268	396,176,335

Approved for issue and signed on behalf of the Management Board on 30 April 2020.

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 2019 (in Azerbaijan manats)

	Notes	Year ended 31 December 2019	Year ended 31 December 2018
CASH FLOWS FROM OPERATING ACTIVITIES:			
Profit before income tax		36,778,222	31,579,667
Adjustments for:			
Provision for impairment losses on interest bearing assets (Recovery of provision) / provision for guarantees and other commitments	6	27,750,133 (21,553)	24,893,112 (74,534)
(Recovery of provision) / provision for impairment losses on non-interest bearing assets		(258,801)	(3,039,742)
Net unrealized loss / (gain) arising from changes in foreign currency exchange rates		(4,086,781)	297,371
Depreciation and amortization	17,19	6,230,710	4,945,635
Gain on revaluation of investment property	18	(277,791)	(201,940)
Gain on disposal of property and equipment		(204,533)	(40,170)
Change in interest accruals, net		(7,881,053)	(1,233,190)
Cash flows from operating activities before changes in operating assets and liabilities		58,028,553	57,126,209
Changes in operating assets and liabilities (Increase)/decrease in operating assets:			
Precious metals		(2,526,456)	316,055
Amounts due from credit institutions		30,190,800	(3,869,207)
Loans to customers		(454,041,843)	(84,513,085)
Forfeiting		-	4,589,966
Other assets		2,126,345	(29,270,022)
Increase/(decrease) in operating liabilities:			
Amounts due to banks and government agencies		7,642,577	19,489,573
Customer accounts		301,166,407	151,566,731
Other liabilities		1,013,583	(476,775)
Cash (outflow) / inflow from operating activities before taxation		(56,400,034)	114,959,445
Income tax paid		(12,563,893)	(5,360,822)
Net cash (outflow) / inflow from operating activities		(68,963,927)	109,598,623
CASH FLOWS FROM INVESTING ACTIVITIES:			
Purchase of property, equipment and intangible assets	17,19	(4,527,623)	(3,238,673)
Proceeds on disposal of property and equipment		207,250	83,600
Proceeds from sale and redemption of investment securities		54,965,394	70,971,075
Investment property improvements	18	(9,963)	-
Acquisition of subsidiary, net of cash acquired		(6,790)	(2,760)
Net cash inflow / (outflow) from investing activities		50,628,268	67,813,242

Open Joint Stock Company Xalq Bank

Consolidated statement of cash flows for the year ended 31 December 2019 (Continued) (in Azerbaijan manats)

	Notes	Year ended 31 December 2019	Year ended 31 December 2018
CASH FLOWS FROM FINANCING ACTIVITIES:			
Dividends paid to shareholders of the Bank		(7,986,660)	(5,989,995)
Increase in share capital		107,999,784	-
Net cash inflow / (outflow) from financing activities		100,013,124	(5,989,995)
Effect of foreign exchange rate changes on cash and cash equivalents		4,086,781	(297,371)
Net increase in cash and cash equivalents		85,764,246	171,124,499
Cash and cash equivalents, beginning of year		278,209,512	107,085,013
Cash and cash equivalents, end of year	13	363,973,758	278,209,512

Interest paid and received by the Group in cash during the year ended 31 December 2019 amounted to AZN19,470,740 and AZN 102,683,480, respectively.

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.

Approved for issue and signed on behalf of the Management Board on 30 April 2020.


Chairman
Mr. Elkhan Aghayev


Chief Accountant
Mrs. Tamilla Asadova



Open Joint Stock Company Xalq Bank

Notes to the consolidated financial statements for the year ended 31 December 2019 (in Azerbaijan manats)

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 30 and 29 branches in Azerbaijan as at 31 December 2019 and 2018 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 2019 and 2018 was 693 and 628, respectively.

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

Name	Country of operation	The Bank ownership interest/ voting rights		Type of operation
		2019	2018	
<i>Xalq Kapital LLC</i>	<i>The Republic of Azerbaijan</i>	100 %	100 %	<i>Securities market transactions</i>
<i>Baki Ayaqqabi -2 OJSC</i>	<i>The Republic of Azerbaijan</i>	98.41%	98.36%	<i>Dormant</i>

"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 2019 and 2018 the following shareholders owned the issued shares of the Bank:

	31 December 2019	31 December 2018
	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 2019 and 2018 the Bank is ultimately owned by Mrs. Leyla Aliyeva and Mrs. Arzu Aliyeva, who exercise joint control over the Bank.

Open Joint Stock Company Xalq Bank

Notes to the consolidated financial statements for the year ended 31 December 2019 (Continued) (in Azerbaijan manats)

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.

Open Joint Stock Company Xalq Bank

Notes to the consolidated financial statements for the year ended 31 December 2019 (Continued) (in Azerbaijan manats)

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.

Open Joint Stock Company Xalq Bank

Notes to the consolidated financial statements for the year ended 31 December 2019 (Continued) (in Azerbaijan manats)

Measurement categories of financial assets and liabilities

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.

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

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.

Open Joint Stock Company Xalq Bank

Notes to the consolidated financial statements for the year ended 31 December 2019 (Continued) (in Azerbaijan manats)

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

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 income 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

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.

Open Joint Stock Company Xalq Bank

Notes to the consolidated financial statements for the year ended 31 December 2019 (Continued) (in Azerbaijan manats)

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 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, 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.

Reclassification of financial assets and liabilities

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 2019.

Renegotiated loans

Where possible, the Bank seeks to restructure loans rather than to take possession of collateral. This may involve extending the payment arrangements and the agreement of new loan conditions.

The Bank derecognises a financial asset, such as a loan to a customer, when the terms and conditions have been renegotiated to the extent that, substantially, it becomes a new loan, with the difference recognised as a derecognition gain or loss, to the extent that an impairment loss has not already been recorded. The newly recognised loans are classified as Stage 1 for ECL measurement purposes, unless the new loan is deemed to be POCI. When assessing whether or not to derecognise a loan to a customer, amongst others, the Bank considers the following factors:

- Change in currency of the loan;
- Change in counterparty;
- If the modification is such that the instrument would no longer meet the SPPI criterion.

If the modification does not result in cash flows that are substantially different, the modification does not result in derecognition. Based on the change in cash flows discounted at the original EIR, the Bank records a modification gain or loss, presented within interest income calculated using EIR in the consolidated statement of profit or loss, to the extent that an impairment loss has not already been recorded.

Open Joint Stock Company Xalq Bank

Notes to the consolidated financial statements for the year ended 31 December 2019 (Continued) (in Azerbaijan manats)

Derecognition of financial assets and liabilities

Financial assets

A financial asset (or, where applicable a part of a financial asset or part of a group of similar financial assets) is derecognised where:

- The rights to receive cash flows from the asset have expired;
- The Group has transferred its rights to receive cash flows from the asset, or retained the right to receive cash flows from the asset, but has assumed an obligation to pay them in full without material delay to a third party under a "pass-through" arrangement; and
- The Group either (a) has transferred substantially all the risks and rewards of the asset, or (b) has neither transferred nor retained substantially all the risks and rewards of the asset, but has transferred control of the asset.

Where the Group has transferred its rights to receive cash flows from an asset and has neither transferred nor retained substantially all the risks and rewards of the asset nor transferred control of the asset, the asset is recognised to the extent of the Group's continuing involvement in the asset. Continuing involvement that takes the form of a guarantee over the transferred asset is measured at the lower of the original carrying amount of the asset and the maximum amount of consideration that the Group could be required to repay.

Where continuing involvement takes the form of a written and/or purchased option (including a cash-settled option or similar provision) on the transferred asset, the extent of the Group's continuing involvement is the amount of the transferred asset that the Group may repurchase, except that in the case of a written put option (including a cash-settled option or similar provision) on an asset measured at fair value, the extent of the Group's continuing involvement is limited to the lower of the fair value of the transferred asset and the option exercise price.

Write-off

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

Financial liabilities

A financial liability is derecognised when the obligation under the liability is discharged or cancelled or expires.

Where an existing financial liability is replaced by another from the same lender on substantially different terms, or the terms of an existing liability are substantially modified, such an exchange or modification is treated as a derecognition of the original liability and the recognition of a new liability, and the difference in the respective carrying amounts is recognised in profit or loss.

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 up to ninety 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.

Open Joint Stock Company Xalq Bank

Notes to the consolidated financial statements for the year ended 31 December 2019 (Continued) (in Azerbaijan manats)

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.

Open Joint Stock Company Xalq Bank

Notes to the consolidated financial statements for the year ended 31 December 2019 (Continued) (in Azerbaijan manats)

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 recognised 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.

Open Joint Stock Company Xalq Bank

Notes to the consolidated financial statements for the year ended 31 December 2019 (Continued) (in Azerbaijan manats)

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 income and expense

The Group calculates interest income 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. 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 income 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 income on a gross basis.

For purchased or originated credit-impaired (POCI) financial assets, the Group calculates interest income 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 income 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.

Open Joint Stock Company Xalq Bank

Notes to the consolidated financial statements for the year ended 31 December 2019 (Continued) (in Azerbaijan manats)

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 2019	31 December 2016
USD 1 = AZN 1.7000	USD 1 = AZN 1.7001
EUR 1 = AZN 1.9035	EUR 1 = AZN 1.9468
GBP 1 = AZN 2.2284	GBP 1 = AZN 2.1529
RUR 1 = AZN 0.0274	RUR 1 = AZN 0.0245

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 2019. The nature and effect of the changes as a result of adoption of these new accounting standards are described below.

IFRS 16 Leases

IFRS 16 supersedes IAS 17 Leases, IFRIC 4 Determining whether an Arrangement Contains a Lease, SIC-15 Operating Leases – Incentives and SIC-27 Evaluating the Substance of Transactions Involving the Legal Form of a Lease. IFRS 16 sets out the principles for the recognition, measurement, presentation and disclosure of leases and requires lessees to account for most leases under a single on-balance sheet model.

Lessor accounting under IFRS 16 is substantially unchanged from IAS 17. Lessors will continue to classify leases using the same classification principle as in IAS 17 and distinguish between two types of leases: operating and finance leases.

The Group adopted IFRS 16 using the modified retrospective method of adoption with the date of initial application of 1 January 2019. Under this method, the standard is applied retrospectively with the cumulative effect of initially applying the standard recognised at the date of initial application. The Group elected to use the transition practical expedient allowing the standard to be applied only to contracts that were previously identified as leases applying IAS 17 and IFRIC 4 at the date of initial application. The Group also elected to use the recognition exemptions for lease contracts that, at the commencement date, have a lease term of 12 months or less and do not contain a purchase option ('short-term leases'), and lease contracts for which the underlying asset is of low ('low-value' assets).

Open Joint Stock Company Xalq Bank

Notes to the consolidated financial statements for the year ended 31 December 2019 (Continued) (in Azerbaijan manats)

The effect of adoption of IFRS 16 as at 1 January 2019 is as follows:

	<i>Effect of transition to IFRS 16</i>
Property and equipment (right of use assets)	4,552,862
Other assets (prepayments)	(296,117)
Lease liabilities	<u>4,256,745</u>

(a) *Nature of the effect of adoption of IFRS 16*

The Group has lease contracts for premises. Before the adoption of IFRS 16, the Group classified each of its leases (as lessee) at the inception date as either a finance lease or an operating lease. A lease was classified as a finance lease if it transferred substantially all of the risks and rewards incidental to ownership of the leased asset to the Group; otherwise it was classified as an operating lease. Finance leases were capitalised at the commencement of the lease at the inception date fair value of the leased property or, if lower, at the present value of the minimum lease payments. Lease payments were apportioned between interest and reduction of the lease liability. In an operating lease, the leased property was not capitalized and the lease payments were recognised as rent expense in profit or loss on a straight-line basis over the lease term. Any prepaid rent and accrued rent were recognized under Other assets and Other liabilities, respectively.

Upon adoption of IFRS 16, the Group applied a single recognition and measurement approach for all leases, except for short-term leases and leases of low-value assets. The standard provides specific transition requirements and practical expedients, which has been applied by the Group.

Leases previously accounted for as operating leases

The Group recognised right-of-use assets and lease liabilities for those leases previously classified as operating leases, except for short-term leases and leases of low-value assets. The right-of-use assets were recognised based on the amount equal to the lease liabilities, adjusted for any related prepaid and accrued lease payments previously recognised. Lease liabilities were recognised based on the present value of the remaining lease payments, discounted using the incremental borrowing rate at the date of initial application.

The Group also applied the available practical expedients wherein it:

- Used a single discount rate to a portfolio of leases with reasonably similar characteristics;
- Relied on its assessment of whether leases are onerous immediately before the date of initial application;
- Applied the short-term leases exemptions to leases with lease term that ends within 12 months at the date of initial application;
- Excluded the initial direct costs from the measurement of the right-of-use asset at the date of initial application;
- Used hindsight in determining the lease term where the contract contains options to extend or terminate the lease.

Based on the foregoing, as at 1 January 2019;

- Right-of-use assets of AZN 4,552,862 were recognised;
- Lease liabilities of AZN 4,256,745 recognised;
- Prepayments of AZN 296,117 related to previous operating leases were derecognised.

Open Joint Stock Company Xalq Bank

Notes to the consolidated financial statements for the year ended 31 December 2019 (Continued) (in Azerbaijan manats)

(b) Summary of new accounting policies

Set out below are the new accounting policies of the Group upon adoption of IFRS 16, which have been applied from the date of initial application:

Group as a lessee

The Group applied a single recognition and measurement approach for all leases, except for short-term leases and leases of low-value assets. The Group recognises lease liabilities to make lease payments and right-of-use assets representing the right to use underlying assets.

Right-of-use Assets

The Group recognises right-of-use assets at the commencement date of the lease (i.e., the date the underlying asset is available for use). Right-of-use assets are measured at cost, less any accumulated depreciation and impairment losses, and adjusted for any remeasurement of lease liabilities. The cost of right-of-use assets includes the amount of lease liabilities recognised, initial direct costs incurred, and lease payments made at or before the commencement date less any lease incentives received. Unless the Group is reasonably certain to obtain ownership of the leased asset at the end of the lease term, the recognised right-of-use assets are depreciated on a straight-line basis over the shorter of its estimated useful life and the lease term. Right-of-use assets are subject to impairment.

Lease liability

At the commencement date of the lease, the Group recognises lease liabilities measured at the present value of lease payments to be made over the lease term. The lease payments include fixed payments (including in-substance fixed payments) less any lease incentives receivable, variable lease payments that depend on an index or a rate, and amounts expected to be paid under residual value guarantees. The lease payments also include the exercise price of a purchase option reasonably certain to be exercised by the Group and payments of penalties for terminating a lease, if the lease term reflects the Group exercising the option to terminate. The variable lease payments that do not depend on an index or a rate are recognised as expense in the period on which the event or condition that triggers the payment occurs.

In calculating the present value of lease payments, the Group use the incremental borrowing rate at the lease commencement date if the interest rate implicit in the lease is not readily determinable. After the commencement date, the amount of lease liabilities is increased to reflect the accretion of interest and reduced for the lease payments made. In addition, the carrying amount of lease liabilities is remeasured if there is a modification, a change in the lease term, a change in the in-substance fixed lease payments or a change in the assessment to purchase the underlying asset.

Short-term leases and leases of low-value assets

The Group applies the short-term lease recognition exemption to its short-term leases (i.e., those leases that have a lease term of 12 months or less from the commencement date and do not contain a purchase option). It also applies the lease of low-value assets recognition exemption to leases of office equipment that are considered of low value. Lease payments on short-term leases and leases of low-value assets are recognised as expense on a straight-line basis over the lease term.

Significant judgement in determining the lease term of contracts with renewal options

The Group determines the lease term as the non-cancellable term of the lease, together with any periods covered by an option to extend the lease if it is reasonably certain to be exercised, or any periods covered by an option to terminate the lease, if it is reasonably certain not to be exercised.

Open Joint Stock Company Xalq Bank

Notes to the consolidated financial statements for the year ended 31 December 2019 (Continued) (in Azerbaijan manats)

Carrying amount of the Group's right-of-use assets and lease liability and the movements during the period are as follows:

	<u>Right-of-use assets</u>	<u>Total Lease Liability</u>
As at 1 January 2019	-	-
Transition effect	4,552,862	4,256,745
Addition	-	-
Depreciation expens	(881,921)	-
Interest expense	-	252,258
Payments	-	(965,531)
As at 31 December 2019	<u>3,670,941</u>	<u>3,543,472</u>

IFRIC Interpretation 23 Uncertainty over Income Tax Treatment

The Interpretation addresses the accounting for income taxes when tax treatments involve uncertainty that affects the application of IAS 12 Income Tax. It does not apply to taxes or levies outside the scope of IAS 12, nor does it specifically include requirements relating to interest and penalties associated with uncertain tax treatments. The Interpretation specifically addresses the following:

- Whether an entity considers uncertain tax treatments separately;
- The assumptions an entity makes about the examination of tax treatments by taxation authorities;
- How an entity determines taxable profit (tax loss), tax bases, unused tax losses, unused tax credits and tax rates;
- How an entity considers changes in facts and circumstances.

The Group determine whether to consider each uncertain tax treatment separately or together with one or more other uncertain tax treatments use the approach that better predicts the resolution of the uncertainty.

The Groupe applies significant judgement in identifying uncertainties over income tax treatments. Since the Group operates in a complex environment, it assessed whether the Interpretation had an impact on its consolidated financial statements. Under adoption of the Interpretation, the Group considered whether it has any uncertain tax positions. The Interpretation dis not have an impact on the consolidated financial statements of the Group.

Amendments to IFRS 9: Prepayment Features with Negative Compensation

Under IFRS 9, a debt instrument can be measured at amortised cost or at fair value through other comprehensive income, provided that the contractual cash flows are 'solely payments of principal and interest on the principal amount outstanding' (the SPPI criterion) and the instrument is held within the appropriate business model for that classification. The amendments to IFRS 9 clarify that a financial asset passes the SPPI criterion regardless of the event or circumstance that causes the early termination of the contract and irrespective of which party pays or receives reasonable compensation for the early termination of the contract. These amendments had no impact on the consolidated financial statements of the Group.

Open Joint Stock Company Xalq Bank

Notes to the consolidated financial statements for the year ended 31 December 2019 (Continued) (in Azerbaijan manats)

New Accounting Pronouncements

The new and amended standards and interpretations have been published that become effective for the accounting periods beginning on or after 1 January 2020 or later periods disclosed below. The Group intended to adopt these new and amended standards and interpretations if applicable, when they become effective.

Amendments to IFRS 3 Definition of a Business

In October 2018, the IASB issued amendments to the definition of a business in IFRS 3 Business Combinations to help entities determine whether an acquired set of activities and assets is a business or not. They clarify the minimum requirements for a business, remove the assessment of whether market participants are capable of replacing any missing elements, add guidance to help entities assess whether an acquired process is substantive, narrow the definitions of a business and of outputs, and introduce an optional fair value concentration test. New illustrative examples were provided along with the amendments.

Since the amendments apply prospectively to transaction or other events that occur on or after the date of first application, the Group will not be affected by these amendments on the date of transition.

Amendments to IAS 1 and IAS 8 Definition Material

In October 2018, the IASB issued amendments to IAS 1 Presentation of Financial Statements and IAS 8 Accounting Policies, Changes in Accounting Estimates and Errors to align the definition of "material" across the standards and to clarify certain aspects of the definition. The new definition states that, "Information is material if omitting, misstating or obscuring it could reasonably be expected to influence decisions that the primary users of general purpose financial statements make on the basis of those financial statement, which provide financial information about a specific reporting entity."

The amendments to the definition of material is not expected to have a significant impact on the Group's financial statements.

Interest Rate Benchmark Reform: Amendments to IFRS 9, IAS 39 and IFRS

Interest Rate Benchmark Reform Amendments to IFRS 9, IAS 39 and IFRS 7 includes a number of reliefs, which apply to all hedging relationships that are directly affected by interest rate benchmark reform. A hedging relationship is affected if the reform gives rise to uncertainties about the timing and or amount of benchmark-based cash flows of the hedged item or the hedging instrument. As a result of interest rate benchmark reform, there may be uncertainties about the timing and or amount of benchmark-based cash flows of the hedged item or the hedging instrument during the period before the replacement of an existing interest rate benchmark with an alternative nearly risk-free interest rate (an RFR). This may lead to uncertainty whether a forecast transaction is highly probable and whether prospectively the hedging relationship is expected to be highly effective.

The amendments come into effect from 1 January 2020, but entities may choose to apply them early. The amendments are not expected to have a significant impact on the Group's consolidated financial statements.

Open Joint Stock Company Xalq Bank

Notes to the consolidated financial statements for the year ended 31 December 2019 (Continued) (in Azerbaijan manats)

5. Net interest income

Net interest income comprise:

	Year ended 31 December 2019	Year ended 31 December 2018
Interest income comprises		
Interest on loans to customers	92,886,035	85,895,081
Interest on debt securities	11,071,433	14,831,174
Interest on due from banks	5,714,928	7,780,398
Interest on guarantees	948,138	736,411
Interest on other operations	99,601	156,630
Total interest income on financial assets recorded at amortized cost	<u>110,720,135</u>	<u>109,399,694</u>
Interest expense comprises:		
Interest on customer accounts	(13,654,392)	(15,663,157)
Interest on due to banks and government agencies	(5,719,692)	(7,494,861)
Interest on lease liabilities	(252,258)	-
Total interest expense on financial assets recorded at amortized cost	<u>(19,626,342)</u>	<u>(23,158,018)</u>
Net interest income before provision for impairment losses on interest bearing assets	<u><u>91,093,793</u></u>	<u><u>86,241,676</u></u>

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 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)
(Provision) / recovery of provision	-	(3,723)	120,177	(27,866,587)	(27,750,133)
Write-off of assets	-	-	-	7,955,921	7,955,921
31 December 2019	<u>-</u>	<u>(89,514)</u>	<u>(12,139)</u>	<u>(138,185,555)</u>	<u>(138,287,208)</u>

Open Joint Stock Company Xalq Bank

Notes to the consolidated financial statements for the year ended 31 December 2019 (Continued) (in Azerbaijan manats)

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

	Guarantees and other commitments
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)
Recovery of provision	21,553
Write-off	-
31 December 2019	(40,150)

7. Fee and commission income and expense

Fee and commission income and expense comprise:

	Year ended 31 December 2019	Year ended 31 December 2018
Fee and commission income:		
Settlements	3,327,920	1,622,754
Cash operations	2,419,900	1,425,163
Plastic cards operations	2,270,894	1,647,636
Letters of credit	75,508	99,734
Guarantee letters	69,160	61,310
Forfeiting	-	1,514,622
Foreign exchange operations	-	882,441
Other	272,978	309,985
Total fee and commission income	8,436,360	7,563,645
Fee and commission expense:		
Plastic cards operations	(1,758,313)	(1,491,476)
Settlements	(566,555)	(659,360)
Cash operations	(97,521)	(199,130)
Letters of credit	(36,995)	(55,353)
Other	(676,028)	(780,554)
Total fee and commission expense	(3,135,412)	(3,185,873)
Net fee and commission income	5,300,948	4,377,772

Open Joint Stock Company Xalq Bank

Notes to the consolidated financial statements for the year ended 31 December 2019 (Continued) (in Azerbaijan manats)

8. Net gain on foreign exchange operations

Net gain on foreign exchange operations comprise:

	Year ended 31 December 2019	Year ended 31 December 2018
Dealing differences, net	2,786,740	2,185,977
Translation differences, net	<u>4,086,781</u>	<u>(297,371)</u>
Total net gain on foreign exchange operations	<u>6,873,521</u>	<u>1,888,606</u>

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

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

	Year ended 31 December 2019	Year ended 31 December 2018
Net gain on precious metals operations	11,041	4,211
Translation difference on precious metals	<u>2,613,841</u>	<u>(215,416)</u>
Total net gain / (loss) on precious metals operations	<u>2,621,882</u>	<u>(211,205)</u>

10. Personnel, general and administrative expenses

Personnel, general and administrative expenses comprises:

	Year ended 31 December 2019	Year ended 31 December 2018
Salaries and bonuses	(20,443,427)	(17,497,906)
Social security costs	(3,269,464)	(3,741,639)
Other employee related expenses	<u>(489,022)</u>	<u>(316,284)</u>
Total personnel expenses	<u>(24,201,913)</u>	<u>(21,555,829)</u>
Payments to the Deposit Insurance Fund of the Republic of Azerbaijan	(3,655,722)	(3,758,078)
Professional services fees	(1,463,825)	(752,023)
Taxes, other than income tax	(1,211,779)	(1,138,598)
Security expenses	(1,158,192)	(990,763)
Membership fees	(902,692)	(1,154,379)
Repairs and maintenance expenses	(770,289)	(787,629)
Advertising and marketing expenses	(658,791)	(650,228)
Transportation and business trip expenses	(541,642)	(470,639)
Entertainment	(528,223)	(269,276)
Communications	(445,082)	(395,729)
Insurance	(430,155)	(352,219)
Utilities	(373,383)	(341,921)
Stationery expenses	(340,916)	(222,194)
Operating leases	(262,319)	(1,282,215)
Other expenses	<u>(620,137)</u>	<u>(1,005,617)</u>
Total general and administrative expenses	<u>(13,361,147)</u>	<u>(13,571,508)</u>

Open Joint Stock Company Xalq Bank

Notes to the consolidated financial statements for the year ended 31 December 2019 (Continued) (in Azerbaijan manats)

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 2019 and 2018 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 2019 and 2018 comprise:

	31 December 2019	31 December 2018
Deductible temporary differences:		
Loans to customers	32,369,443	19,188,248
Other liabilities	7,615,055	3,383,366
Intangible assets	696,780	585,880
Investment securities	89,514	85,790
Total deductible temporary differences	<u>40,770,792</u>	<u>23,243,284</u>
Taxable temporary differences:		
Premises, equipment and right-of-use assets	(16,955,895)	(12,423,595)
Precious metals	(10,755,542)	(8,142,647)
Provision for impairment losses on other operations	(545,489)	(336,959)
Amounts due from credit institutions	(379,437)	(107,645)
Other assets	(17,855,588)	(14,172,038)
Total deductible temporary differences	<u>(46,493,951)</u>	<u>(35,182,884)</u>
Net deferred (taxable) / deductible temporary differences	(5,723,159)	(11,939,600)
Net deferred tax liability at the statutory tax rate (20%)	<u>(1,144,632)</u>	<u>(2,387,920)</u>
Net deferred tax liability	<u>(1,144,632)</u>	<u>(2,387,920)</u>

Relationships between tax expenses and accounting profit for the years ended 31 December 2019 and 2018 are explained as follows:

	Year ended 31 December 2019	Year ended 31 December 2018
Profit before income tax	36,773,222	31,579,667
Tax at the statutory tax rate of 20%	7,355,644	6,315,933
Tax effect of permanent differences	<u>112,361</u>	<u>38,054</u>
Income tax expense	<u>7,468,005</u>	<u>6,353,987</u>
Current income tax expense	8,711,293	7,080,319
Deferred income tax expense	<u>(1,243,288)</u>	<u>(726,332)</u>
Income tax expense	<u>7,468,005</u>	<u>6,353,987</u>

Open Joint Stock Company Xalq Bank

Notes to the consolidated financial statements for the year ended 31 December 2019 (Continued) (in Azerbaijan manats)

	31 December 2019	31 December 2018
Deferred income tax liability		
Beginning of the period	(2,387,920)	(1,457,705)
Effect of adoption of IFRS 9	-	(1,656,547)
Change in the income tax assets for the period charged to profit	<u>1,243,288</u>	<u>726,332</u>
End of the period	<u><u>(1,144,632)</u></u>	<u><u>(2,387,920)</u></u>

12. Earnings per share

The earnings per share are calculated as follows:

	Year ended 31 December 2019	Year ended 31 December 2018
Profit:		
Net profit for the year	29,304,206	25,221,584
Weighted average number of ordinary shares for basic earnings per share	<u>3,630,300</u>	<u>3,630,300</u>
Earnings per share – basic and diluted (AZN)	<u><u>8.072</u></u>	<u><u>6.948</u></u>

13. Cash and cash equivalents

Cash and cash equivalents comprise:

	31 December 2019	31 December 2018
Cash on hand	86,239,162	42,947,648
Correspondent accounts with the Central Bank of Azerbaijan Republic	72,097,863	40,119,798
Correspondent accounts with other banks	175,467,239	85,595,281
Time deposits with Central Bank of Azerbaijan Republic up to 90 days	<u>30,169,494</u>	<u>109,546,785</u>
Total cash and cash equivalents	<u><u>363,973,758</u></u>	<u><u>278,209,512</u></u>

As at 31 December 2019 and 2018 accrued interest income included in cash and cash equivalents amounted to AZN 114,585 and AZN 266,290, 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.

Open Joint Stock Company Xalq Bank

Notes to the consolidated financial statements for the year ended 31 December 2019 (Continued) (in Azerbaijan manats)

14. Amounts due from credit institutions

Amounts due from credit institutions comprise:

	31 December 2019	31 December 2018
Loans and time deposits with other banks	16,675,487	40,890,716
Obligatory reserve with the Central Bank of Azerbaijan Republic	10,677,416	10,156,520
Restricted deposits	9,044,991	15,525,045
	36,397,894	66,572,281
Less: allowance for impairment	(12,139)	(132,316)
Total amounts due from credit institutions	36,385,755	66,439,965

As at 31 December 2019 and 2018 accrued interest income included in due from credit institutions amounted to AZN 79,467 and AZN 63,054, respectively.

As at 31 December 2019 and 2018 the Bank had restricted deposits blocked in support of guarantees issued and plastic cards operations and money transfers totaling AZN 9,044,991 and AZN 15,525,045, 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 2019 is as follows:

	<u>Stage 1</u>	<u>Stage 2</u>	<u>Stage 3</u>	<u>Total</u>
Gross carrying value as at 1 January 2019	66,572,281	-	-	66,572,281
New assets originated	32,388,574	-	-	32,388,574
Assets repaid				
- Principal	(66,473,640)	-	-	(66,473,640)
- Interest	(383,119)	-	-	(383,119)
Unwinding of discount	398,979	-	-	398,979
Amounts written off	-	-	-	-
Foreign exchange adjustments	3,894,819	-	-	3,894,819
At 31 December 2019	36,397,894	-	-	36,397,894

	<u>Stage 1</u>	<u>Stage 2</u>	<u>Stage 3</u>	<u>Total</u>
ECL as at 1 January 2019	(132,316)	-	-	(132,316)
New assets originated	(11,621)	-	-	(11,621)
Assets repaid				
- Principal	132,072	-	-	132,072
- Interest	15	-	-	15
Unwinding of discount	(20)	-	-	(20)
Changes to models and inputs used for ECL calculations	25	-	-	25
Amounts written off	-	-	-	-
Foreign exchange adjustments	(294)	-	-	(294)
At 31 December 2019	(12,139)	-	-	(12,139)

Open Joint Stock Company Xalq Bank

Notes to the consolidated financial statements for the year ended 31 December 2019 (Continued) (in Azerbaijan manats)

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:

	<u>Stage 1</u>	<u>Stage 2</u>	<u>Stage 3</u>	<u>Total</u>
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				
- <i>Principal</i>	(27,015,195)	-	-	(27,015,195)
- <i>Interest</i>	(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

	<u>Stage 1</u>	<u>Stage 2</u>	<u>Stage 3</u>	<u>Total</u>
ECL as at 1 January 2018	(4,179)	-	-	(4,179)
New assets originated	(130,702)	-	-	(130,702)
Assets repaid				
- <i>Principal</i>	2,640	-	-	2,640
- <i>Interest</i>	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)

Open Joint Stock Company Xalq Bank

Notes to the consolidated financial statements for the year ended 31 December 2019 (Continued) (in Azerbaijan manats)

15. Loans to customers

Loans to customers comprise:

	31 December 2019	31 December 2018
Loans to corporate customers	1,294,799,422	1,242,821,009
Loans to individuals	610,185,244	207,664,914
Gross loans to customers at amortised cost	1,904,984,666	1,450,485,923
Less allowance for impairment	(138,165,555)	(118,274,889)
Total loans to customers at amortised cost	1,766,799,111	1,332,211,034

As at 31 December 2019 and 2018 accrued interest income included in loans to customers amounted to AZN 62,302,640 and AZN 53,889,819, 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 2019 is as follows:

<i>Corporate customers</i>	<u>Stage 1</u>	<u>Stage 2</u>	<u>Stage 3</u>	<u>Total</u>
Gross carrying value as at 1 January 2019	959,711,470	-	283,109,539	1,242,821,009
New assets originated	486,207,790	-	5,747,158	491,954,948
Assets repaid				
- Principal	(419,708,954)	-	(32,041,642)	(451,750,596)
- Interest	(51,848,211)	-	(6,070,899)	(57,919,110)
Transfers to Stage 1	14,331,316	-	(14,331,316)	-
Transfers to Stage 2	(1,733,402)	1,733,402	-	-
Transfers to Stage 3	(107,923)	-	107,923	-
Unwinding of discount	51,509,465	-	23,995,979	75,505,444
Recoveries	-	-	-	-
Amounts written off	-	-	(3,895,083)	(3,895,083)
Foreign exchange adjustments	(401,124)	-	(1,516,066)	(1,917,190)
At 31 December 2019	1,037,960,427	1,733,402	255,105,593	1,294,799,422

<i>Corporate customers</i>	<u>Stage 1</u>	<u>Stage 2</u>	<u>Stage 3</u>	<u>Total</u>
ECL as at 1 January 2019	(861,366)	-	(91,861,290)	(92,722,656)
New assets originated	(417,221)	-	(2,712,448)	(3,129,669)
Assets repaid				
- Principal	676,081	-	4,806,429	5,482,510
- Interest	120,929	-	1,258,574	1,379,503
Transfers to Stage 1	(11,679)	-	11,679	-
Transfers to Stage 2	50,955	(50,955)	-	-
Transfers to Stage 3	16,389	-	(16,389)	-
Impact on period end ECL of exposures transferred between stages during the period	(55,954)	-	2,124,402	2,068,448
Unwinding of discount	(126,856)	-	(13,873,384)	(14,000,240)
Changes to models and inputs used for ECL calculations	(1,829,280)	-	(19,637,315)	(21,466,595)
Recoveries	-	-	-	-
Amounts written off	-	-	3,395,083	3,395,083
Foreign exchange adjustments	235	-	18,303	18,538
At 31 December 2019	(2,437,767)	(50,955)	(115,986,356)	(118,475,078)

Open Joint Stock Company Xalq Bank

Notes to the consolidated financial statements for the year ended 31 December 2019 (Continued) (in Azerbaijan manats)

An analysis of changes in the gross carrying value and corresponding ECL in relation to loans to individuals during the year ended 31 December 2019 is as follows:

<i>Individuals</i>	<i>Stage 1</i>	<i>Stage 2</i>	<i>Stage 3</i>	<i>Total</i>
Gross carrying value as at 1 January 2019	168,131,727	610,538	38,922,649	207,664,914
New assets originated	552,614,146	101,197	10,394	552,725,737
Assets repaid				
- <i>Principal</i>	(143,035,566)	(162,773)	(5,962,495)	(149,160,834)
- <i>Interest</i>	(13,422,266)	(44,486)	(1,008,815)	(14,475,567)
Transfers to Stage 1	983,877	(261,506)	(722,371)	-
Transfers to Stage 2	(359,133)	359,133	-	-
Transfers to Stage 3	(753,274)	(202,483)	955,757	-
Unwinding of discount	14,136,500	48,692	3,195,399	17,380,591
Recoveries	-	-	-	-
Amounts written off	-	-	(4,060,838)	(4,060,838)
Foreign exchange adjustments	112,975	(1)	(1,733)	111,241
At 31 December 2019	578,408,986	448,311	31,327,947	610,185,244

<i>Individuals</i>	<i>Stage 1</i>	<i>Stage 2</i>	<i>Stage 3</i>	<i>Total</i>
ECL as at 1 January 2019	(848,373)	(102,970)	(24,600,890)	(25,552,233)
New assets originated	(251,230)	(957)	(8,024)	(260,211)
Assets repaid				
- <i>Principal</i>	283,114	7,813	4,066,426	4,357,353
- <i>Interest</i>	53,461	4,114	409,291	466,866
Transfers to Stage 1	(2,749)	1,825	924	-
Transfers to Stage 2	56,679	(56,679)	-	-
Transfers to Stage 3	233,445	73,399	(306,844)	-
Impact on period end ECL of exposures transferred between stages during the period	(339,941)	11,658	259,111	(69,172)
Unwinding of discount	(55,177)	(5,762)	(2,200,324)	(2,261,263)
Changes to models and inputs used for ECL calculations	575,296	5,217	(1,034,902)	(454,389)
Recoveries	-	-	-	-
Amounts written off	-	-	4,060,838	4,060,838
Foreign exchange adjustments	1	-	1,733	1,734
At 31 December 2019	(295,474)	(62,342)	(19,352,661)	(19,710,477)

Open Joint Stock Company Xalq Bank

Notes to the consolidated financial statements for the year ended 31 December 2019 (Continued) (in Azerbaijan manats)

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:

<i>Corporate customers</i>	<u>Stage 1</u>	<u>Stage 2</u>	<u>Stage 3</u>	<u>Total</u>
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

<i>Corporate customers</i>	<u>Stage 1</u>	<u>Stage 2</u>	<u>Stage 3</u>	<u>Total</u>
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)

Open Joint Stock Company Xalq Bank

Notes to the consolidated financial statements for the year ended 31 December 2019 (Continued) (in Azerbaijan manats)

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:

<i>Individuals</i>	<u>Stage 1</u>	<u>Stage 2</u>	<u>Stage 3</u>	<u>Total</u>
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

<i>Individuals</i>	<u>Stage 1</u>	<u>Stage 2</u>	<u>Stage 3</u>	<u>Total</u>
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)

Open Joint Stock Company Xalq Bank

Notes to the consolidated financial statements for the year ended 31 December 2019 (Continued) (in Azerbaijan manats)

Loans to corporate customers are made in the following industry sectors:

Analysis by industry	31 December 2019	31 December 2018
Construction	370,797,489	364,751,270
Telecommunication	151,056,259	226,706,489
Energy	172,347,616	180,568,059
Agriculture	218,859,519	129,472,169
Mining	98,665,733	126,734,433
Manufacturing	97,371,296	84,056,932
Trading	99,100,985	76,525,532
Financing	13,807,836	14,593,854
Other	72,792,689	39,412,271
	1,294,799,422	1,242,821,009
Less allowance for impairment	(118,475,078)	(92,722,656)
Total loans to corporate customers	1,176,324,344	1,150,098,353

Loans to individuals comprise the following products:

	31 December 2019	31 December 2018
Business loans	407,030,930	32,023,875
Mortgage loans	117,980,986	116,098,553
Consumer loans	73,111,128	55,765,196
Auto loans	9,874,909	3,101,550
Credit cards	2,187,291	675,740
	610,185,244	207,664,914
Less allowance for impairment	(19,710,477)	(25,552,233)
Total loans to individuals	590,474,767	182,112,681

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

	31 December 2019	31 December 2018
Loans collateralized by real estate	858,667,104	668,513,749
Loans collateralized by cash	436,281,912	154,564,618
Loans collateralized by equipment	241,809,397	150,847,270
Loans collateralized by guarantees	80,731,159	93,991,980
Loans collateralized by vehicles	14,624,724	3,674,389
Loans collateralized by trade receivable	9,942,355	1,865,015
Unsecured loans	262,929,015	377,028,902
	1,904,984,666	1,450,485,923
Less allowance for impairment	(138,185,555)	(118,274,889)
Total loans to customers	1,766,799,111	1,332,211,034

As at 31 December 2019 and 2018 the Bank granted 10 and 11 loans totaling AZN 983,195,132 and AZN 786,098,661, respectively, which individually exceeded 10% of the Group's equity.

As at 31 December 2019 and 2018 loans to customers included loans in amount of AZN 364,019,633 and AZN 261,271,476, respectively, whose terms have been renegotiated.

Open Joint Stock Company Xalq Bank

Notes to the consolidated financial statements for the year ended 31 December 2019 (Continued) (in Azerbaijan manats)

As at 31 December 2019 and 2018, 65% and 61% of total amount of loans to customers are given to 17 and 14 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. Investment securities

Investment securities comprise:

	31 December 2019	31 December 2018
Equity securities at FVOCI	447,159	447,258
Debt securities at amortised cost	<u>109,714,137</u>	<u>165,074,412</u>
Total investment securities	<u>110,161,296</u>	<u>165,521,670</u>

As at 31 December 2019 and 2018 accrued interest income included in investments securities amounted to AZN 666,321 and AZN 1,057,578, respectively.

Equity securities at FVOCI	Share %	31 December 2019	Share %	31 December 2018
Azerbaijan Credit Bureau LLC	12.5	250,000	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	2.55	17,800
SWIFT SCRL		<u>4,359</u>		<u>4,458</u>
Total equity securities		<u>447,159</u>		<u>447,258</u>

Debt securities at amortised cost	Coupon rate	31 December 2019	Coupon rate	31 December 2018
Notes issued by Central Bank of Azerbaijan Republic	6%	62,976,990	8%	122,419,900
Bonds issued by SOCAR	5%	27,448,641	5%	27,448,641
Eurobonds issued by CJSC Southern Gas Corridor (SGC)	7%	14,780,561	7%	14,903,551
Bonds issued by Ministry of Finance of the Republic of Azerbaijan	5%	2,585,292	10%	368,110
Notes Issued by the Azerbaijan Mortgage Fund	3%	2,012,167	-	-
Notes issued by other organisations	-	<u>-</u>	12%	<u>20,000</u>
		109,803,651		165,160,202
Less: allowance for impairment		<u>(89,514)</u>		<u>(85,790)</u>
Total debt securities		<u>109,714,137</u>		<u>165,074,412</u>

Open Joint Stock Company Xalq Bank

Notes to the consolidated financial statements for the year ended 31 December 2019 (Continued) (in Azerbaijan manats)

An analysis of changes in the gross carrying values and associated ECLs in relation to debt securities at amortized cost during the year ended 31 December 2019 is as follows:

<i>Debt securities at amortised cost</i>	<i>Central Bank of the AR</i>	<i>SOCAR</i>	<i>SGC and others</i>	<i>Total</i>
Gross carrying value as at 1 January 2019	122,419,900	27,448,641	15,291,661	165,160,202
New assets originated or purchased	1,598,352,231	-	37,120,150	1,635,472,381
Assets repaid				
- <i>Principal</i>	(1,637,462,990)	-	(25,380,113)	(1,662,843,103)
- <i>Interest</i>	(9,001,110)	(1,358,470)	(1,111,629)	(11,471,209)
Assets sold	(20,008,556)	-	(7,577,494)	(27,586,050)
Unwinding of discount (recognised in interest income)	8,677,515	1,358,472	1,035,446	11,071,433
Amounts written off	-	-	-	-
Foreign exchange adjustments	-	(2)	(1)	(3)
At 31 December 2019	62,976,990	27,448,641	19,378,020	109,803,651

<i>Debt securities at amortised cost</i>	<i>Central Bank of the AR</i>	<i>SOCAR</i>	<i>SGC and others</i>	<i>Total</i>
ECLs as at 1 January 2019	(12,385)	(63,392)	(10,013)	(85,790)
New assets originated or purchased	(161,477)	-	(11,649)	(173,126)
Assets repaid				
- <i>Principal</i>	165,428	-	-	165,428
- <i>Interest</i>	909	3,137	1,084	5,130
Assets sold	2,021	-	9,072	11,093
Unwinding of discount (recognised in interest income)	(877)	(3,137)	(993)	(5,007)
Changes to models and inputs used for ECL calculations	19	-	(7,261)	(7,242)
Amounts written off	-	-	-	-
Foreign exchange adjustments	-	-	-	-
At 31 December 2019	(6,362)	(63,392)	(19,760)	(89,514)

All balances of investment securities are allocated to Stage 1.

Open Joint Stock Company Xalq Bank

Notes to the consolidated financial statements for the year ended 31 December 2019 (Continued) (in Azerbaijan manats)

An analysis of changes in the gross carrying values and associated ECLs in relation to debt securities at amortized cost during the year ended 31 December 2018 is as follows:

<i>Debt securities at amortised cost</i>	<i>Central Bank of the AR</i>	<i>SOCAR</i>	<i>SGC and others</i>	<i>Total</i>
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				
- <i>Principal</i>	(1,973,450,863)	-	(5 586,845)	(1,979,037,708)
- <i>Interest</i>	(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

<i>Debt securities at amortised cost</i>	<i>Central Bank of the AR</i>	<i>SOCAR</i>	<i>SGC and others</i>	<i>Total</i>
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				
- <i>Principal</i>	199,653	-	5,881	205,534
- <i>Interest</i>	1,298	3,137	662	5,097
Assets sold	-	-	7,580	7,580
Unwinding of discount (recognised in interest income)	(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.

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.

Open Joint Stock Company Xalq Bank

Notes to the consolidated financial statements for the year ended 31 December 2019 (Continued) (in Azerbaijani manats)

17. Premises, equipment and right-of-use assets

	Land	Buildings	Computers	Vehicles	Furniture & Equipment	Other Equipment	Leasehold Improvements	Construction in progress	Right-of-use assets	Total
Cost at 31 December 2017	1,095,138	74,387,090	4,880,662	6,174,928	12,297,268	1,492,844	671,519	251,028	-	101,250,477
Additions	-	1,046	195,765	1,096,438	1,001,162	63,231	-	555,691	-	2,913,333
Disposals	-	-	(3,109)	(301,180)	(22,656)	-	-	-	-	(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	671,519	740,316	-	103,836,865
IFRS 16 transition effect	-	-	-	-	-	-	-	-	4,552,862	4,552,862
Additions	-	(4,540)	1,079,413	1,554,972	844,787	41,683	-	72,220	-	3,588,535
Disposals	-	-	(1,411)	(612,104)	-	-	-	(761)	-	(614,276)
Transfers	54,000	457,792	421	-	100,674	14,263	-	(627,150)	-	-
Cost at 31 December 2019	1,149,138	74,907,791	6,151,741	7,913,054	14,221,235	1,612,021	671,519	184,625	4,552,862	111,363,986
Accumulated depreciation at 31 December 2017	-	(14,681,417)	(3,918,661)	(3,076,969)	(9,903,265)	(782,010)	(134,304)	-	-	(32,498,626)
Charge for the year	-	(2,476,522)	(253,484)	(655,690)	(992,123)	(135,009)	(67,152)	-	-	(4,579,980)
Disposals	-	-	3,109	257,750	22,656	-	-	-	-	283,515
Accumulated depreciation at 31 December 2018	-	(17,157,939)	(4,169,036)	(3,476,909)	(10,872,732)	(917,019)	(201,456)	-	-	(36,795,091)
Charge for the year	-	(2,488,331)	(245,036)	(836,237)	(1,166,262)	(129,819)	(67,152)	-	(881,921)	(5,814,758)
Disposals	-	-	1,411	610,147	-	-	-	-	-	611,558
Transfers	-	-	-	-	-	-	-	-	-	-
Accumulated depreciation at 31 December 2019	-	(19,646,270)	(4,412,661)	(3,702,999)	(12,038,994)	(1,046,838)	(268,608)	-	(881,921)	(41,998,291)
NBV at 31 December 2018	1,095,138	57,296,600	904,282	3,493,277	2,403,042	639,056	470,063	740,316	-	67,041,774
NBV at 31 December 2019	1,149,138	55,261,521	1,739,080	4,210,055	2,182,241	565,183	402,911	184,625	3,670,941	69,365,695

Open Joint Stock Company Xalq Bank

Notes to the consolidated financial statements for the year ended 31 December 2019 (Continued) (in Azerbaijan manats)

18. Investment properties

Investment properties comprise:

	31 December 2019	31 December 2018
Investment property at fair value at beginning of the year	<u>7,027,246</u>	<u>6,825,306</u>
Additions (subsequent expenditure)	9,963	-
Re-measurement recognised in profit or loss	277,791	201,940
Investment properties at fair value at end of the year	<u>7,315,000</u>	<u>7,027,246</u>

The fair value of investment property as at 31 December 2019 was determined on 30 March 2020 by AIS Azintellektservice, who holds a recognized professional qualification. The basis used for the appraisal was market value.

	Year ended 31 December 2019	Year ended 31 December 2018
Rental income derived from investment properties	419,368	359,368
Direct operating expenses arising from investment property that generated rental income	(305,654)	(322,192)
Direct operating expenses arising from investment property that did not generate rental income	(23,250)	(15,682)
	<u>90,464</u>	<u>21,494</u>

19. Intangible assets

Intangible assets comprise:

	Licenses	Computer software	Other	Total
Cost at 31 December 2017	<u>1,009,534</u>	<u>2,585,408</u>	<u>-</u>	<u>3,594,942</u>
Additions	21,715	303,625	-	325,340
Cost at 31 December 2018	<u>1,031,249</u>	<u>2,889,033</u>	<u>-</u>	<u>3,920,282</u>
Additions	403,584	532,379	3,125	939,088
Cost at 31 December 2019	<u>1,434,833</u>	<u>3,421,412</u>	<u>3,125</u>	<u>4,859,370</u>
Accumulated amortization at 31 December 2017	<u>(483,029)</u>	<u>(1,559,943)</u>	<u>-</u>	<u>(2,042,972)</u>
Charge for the year	(105,684)	(259,971)	-	(365,655)
Accumulated amortization at 31 December 2018	<u>(588,713)</u>	<u>(1,819,914)</u>	<u>-</u>	<u>(2,408,627)</u>
Charge for the year	(129,393)	(285,933)	(625)	(415,951)
Accumulated amortization at 31 December 2019	<u>(718,106)</u>	<u>(2,105,847)</u>	<u>(625)</u>	<u>(2,824,578)</u>
NBV at 31 December 2018	<u>442,536</u>	<u>1,069,119</u>	<u>-</u>	<u>1,511,655</u>
NBV at 31 December 2019	<u>716,727</u>	<u>1,315,565</u>	<u>2,500</u>	<u>2,034,792</u>

Open Joint Stock Company Xalq Bank

Notes to the consolidated financial statements for the year ended 31 December 2019 (Continued) (in Azerbaijan manats)

20. Other assets

Other assets comprise:

	31 December 2019	31 December 2018
Other financial assets		
Settlements on money transfers and plastic cards	3,998,109	3,846,188
Accrued interests on other operations	-	20,447
Other non-financial assets		
Collateral repossessed	47,787,479	60,716,298
Prepayments and receivables on other transactions	4,186,557	494,123
Prepayments for purchase of property and equipment	3,547,181	217,860
Prepayments for purchases of intangible assets	3,178,150	181,818
Prepaid operating taxes	1,199,547	218,584
Deferred expenses	646,405	777,336
Other	101,898	300,339
	<u>64,645,326</u>	<u>66,772,993</u>
Less: Provision for impairment of other non-financial assets	<u>(7,717,931)</u>	<u>(7,976,732)</u>
Total other assets	<u>56,927,395</u>	<u>58,796,261</u>

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

	Other non- financial assets
31 December 2017	(11,299,624)
Recovery of provision	3,039,742
Write-off	<u>283,150</u>
31 December 2018	(7,976,732)
Recovery of provision	<u>258,801</u>
31 December 2019	<u>(7,717,931)</u>

21. Amounts due to banks and government agencies

Amounts due to banks and government agencies comprise:

	31 December 2019	31 December 2018
Amount due to the National Fund for Support of Entrepreneurship	121,179,479	127,381,325
Amount due to State Oil Company of Azerbaijan Republic	114,618,199	34,684,907
Correspondent accounts of other banks	71,496,048	20,617,783
Amount due to Azerbaijan Mortgage Fund	62,138,012	57,561,707
Long-term deposits from banks	13,700,000	103,800,000
Loans from the Central Bank of Azerbaijan Republic	673,595	24,091,778
Amount due to the National Depository Center	-	8,020,133
Total amounts due to banks and government agencies	<u>383,805,333</u>	<u>376,157,633</u>

As at 31 December 2019 and 2018 accrued interest expense included in due to banks and government agencies amounted to AZN 239,403 and AZN 234,280, respectively.

Open Joint Stock Company Xalq Bank

Notes to the consolidated financial statements for the year ended 31 December 2019 (Continued) (in Azerbaijan manats)

22. Customer accounts

Customer accounts comprise:

	31 December 2019	31 December 2018
Time deposits	1,111,491,707	859,949,574
Repayable on demand	<u>524,859,965</u>	<u>475,085,212</u>
Total customer accounts	<u>1,636,351,672</u>	<u>1,335,034,786</u>

As at 31 December 2019 and 2018 accrued interest expense included in customer accounts amounted to AZN 926,032 and AZN 775,553, respectively.

As at 31 December 2019 and 2018 customer accounts amounting to AZN 1,270,653,005 and AZN 1,004,262,036 were due to 15 and 16 customers representing a significant concentration, being approximately 78% and 75%, respectively.

An analysis of customer accounts by economic sector follows:

	31 December 2019	31 December 2018
Individuals	762,038,627	734,096,585
Energy	390,563,710	143,107,979
Investing	240,635,291	245,735,318
Construction	60,725,538	29,493,369
Manufacturing	60,768,213	18,178,382
Transport and communication	48,128,642	67,064,753
Insurance	32,640,221	44,913,408
Trade	21,036,954	31,706,733
Agriculture	2,395,542	6,941,275
Other	<u>17,418,934</u>	<u>13,796,984</u>
Total customer accounts	<u>1,636,351,672</u>	<u>1,335,034,786</u>

23. Other liabilities

Other liabilities comprise:

	31 December 2019	31 December 2018
Other financial liabilities		
Lease liability (Note 4)	3,543,472	-
Settlements on money transfers and plastic cards	2,560,822	1,768,468
Accrued expenses	637,369	183,516
Other non-financial liabilities		
Payables to the employees	4,021,701	3,276,740
Payables to the Deposit Insurance Fund	880,132	880,254
Taxes other than income tax	851,848	733,992
Provisions for ECL for credit related commitments (Note 25)	40,150	61,703
Deferred revenue	57,873	32,229
Other	<u>100,799</u>	<u>212,372</u>
Total other liabilities	<u>12,694,166</u>	<u>7,149,274</u>

Open Joint Stock Company Xalq Bank

Notes to the consolidated financial statements for the year ended 31 December 2019 (Continued) (in Azerbaijan manats)

24. Share capital

As at 31 December 2019 and 2018 the Banks's authorized, issued and fully paid capital amounted to AZN 364,772,544 and AZN 225,078,600 comprising of 3,630,300 ordinary shares with a par value of AZN 100.48 and AZN 62 per ordinary share, respectively. 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 2017	62.00	3,630,300	225,078,600
Capitalization of retained earnings	-	-	-
31 December 2018	62.00	3,630,300	225,078,600
Increase in share capital	29.75	-	107,999,784
Capitalization of retained earnings	8.73	-	31,694,160
31 December 2019	100.48	3,630,300	364,772,544

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 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 2019 and 2018, the Group's commitments and contingencies comprised the following:

	31 December 2019	31 December 2018
Credit related commitments		
Unused credit lines	171,600,226	192,524,895
Letters of credit	1,052,093	1,701,816
Financial guarantees	15,131,820	22,029,552
	187,784,139	216,256,263
Operating lease commitments		
Not later than 1 year	41,919	296,874
Later than 1 year but not later than 5 years	-	1,187,497
Later than 5 years	-	219,809
	41,919	1,704,180
Performance guarantees	30,013,211	24,322,271
Commitments and contingencies before deducting collateral and provision	217,839,269	242,282,714
Less: provisions for ECL for credit related commitments	(40,150)	(61,703)
Less: cash held as security against letters of credit and guarantees	(1,019,851)	(21,896,159)
Commitments and contingencies	216,779,268	220,324,852

Open Joint Stock Company Xalq Bank

Notes to the consolidated financial statements for the year ended 31 December 2019 (Continued) (in Azerbaijan manats)

An analysis of changes in the ECL allowance during the year ended 31 December 2019 is as follows:

	<u>Stage 1</u>	<u>Stage 2</u>	<u>Stage 3</u>	<u>Total</u>
ECL as at 1 January 2018	(9,812)	-	(51,891)	(61,703)
New exposures	(25,059)	-	(1,353)	(26,412)
Amounts paid	-	-	-	-
Exposures expired or derecognised	298	-	51,891	52,189
Transfers to Stage 1	-	-	-	-
Transfers to Stage 2	-	-	-	-
Transfers to Stage 3	-	-	-	-
Changes to models and inputs used for ECL calculations	(4,224)	-	-	(4,224)
Amounts written off	-	-	-	-
At 31 December 2018	<u>(38,797)</u>	<u>-</u>	<u>(1,353)</u>	<u>(40,150)</u>

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

	<u>Stage 1</u>	<u>Stage 2</u>	<u>Stage 3</u>	<u>Total</u>
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
Exposures expired or derecognised	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	<u>(9,812)</u>	<u>-</u>	<u>(51,891)</u>	<u>(61,703)</u>

Capital commitments – The Group had no material commitments for capital expenditures outstanding as at 31 December 2019.

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 2019 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.

Open Joint Stock Company Xalq Bank

Notes to the consolidated financial statements for the year ended 31 December 2019 (Continued) (in Azerbaijan manats)

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 them 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 2019 and 2018 with related parties:

	31 December 2019		31 December 2018	
	Related party transactions	Total category as per financial statements caption	Related party transactions	Total category as per financial statements caption
Loans to customers		1,904,984,666		1,450,485,923
- <i>shareholders and entities in which a substantial interest is owned by shareholders of the Group</i>	-		-	
- <i>key management personnel of the entity</i>	811,832		803,950	
Allowance for impairment losses		(138,185,555)		(118,274,889)
- <i>shareholders and entities in which a substantial interest is owned by shareholders of the Group</i>	-		-	
- <i>key management personnel of the entity</i>	(522)		(1,385)	
Customer accounts		1,636,351,672		1,335,034,786
- <i>shareholders and entities in which a substantial interest is owned by shareholders of the Group</i>	63,274,830		54,365,749	
- <i>key management personnel of the entity</i>	799,976		1,422,576	
Guarantees issued		45,145,031		46,351,823
- <i>shareholders and entities in which a substantial interest is owned by shareholders of the Group</i>	95,175		612,010	
Letters of credit		1,052,093		1,701,816
- <i>shareholders and entities in which a substantial interest is owned by shareholders of the Group</i>	773,573		324,216	
Unused loan commitments		170,600,226		192,524,895
- <i>shareholders and entities in which a substantial interest is owned by shareholders of the Group</i>	121,890,000		-	
- <i>key management personnel of the entity</i>	143,789		142,702	

Open Joint Stock Company Xalq Bank

Notes to the consolidated financial statements for the year ended 31 December 2019 (Continued) (in Azerbaijan manats)

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.

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

	Level 1	Level 2	Level 3	31 December 2019 Total
Assets measured at fair value				
Investment securities	-	4,359	442,800	447,159
Investment property	-	7,315,000	-	7,315,000
Assets for which fair values are disclosed				
Cash and cash equivalents	363,973,758	-	-	363,973,758
Precious metals	17,515,867	-	-	17,515,867
Amounts due from credit institutions	-	36,385,755	-	36,385,755
Investment securities at amortised cost	42,148,680	67,565,457	-	109,714,137
Loans to customers	-	-	1,766,799,111	1,766,799,111
Other assets	-	-	3,998,109	3,998,109
Assets	423,638,305	111,270,571	1,771,240,020	2,306,148,896
Liabilities for which fair values are disclosed				
Amounts due to banks and government agencies	-	-	383,805,333	383,805,333
Customer accounts	-	-	1,636,351,672	1,636,351,672
Other liabilities	-	-	6,741,663	6,741,663
Liabilities	-	-	2,026,898,668	2,026,898,668

Open Joint Stock Company Xalq Bank

Notes to the consolidated financial statements for the year ended 31 December 2019 (Continued) (in Azerbaijan manats)

	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 at amortised cost	-	-	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	-	-	1,758,468	1,768,468
Liabilities	475,085,212	-	1,237,875,675	1,712,960,887

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

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

	31 December 2019			31 December 2018		
	Carrying amount	Fair value	Unrecognised gain	Carrying amount	Fair value	Unrecognised gain
Financial assets						
Cash and cash equivalents	363,973,758	363,973,758	-	278,209,512	278,209,512	-
Precious metals	17,515,867	17,515,867	-	14,989,411	14,989,411	-
Amounts due from credit institutions	36,385,755	36,385,755	-	66,439,965	66,439,965	-
Loans to customers	1,766,799,111	1,766,799,111	-	1,332,211,034	1,332,211,034	-
Investment securities	110,161,296	112,231,163	2,069,867	165,521,670	165,907,828	386,158
Other financial assets	3,998,109	3,998,109	-	3,866,635	3,866,635	-
Financial liabilities						
Amounts due to banks and government agencies	383,805,333	383,805,333	-	376,157,633	376,157,633	-
Customer accounts	1,636,351,672	1,636,351,672	-	1,335,034,786	1,335,034,786	-
Other financial liabilities	6,741,663	6,741,663	-	1,951,984	1,951,984	-
			2,069,867			386,158

The fair value of equity securities included in investment securities cannot be measured reliably. As at 31 December 2019 and 2018 the cost of them was AZN 447,159 and AZN 447,258, 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.

Open Joint Stock Company Xalq Bank

Notes to the consolidated financial statements for the year ended 31 December 2019 (Continued) (in Azerbaijan manats)

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 2019 the Group's total capital amount for Capital Adequacy purposes was AZN 397,129,883 and tier 1 capital amount was AZN 394,141,543 with ratios of 17.90% and 17.77%, respectively.

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 14.69% and 14.57%, 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 2019 and 2018 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 2018.

Open Joint Stock Company Xalq Bank

Notes to the consolidated financial statements for the year ended 31 December 2019 (Continued) (in Azerbaijan manats)

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

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.

Open Joint Stock Company Xalq Bank

Notes to the consolidated financial statements for the year ended 31 December 2019 (Continued) (in Azerbaijan manats)

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 demonstrate 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.

Open Joint Stock Company Xalq Bank

Notes to the consolidated financial statements for the year ended 31 December 2019 (Continued) (in Azerbaijan manats)

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.

Open Joint Stock Company Xalq Bank

Notes to the consolidated financial statements for the year ended 31 December 2019 (Continued) (in Azerbaijan manats)

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

<i>Internal rating grade</i>	<i>International external rating agency (Fitch) rating</i>	<i>Internal rating description</i>	<i>Lifetime PD</i>
>13	AA+ to AAA AA A+ to AA- A- BBB+ BBB BBB-	High grade	0 - 0.13%
8-13	BB+ BB- to BB	Standard grade	0.13 - 2.09%
4-8	B- to B+ CCC CCC-	Sub-standard grade	2.09 - 100%
<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.

Open Joint Stock Company Xalq Bank

Notes to the consolidated financial statements for the year ended 31 December 2019 (Continued) (in Azerbaijan manats)

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	

Open Joint Stock Company Xalq Bank

Notes to the consolidated financial statements for the year ended 31 December 2019 (Continued) (in Azerbaijan manats)

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 2019 included the following key indicators for the Republic of Azerbaijan for the years ending 31 December 2020 through 2024.

Years	Real GDP growth rate
2020	1.68%
2021	1.68%
2022	1.76%
2023	1.84%
2024	1.92%

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.

Open Joint Stock Company Xalq Bank

Notes to the consolidated financial statements for the year ended 31 December 2019 (Continued) (in Azerbaijan manats)

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.

31 December 2019	Note		High grade	Standard grade	Sub-standard grade	Impaired	Total
Cash and cash equivalents, except for cash on hand	13	Stage 1	277,669,208	65,218	17C	-	277,734,596
Amount due from credit institutions	14	Stage 1	34,380,894	2,017,000	-	-	36,397,894
Loans to customers at amortised cost	15						
-Loans to corporate customers		Stage 1	-	982,541,788	55,418,639	-	1,037,960,427
		Stage 2	-	-	1,733,402	-	1,733,402
		Stage 3	-	-	-	255,105,593	255,105,593
-Loans to individuals							
<i>Auto loans</i>		Stage 1	-	9,615,648	176,167	-	9,791,815
		Stage 2	-	-	-	-	-
		Stage 3	-	-	-	83,094	83,094
<i>Consumer loans</i>		Stage 1	-	17,073,564	48,772,540	-	65,846,104
		Stage 2	-	-	12,489	-	12,489
		Stage 3	-	-	-	7,252,535	7,252,535
<i>Mortgage loans</i>		Stage 1	-	111,389,562	2,003,218	-	113,392,780
		Stage 2	-	-	412,278	-	412,278
		Stage 3	-	-	-	4,175,928	4,175,928
<i>Credit cards</i>		Stage 1	-	343,337	1,698,844	-	2,042,181
		Stage 2	-	-	23,544	-	23,544
		Stage 3	-	-	-	121,566	121,566
<i>Business loans</i>		Stage 1	-	15,232,585	372,103,521	-	387,336,106
		Stage 2	-	-	-	-	-
		Stage 3	-	-	-	19,694,824	19,694,824
Investment securities							
- Debt securities at amortised cost	16	Stage 1	65,562,282	27,448,641	16,792,728	-	109,803,651
Letters of credit	25	Stage 1	278,520	773,573	-	-	1,052,093
Financial guarantees	25	Stage 1	4,390,000	10,265,945	475,875	-	15,131,820
Undrawn loan commitments	25	Stage 1	27,535	168,390,674	3,168,413	-	171,586,622
		Stage 2	-	-	-	-	-
		Stage 3	-	-	-	13,604	13,604
Total			382,308,439	1,345,157,535	502,791,828	286,447,144	2,516,704,946

Open Joint Stock Company Xalq Bank

Notes to the consolidated financial statements for the year ended 31 December 2019 (Continued) (in Azerbaijan manats)

31 December 2018	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							
<i>Auto loans</i>		Stage 1	-	2,656,987	87,442	-	2,744,429
		Stage 2	-	-	1,021	-	1,021
		Stage 3	-	-	-	356,099	356,099
<i>Consumer loans</i>		Stage 1	-	43,724,224	495,986	-	44,220,210
		Stage 2	-	-	17,900	-	17,900
		Stage 3	-	-	-	11,527,086	11,527,086
<i>Mortgage loans</i>		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
<i>Credit cards</i>		Stage 1	14,417	514,978	-	-	529,395
		Stage 2	-	98,835	-	-	98,835
		Stage 3	-	-	-	32,946	32,946
<i>Business loans</i>		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	16	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

Financial guarantees, letters of credit and loan commitments are assessed and a provision for expected credit losses is calculated in similar manner as for loans.

Open Joint Stock Company Xalq Bank

Notes to the consolidated financial statements for the year ended 31 December 2019 (Continued)
(in Azerbaijan manats)

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 2019 Total
Assets				
Cash and cash equivalents	214,137,967	433,789	149,402,002	363,973,758
Precious metals	17,515,867	-	-	17,515,867
Amounts due from credit institutions	13,940,094	-	22,445,661	36,385,755
Loans to customers	1,766,799,111	-	-	1,766,799,111
Investment securities	110,156,937	-	4,359	110,161,296
Property, equipment and right-of-use assets	69,365,695	-	-	69,365,695
Investment property	7,315,000	-	-	7,315,000
Intangible assets	2,034,792	-	-	2,034,792
Other assets	56,775,929	78,682	72,784	56,927,395
Total assets	2,258,041,392	512,471	171,924,806	2,430,478,669
Liabilities				
Amounts due to banks and government agencies	383,805,333	-	-	383,805,333
Customer accounts	1,636,351,672	-	-	1,636,351,672
Current income tax liability	306,531	-	-	306,531
Deferred income tax liability	1,144,632	-	-	1,144,632
Other liabilities	12,586,779	11,061	96,326	12,694,166
Total liabilities	2,034,194,947	11,061	96,326	2,034,302,334
Net position	223,846,445	501,410	171,828,480	

Open Joint Stock Company Xalq Bank

Notes to the consolidated financial statements for the year ended 31 December 2019 (Continued) (in Azerbaijan manats)

	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
Current income tax liability	4,159,131	-	-	4,159,131
Deferred income tax liability	2,387,920	-	-	2,387,920
Other liabilities	7,067,513	11	81,750	7,149,274
Total liabilities	1,724,806,983	11	81,750	1,724,888,744
Net position	132,443,467	1,253,023	133,163,294	

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.

Open Joint Stock Company Xalq Bank

Notes to the consolidated financial statements for the year ended 31 December 2019 (Continued) (in Azerbaijan manats)

	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 2019 Total
Assets								
Cash and cash equivalents	2.88%	98,142,443	-	-	-	-	-	98,142,443
Amounts due from credit institutions	1.91%	-	-	16,596,020	-	-	-	16,596,020
Loans to customers	5.04%	24,972,903	34,155,145	400,243,789	929,872,802	368,523,771	-	1,757,771,410
Investment securities	5.69%	64,923,139	-	35,864	27,524,197	16,564,616	-	109,047,816
Total interest bearing assets at fixed rates		89,896,042	34,155,145	416,875,673	957,396,998	385,091,387	-	1,883,415,246
Cash and cash equivalents		265,831,315	-	-	-	-	-	265,831,315
Precious metals		17,515,867	-	-	-	-	-	17,515,867
Amounts due from credit institutions		79,467	-	-	-	-	19,710,268	19,789,735
Loans to customers		2,628,237	-	-	-	-	6,399,464	9,027,702
Investment securities		666,320	-	-	-	-	447,159	1,113,479
Other assets		3,998,109	50,858	-	40,069,548	-	-	44,118,515
		380,615,357	34,206,003	416,875,673	997,466,546	385,091,387	26,556,891	2,240,811,859
Liabilities								
Amounts due to banks and government agencies	1.77%	10,000,000	747,699	108,765,230	43,471,080	149,085,873	-	312,069,883
Customer accounts	1.37%	18,550,767	187,377,160	551,543,638	352,930,274	-	-	1,110,401,839
Total interest bearing liabilities at fixed rates		28,550,767	188,124,859	660,308,868	396,401,354	149,085,873	-	1,422,471,722
Amounts due to banks and government agencies		71,735,450	-	-	-	-	-	71,735,450
Customer accounts		386,607,972	-	-	200,000	-	139,141,861	525,949,833
Current income tax liability		-	-	306,531	-	-	-	306,531
Other liabilities		4,021,223	908,948	5,112,997	2,610,848	-	-	12,654,016
Guarantees issued		5,213,724	1,149,707	33,057,883	5,723,716	-	-	45,145,031
Letters of credit		278,520	773,573	-	-	-	-	1,052,093
Undrawn loan commitments		27,535	5,105,723	11,497,135	18,418,983	136,550,850	-	171,600,226
		496,435,192	196,062,809	710,283,415	423,354,901	285,635,723	139,141,861	2,250,914,902
Liquidity gap		(115,819,835)	(161,856,806)	(293,407,741)	574,111,646	99,454,663		
Interest sensitivity gap for fixed rate instruments		61,345,275	(153,969,714)	(243,433,195)	560,995,645	236,005,513		
Interest sensitivity gap		61,345,275	(153,969,714)	(243,433,195)	560,995,645	236,005,513		
Cumulative interest sensitivity gap		61,345,275	(92,624,439)	(336,057,634)	224,938,011	460,943,524		

Open Joint Stock Company Xalq Bank

Notes to the consolidated financial statements for the year ended 31 December 2019 (Continued) (in Azerbaijan manats)

	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		

Open Joint Stock Company Xalq Bank

Notes to the consolidated financial statements for the year ended 31 December 2019 (Continued) (in Azerbaijan manats)

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 2019		As at 31 December 2018	
	Interest rate +1%	Interest rate -1%	Interest rate +1%	Interest rate -1%
Assets:				
Cash and cash equivalents	981,424	(981,424)	1,279,817	(1,279,817)
Amounts due from credit institutions	165,960	(165,960)	408,277	(408,277)
Loans to customers	17,577,714	(17,577,714)	13,282,926	(13,282,926)
Investment securities	1,090,478	(1,090,478)	1,640,168	(1,640,168)
Liabilities:				
Amounts due to banks and government agencies	(3,120,699)	3,120,699	(3,553,056)	3,553,056
Customer accounts	(3,120,699)	3,120,699	(8,579,260)	8,579,260
Net impact on profit before tax	13,574,178	(13,574,178)	4,478,872	(4,478,872)

Open Joint Stock Company Xalq Bank

Notes to the consolidated financial statements for the year ended 31 December 2019 (Continued) (in Azerbaijan manats)

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 2019 Total
Assets					
Cash and cash equivalents	126,300,276	201,450,981	10,392,134	25,830,367	363,973,758
Precious metals	-	-	-	17,515,867	17,515,867
Amounts due from credit institutions	3,651,506	1,272,593	16,786,169	14,675,487	36,385,755
Loans to customers	335,577,944	1,335,699,770	95,521,397	-	1,766,799,111
Investment securities	67,927,735	42,229,202	4,359	-	110,161,296
Property, equipment and right-of-use assets	69,365,695	-	-	-	69,365,695
Investment property	7,315,000	-	-	-	7,315,000
Intangible assets	2,034,792	-	-	-	2,034,792
Other assets	55,376,060	907,929	329,653	313,753	56,927,395
Total assets	667,549,008	1,581,560,475	123,033,712	58,335,474	2,430,478,669
Liabilities					
Amounts due to banks and government agencies	222,175,994	161,613,726	15,613	-	383,805,333
Customer accounts	338,624,694	1,152,892,950	129,740,538	15,093,490	1,636,351,672
Current income tax liability	306,531	-	-	-	306,531
Deferred income tax liability	1,144,632	-	-	-	1,144,632
Other liabilities	10,582,865	1,311,821	783,497	15,983	12,694,166
Total liabilities	572,834,716	1,315,818,497	130,539,648	15,109,473	2,034,302,334
Net balance sheet position	94,714,292	265,741,978	(7,505,936)	43,226,001	

Open Joint Stock Company Xalq Bank

Notes to the consolidated financial statements for the year ended 31 December 2019 (Continued) (in Azerbaijan manats)

	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
Current income tax liability	4,159,131	-	-	-	4,159,131
Deferred income tax liability	2,387,920	-	-	-	2,387,920
Other liabilities	5,106,890	1,118,222	924,157	5	7,149,274
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	

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 2019		As at 31 December 2018	
	AZN / USD +10%	AZN / USD -10%	AZN / USD +10%	AZN / USD -10%
Impact on profit or loss	26,574,198	(26,574,198)	20,156,650	(20,156,650)

	As at 31 December 2019		As at 31 December 2018	
	AZN / EURO +10%	AZN / EURO -10%	AZN / EURO +10%	AZN / EURO -10%
Impact on profit or loss	(750,594)	750,594	(10,235)	10,235

Open Joint Stock Company Xalq Bank

Notes to the consolidated financial statements for the year ended 31 December 2019 (Continued) (in Azerbaijan manats)

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 13 February 2020 Shareholders of the Bank declared dividends in the amount of AZN 7,260,600 on ordinary shares which was paid on 21 February 2020.

In March 2020 the World Health Organization confirmed the novel coronavirus ("COVID-19") as a global pandemic. There is uncertainty over the magnitude of the global slowdown that will result from this pandemic and its impact on Azerbaijan economy. The Government of Azerbaijan has introduced number of measures aimed at containment of the spread of COVID-19, which have significant social and economic impact. Management is monitoring impact of COVID-19 outbreak on Group's business, customers and employees and follows the official guidance introduced by the Government to safeguard its people and to maintain business continuity. The further spread of COVID-19 is expected to have a negative impact on the economy, however it is too early to fully understand the impact this may have on the Group's business. The Group considers coronavirus (COVID-19) outbreak to be a non-adjusting post balance sheet event.