OJSC PASHA Bank

Consolidated financial statements

Year ended 31 December 2019
together with independent auditor's report

Contents

Independent auditor's report

Consolidated financial statements

Consolidated statement of financial position ... 1
Consolidated statement of profit or loss ... 2
Consolidated statement of comprehensive income ... 3
Consolidated statement of changes in equity ... 4
Consolidated statement of cash flows ... 5

Notes to the consolidated financial statements

1. Principal activities ... 6
2. Basis of preparation ... 6
3. Summary of accounting policies ... 7
4. Significant accounting judgements and estimates ... 22
5. Cash and cash equivalents ... 23
6. Amounts due from credit institutions ... 24
7. Investment securities ... 25
8. Loans to customers ... 27
9. Investment property ... 30
10. Property and equipment ... 31
11. Intangible assets ... 32
12. Other assets and liabilities ... 33
13. Amounts due to banks and government funds ... 34
14. Amounts due to customers ... 35
15. Debt securities issued ... 36
16. Subordinated debts ... 36
17. Derivative financial instruments ... 36
18. Taxation ... 37
19. Equity ... 38
20. Commitments and contingencies ... 39
21. Credit loss expense and other impairment and provisions ... 41
22. Net fee and commission income ... 42
23. Personnel, general and administrative expenses ... 42
24. Risk management ... 43
25. Fair values measurement ... 54
26. Maturity analysis of assets and liabilities ... 57
27. Related party disclosures ... 57
28. Changes in liabilities arising from financing activities ... 59
29. Capital adequacy ... 59
30. Events after the reporting period ... 60

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Independent auditor's report

To the Shareholders and Supervisory Board of OJSC PASHA Bank

Opinion

We have audited the consolidated financial statements of OJSC PASHA Bank and its subsidiaries (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 comprehensive income, 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 consolidated financial position of the Group as at 31 December 2019, and its consolidated financial performance and its consolidated 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 our report. We are independent of the Group in accordance with the International Ethics Standards Board for Accountants' Code of Ethics for Professional Accountants (including International Independence Standards) (IESBA Code), and we have fulfilled our other ethical responsibilities in accordance with the IESBA Code. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Responsibilities of management and 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.

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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.

Ernst & Young Holdings (CIS) B.V.

11 March 2020

Baku, Azerbaijan

Consolidated statement of financial position

As at 31 December 2019

(Figures in tables are in thousands of Azerbaijani manats)

	Notes	2019	2018
Assets			
Cash and cash equivalents	5	1,185,839	1,503,046
Trading securities		–	895
Amounts due from credit institutions	6	624,394	334,834
Investment securities	7	1,146,353	1,458,146
Derivative financial assets	17	457	2,050
Loans to customers	8	2,296,988	1,731,565
Investment property	9	43,202	71,719
Property and equipment	10	46,036	18,236
Intangible assets	11	50,421	49,754
Right-of-use assets	3	9,142	–
Current income tax assets		3,198	–
Deferred income tax assets	18	4,466	4,003
Other assets	12	29,943	35,116
Total assets		**5,440,439**	**5,209,364**
Liabilities			
Amounts due to banks and government funds	13	862,143	524,975
Amounts due to customers	14	3,788,941	3,953,952
Lease liabilities	3	9,537	–
Debt securities issued	15	136,031	102,300
Derivative financial liabilities	17	137	81
Current income tax liabilities		560	5,516
Deferred income tax liabilities	18	13,037	7,886
Provision for guarantees and other commitments	20	10,550	6,425
Subordinated debts	16	27,111	18,921
Other liabilities	12	32,336	41,299
Total liabilities		**4,880,383**	**4,661,355**
Equity			
Share capital	19	333,000	333,000
Additional paid-in capital	19	343	–
Retained earnings		143,432	114,930
Other reserves		1,983	1,983
Net unrealised gain on investment securities		4,668	338
Foreign currency translation reserve		(4,331)	9,774
Total equity attributable to shareholders of the Bank		**479,095**	**460,025**
Non-controlling interests		80,961	87,984
Total equity		**560,056**	**548,009**
Total liabilities and equity		**5,440,439**	**5,209,364**

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

Taleh Kazimov — Chairman of the Executive Board

Bahruz Nagiyev — Chief Financial Officer

11 March 2020

Azərbaycan Respublikası Açıq Səhmdar Cəmiyyəti PAŞA Bank Open Joint Stock Company Azerbaijan Republic

The accompanying notes on pages 6 to 60 are an integral part of these consolidated financial statements.

Consolidated statement of profit or loss

For the year ended 31 December 2019

(Figures in tables are in thousands of Azerbaijani manats)

	Notes	2019	2018
Interest income			
Loans to customers		164,657	140,670
Investment securities		56,586	48,095
Cash and cash equivalents		21,221	27,665
Amounts due from credit institutions		14,639	11,985
Interest revenue calculated using effective interest rate		**257,103**	**228,415**
Finance lease receivables		557	1,151
Other interest revenue		**557**	**1,151**
Interest expense			
Amounts due to customers		(33,985)	(33,630)
Amounts due to banks and government funds		(15,897)	(12,969)
Debt securities issued		(6,184)	(7,536)
Lease liabilities	3	(915)	–
Subordinated debts		(592)	(221)
Other borrowed funds		(85)	(316)
		(57,658)	**(54,672)**
Net interest income		**200,002**	**174,894**
Credit loss expense on financial assets	21	(19,343)	(4,296)
Net interest income after credit loss expense		**180,659**	**170,598**
Net fee and commission income	22	25,622	16,505
Net gains from trading securities		38	176
Net gains from investment securities		–	23
Net gains/(losses) from foreign currencies			
- dealing		25,665	20,562
- translation differences		(300)	(2,819)
- foreign currency derivatives		(1,484)	2,839
Other income		1,842	1,982
Non-interest income		**51,383**	**39,268**
Personnel expenses	23	(57,568)	(51,555)
General and administrative expenses	23	(45,525)	(35,652)
Depreciation and amortisation	3, 9, 10, 11	(18,512)	(8,603)
Impairment of investment property	9	–	(13,546)
Net loss arising on modification of loans to customers	8	(312)	–
Impairment of license and digital products	11	(2,985)	(2,659)
Provision for credit related commitments and other assets	21	(4,364)	(2,867)
Other operating expenses		(353)	–
Non-interest expenses		**(129,619)**	**(114,882)**
Profit before income tax expense		**102,423**	**94,984**
Income tax expense	18	(25,326)	(20,931)
Profit for the year		**77,097**	**74,053**
Attributable to:			
- shareholders of the Bank		73,734	76,298
- non-controlling interests		3,363	(2,245)
		77,097	**74,053**

The accompanying notes on pages 6 to 60 are an integral part of these consolidated financial statements.

Consolidated statement of comprehensive income

For the year ended 31 December 2019

(Figures in tables are in thousands of Azerbaijani manats)

	Notes	2019	2018
Profit for the year		77,097	74,053
Other comprehensive income			
Other comprehensive income to be reclassified to profit or loss in subsequent periods			
Reclassification of cumulative loss on disposal of investment securities at fair value through other comprehensive income to profit or loss		–	(23)
Net change in fair value of investment securities at fair value through other comprehensive income	7	5,362	(323)
Changes in allowance for expected credit losses of investment securities at fair value through other comprehensive income	7, 21	51	756
Net unrealised gains on investment securities at fair value through other comprehensive income	19	**5,413**	**410**
Income tax relating to components of other comprehensive income	18	(1,083)	(82)
Foreign currency translation differences	19	(24,491)	(65,612)
Net other comprehensive loss to be reclassified to profit or loss in subsequent periods		**(20,161)**	**(65,284)**
Total comprehensive income for the year		**56,936**	**8,769**
Attributable to:			
- shareholders of the Bank		63,959	37,120
- non-controlling interests		(7,023)	(28,351)
		56,936	**8,769**

The accompanying notes on pages 6 to 60 are an integral part of these consolidated financial statements.

Consolidated statement of changes in equity

For the year ended 31 December 2019

(Figures in tables are in thousands of Azerbaijani manats)

	Attributable to shareholders of the Bank								
	Share capital	*Additional paid-in capital*	*Retained earnings*	*Net unrealised gain/ (losses) on investment securities*	*Other reserves*	*Foreign currency translation reserve*	*Total*	*Non-controlling interests*	*Total equity*
As at 1 January 2018	**333,000**	**–**	**113,601**	**(24)**	**–**	**52,496**	**499,073**	**76**	**499,149**
Impact of adopting IFRS 9	–	–	(147)	–	–	–	(147)	–	(147)
Restated opening balance under IFRS 9	**333,000**	**–**	**113,454**	**(24)**	**–**	**52,496**	**498,926**	**76**	**499,002**
Profit for the year	–	–	76,298	–	–	–	76,298	(2,245)	74,053
Other comprehensive loss income/(loss) for the year	–	–	–	328	–	(39,506)	(39,178)	(26,106)	(65,284)
Total comprehensive income/(loss) for the year	**–**	**–**	**76,298**	**328**	**–**	**(39,506)**	**37,120**	**(28,351)**	**8,769**
Sale of non-controlling interests (Note 1)	–	–	(11,425)	34	–	(3,216)	(14,607)	116,259	101,652
Transfers to reserves	–	–	(1,983)	–	1,983	–	–	–	–
Dividends to shareholders of the Bank (Note 19)	–	–	(61,414)	–	–	–	(61,414)	–	(61,414)
As at 31 December 2018	**333,000**	**–**	**114,930**	**338**	**1,983**	**9,774**	**460,025**	**87,984**	**548,009**
Profit for the year	–	–	73,734	–	–	–	73,734	3,363	77,097
Other comprehensive income/(loss) for the year	–	–	–	4,330	–	(14,105)	(9,775)	(10,386)	(20,161)
Total comprehensive income/(loss) for the year	**–**	**–**	**73,734**	**4,330**	**–**	**(14,105)**	**63,959**	**(7,023)**	**56,936**
Additional paid-in capital (Note 19)	–	343	–	–	–	–	343	–	343
Dividends to shareholders of the Bank (Note 19)	–	–	(45,232)	–	–	–	(45,232)	–	(45,232)
As at 31 December 2019	**333,000**	**343**	**143,432**	**4,668**	**1,983**	**(4,331)**	**479,095**	**80,961**	**560,056**

The accompanying notes on pages 6 to 60 are an integral part of these consolidated financial statements.

Consolidated statement of cash flows

For the year ended 31 December 2019

(Figures in tables are in thousands of Azerbaijani manats)

	Notes	*2019*	*2018*
Cash flows from operating activities			
Interest received		250,025	228,943
Interest paid		(54,376)	(54,722)
Fees and commissions received		48,553	33,415
Fees and commissions paid		(23,347)	(17,358)
Net realized gains on sale of investment securities		–	23
Net gains from trading securities		36	–
Realised gains less losses from dealing in foreign currencies and foreign currency derivatives		26,370	21,099
Personnel expenses paid		(55,766)	(48,481)
General and administrative expenses paid		(39,799)	(33,427)
Other operating income received		864	2,963
Cash flows from operating activities before changes in operating assets and liabilities		**152,560**	**132,455**
Net (increase)/decrease in operating assets			
Trading securities		835	100
Amounts due from credit institutions		(286,495)	237,877
Loans to customers		(589,451)	(489,145)
Other assets		(4,765)	7,596
Net increase/(decrease) in operating liabilities			
Amounts due to banks and government funds		295,830	169,706
Amounts due to customers		(140,318)	1,086,414
Other borrowed funds		–	(38,575)
Other liabilities		(7,750)	(7,441)
Net cash flows from operating activities before income tax		**(579,554)**	**1,098,987**
Income tax paid		(29,186)	(16,128)
Net cash (used in) / from operating activities		**(608,740)**	**1,082,859**
Cash flows from investing activities			
Proceeds from sale and redemption of investment securities		5,727,314	6,696,415
Purchase of investment securities		(5,393,962)	(7,707,580)
Proceeds from sale of trading securities		–	711
Proceeds from sale of property and equipment		117	19
Purchase and prepayments for property and equipment		(14,768)	(42,709)
Acquisition of intangible assets		(10,019)	(15,743)
Purchase of investment property		(174)	(78,771)
Net cash flows from / (used in) investing activities		**308,508**	**(1,147,658)**
Cash flows from financing activities			
Sale of non-controlling interest		–	101,652
Proceeds from bonds issued	28	103,825	146,132
Redemption of bonds issued	28	(70,901)	(110,453)
Proceeds from subordinated debts	28	8,772	18,700
Finance lease paid	3	(5,548)	–
Dividends paid	19	(45,232)	(61,414)
Net cash (used in) / from financing activities		**(9,084)**	**94,617**
Effect of exchange rates changes on cash and cash equivalents		(7,879)	7,449
Effect of expected credit losses on cash and cash equivalents		(12)	8
Net (decrease)/increase in cash and cash equivalents		**(317,207)**	**37,275**
Cash and cash equivalents, beginning	5	1,503,046	1,465,771
Cash and cash equivalents, ending	5	**1,185,839**	**1,503,046**

The accompanying notes on pages 6 to 60 are an integral part of these consolidated financial statements.

(Figures in tables are in thousands of Azerbaijani manats)

1. Principal activities

OJSC PASHA Bank (the "Bank") was established on 18 June 2007, as an open joint stock company under the laws of the Republic of Azerbaijan. The Bank operates under a banking licence No. 250 issued by the Central Bank of the Republic of Azerbaijan (the "CBAR") on 28 November 2007.

The Bank and its subsidiaries (together – "the Group") accept deposits from the public and extend credit, transfer payments, exchange currencies and provide other banking services to its commercial and private customers.

As at 31 December 2019, the Bank has five service points (2018: five), three branches (2018: two) in Azerbaijan and two subsidiaries (2018: two), JSC PASHA Bank Georgia located in the Republic of Georgia and PASHA Yatirim Bankasi A.Ş. (the "Subsidiaries") located in the Republic of Turkey.

The Bank's registered legal address is 15 Yusif Mammadaliyev Street, Baku, AZ1005, Azerbaijan.

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

Shareholder	*2019, (%)*	*2018, (%)*
PASHA Holding Ltd.	60	60
Ador Ltd.	30	30
Mr. Arif Pashayev	10	10
Total	**100**	**100**

As at 31 December 2019, the Group is ultimately owned by Mrs. Leyla Aliyeva, Mrs. Arzu Aliyeva and Mr. Arif Pashayev (31 December 2018: Mrs. Leyla Aliyeva and Mrs. Arzu Aliyeva) who exercise joint control over the Group.

PASHA Bank Georgia JSC, a wholly – owned subsidiary, is located in the Republic of Georgia, operating in the banking sector, with registered and paid up share capital of GEL 35,000 thousand as at 31 December 2013. In March 2014 share capital of subsidiary was increased and amounted to GEL 103,000 thousand as at 31 December 2019 and 2018. PASHA Bank Georgia JSC operates under a banking licence issued by the National Bank of Georgia (the "NBG") on 17 January 2013.

Legal address of the PASHA Bank Georgia JSC is 15 Rustaveli Street, Tbilisi, GE 0108, Georgia.

TAIB Yatirim Bank A.Ş. was incorporated in 1987 as an investment bank in Turkey with the permission of the Council of Ministers decision No. 6224 which allows the transfer of the banks' net profit after statutory liabilities and in case of liquidation the transfer of capital to foreign shareholders. On 27 January 2015, the Bank acquired 79.47% of the voting common shares of TAIB Yatirim Bank A.Ş. and it was renamed to PASHA Yatirim Bankasi A.Ş. at the registration of the Bank as shareholder. In March 2015, investment in share capital of the subsidiary was increased by TRY 175,000 thousand to TRY 255,000 thousand increasing ownership in subsidiary to 99.92%. On 6 June 2018, share capital of subsidiary was increased by TRY 245,000 thousand to TRY 500,000 thousand. The increase was made based on decision of Supervisory Board of the Bank, according to which newly issued shares were acquired by PASHA Holding Ltd. As a result, the Bank's shares in the subsidiary decreased from 99.92% to 50.96% and PASHA Holding Ltd became a new non-controlling shareholder with ownership of 49% as at 31 December 2019. Head office of PASHA Yatirim Bankasi A.Ş. is located in Istanbul. The activities of the bank are regulated by the Central Bank of the Republic of Turkey (the "CBRT").

OJSC PASHA Bank and its Subsidiaries (together – "the Group") were consolidated in these financial statements.

2. Basis of preparation

General

These consolidated financial statements have been prepared in accordance with International Financial Reporting Standards ("IFRS").

The Azerbaijani manat is the functional and presentation currency of OJSC PASHA Bank as the majority of the transactions are denominated, measured, or funded in Azerbaijani manat. Transactions in other currencies are treated as transactions in foreign currencies. The Group is required to maintain its records and prepare its financial statements in Azerbaijani manat and in accordance with IFRS. These consolidated financial statements are presented in thousands of Azerbaijani manat ("AZN"), except per share amounts and unless otherwise indicated. The consolidated financial statements have been prepared under the historical cost convention except as disclosed in the accounting policies, for certain investment securities at FVOCI and derivative financial instruments which have been measured at fair value.

(Figures in tables are in thousands of Azerbaijani manats)

3. Summary of accounting policies

Changes in accounting policies

The Group applied for the first time certain amendments to the standards, which are effective for annual periods beginning on or after 1 January 2019. The Group has not early adopted any standards, interpretations or amendments that have been issued but are not yet effective. The nature and the impact of each amendment is 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*. The standard 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 as either operating or finance leases using similar principles as in IAS 17. Therefore, IFRS 16 did not have an impact for leases where the Group is the lessor.

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 recognized 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 value ('low-value assets').

The effect of adoption IFRS 16 as at 1 January 2019 (increase/(decrease)) is as follows:

Assets	
Right-of-use assets	14,034
Other assets	(212)
Total assets	**13,822**
Liabilities	
Lease liabilities	13,822
Total liabilities	**13,822**

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

The Group has lease contracts for various items of property and equipment. 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 capitalised 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 recognised 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.

<u>Leases previously accounted for as operating leases</u>

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. For all leases of the Group, the right-of-use assets were recognized based on the amount equal to the lease liabilities, adjusted for any related prepaid and accrued lease payments previously recognized. 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.

3. Summary of accounting policies (continued)

Changes in accounting policies (continued)

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 14,034 thousands were recognized.
- Lease liabilities of AZN 13,822 thousand were recognised;
- Prepayments of AZN 212 thousand related to previous operating leases were derecognised;

The lease liabilities as at 1 January 2019 can be reconciled to the operating lease commitments as of 31 December 2018 as follows:

Operating lease commitments as at 31 December 2018	**24,087**
Weighted average incremental borrowing rate as at 1 January 2019	7%
Discounted operating lease commitments at 1 January 2019	**22,295**
Less:	
Commitments relating to short-term leases	(24)
Commitments relating to lease agreements with the change of management estimation about lease agreement terms	(8,449)
Lease liabilities as at 1 January 2019	**13,822**

(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:

<u>Group as a lessee</u>

The Group applies 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 the underlying assets.

<u>Right-of-use assets</u>

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.

<u>Lease liabilities</u>

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.

3. Summary of accounting policies (continued)

Changes in accounting policies (continued)

In calculating the present value of lease payments, the Group uses 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 (i.e., below USD 5,000). 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.

The Group has the option, under some of its leases to lease the assets for additional years. The Group applies judgement in evaluating whether it is reasonably certain to exercise the option to renew. That is, it considers all relevant factors that create an economic incentive for it to exercise the renewal. After the commencement date, the Group reassesses the lease term if there is a significant event or change in circumstances that is within its control and affects its ability to exercise (or not to exercise) the option to renew (e.g., a change in business strategy).

Amounts recognised in the consolidated statement of financial position, consolidated income statement and consolidated statement of cash flows

Set out below, are the carrying amounts of the Group's right-of-use assets and lease liabilities and the movements during the period:

	Right-of-use assets	*Lease liabilities*
As at 1 January 2019	**14,034**	**13,822**
Additions	445	445
Depreciation expense	(5,280)	–
Interest expense	–	915
Payments	–	(5,548)
Foreign currency translation difference	(57)	(97)
As at 31 December 2019	**9,142**	**9,537**

The Group had total cash outflows for leases of AZN 5,548 thousand in 2019. The Group also had non-cash additions to right-of-use assets and lease liabilities of AZN 445 thousand in 2019.

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 Taxes*. 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 determines whether to consider each uncertain tax treatment separately or together with one or more other uncertain tax treatments and uses the approach that better predicts the resolution of the uncertainty.

3. Summary of accounting policies (continued)

Changes in accounting policies (continued)

Upon adoption of the Interpretation, the Group considered whether it has any uncertain tax positions, particularly those relating to transfer pricing. The Bank's and the subsidiaries' tax filings in different jurisdictions include deductions related to transfer pricing and the taxation authorities may challenge those tax treatments. The Group determined, based on its tax compliance and transfer pricing study, that it is probable that its tax treatments (including those for the subsidiaries) will be accepted by the taxation authorities. The Interpretation did 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 an 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.

Annual improvements 2015-2017 cycle

IFRS 3 Business Combinations

The amendments clarify that, when an entity obtains control of a business that is a joint operation, it applies the requirements for a business combination achieved in stages, including remeasuring previously held interests in the assets and liabilities of the joint operation at fair value. In doing so, the acquirer remeasures its entire previously held interest in the joint operation.

An entity applies those amendments to business combinations for which the acquisition date is on or after the beginning of the first annual reporting period beginning on or after 1 January 2019, with early application permitted.

These amendments had no impact on the consolidated financial statements of the Group as there is no transaction where joint control is obtained.

IAS 12 Income Taxes

The amendments clarify that the income tax consequences of dividends are linked more directly to past transactions or events that generated distributable profits than to distributions to owners. Therefore, an entity recognises the income tax consequences of dividends in profit or loss, other comprehensive income or equity according to where it originally recognised those past transactions or events.

An entity applies the amendments for annual reporting periods beginning on or after 1 January 2019, with early application permitted. When the entity first applies those amendments, it applies them to the income tax consequences of dividends recognised on or after the beginning of the earliest comparative period.

Since the Group's current practice is in line with these amendments, they had no impact on the consolidated financial statements of the Group.

Basis of consolidation

Subsidiaries, which are those entities which are controlled by the Group, are consolidated. Control is achieved when the Group is exposed, or has rights, to variable returns from its involvement with the investee and has the ability to affect those returns through its power over the investee. Specifically, the Group controls an investee if, and only if, the Group has:

- Power over the investee (i.e., existing rights that give it the current ability to direct the relevant activities of the investee);
- Exposure, or rights, to variable returns from its involvement with the investee;
- The ability to use its power over the investee to affect its returns.

3. Summary of accounting policies (continued)

Basis of consolidation (continued)

Generally, there is a presumption that a majority of voting rights results in control. To support this presumption and when the Group has less than a majority of the voting or similar rights of an investee, the Group considers all relevant facts and circumstances in assessing whether it has power over an investee, including:

- The contractual arrangement(s) with the other vote holders of the investee;
- Rights arising from other contractual arrangements;
- The Group's voting rights and potential voting rights.

Subsidiaries are consolidated from the date on which control is transferred to the Group and are no longer consolidated from the date that control ceases. All intra-group transactions, balances and unrealised gains on transactions between group companies are eliminated in full; unrealised losses are also eliminated unless the transaction provides evidence of an impairment of the asset transferred. Where necessary, accounting policies for subsidiaries have been changed to ensure consistency with the policies adopted by the Group.

A change in the ownership interest of a subsidiary, without a change of control, is accounted for as an equity transaction. Losses are attributed to the non-controlling interests even if that results in a deficit balance.

If the Group loses control over a subsidiary, it derecognises the assets (including goodwill) and liabilities of the subsidiary, the carrying amount of any non-controlling interests, the cumulative translation differences, recorded in equity; recognises the fair value of the consideration received, the fair value of any investment retained and any surplus or deficit in profit or loss and reclassifies the parent's share of components previously recognised in other comprehensive income to profit or loss.

Business combinations

Business combinations are accounted for using the acquisition method. The cost of an acquisition is measured as the aggregate of the consideration transferred, measured at acquisition date fair value and the amount of any non-controlling interests in the acquiree. For each business combination, the acquirer measures the non-controlling interests in the acquiree that are present ownership interests either at fair value or at the proportionate share of the acquiree's identifiable net assets and other components of non-controlling interests at their acquisition date fair value. Acquisition costs incurred are expensed.

When the Group acquires a business, it assesses the financial assets and liabilities assumed for appropriate classification and designation in accordance with the contractual terms, economic circumstances and pertinent conditions as at the acquisition date. This includes the separation of embedded derivatives in host contracts by the acquiree.

If the business combination is achieved in stages, the acquisition date fair value of the acquirer's previously held equity interest in the acquiree is remeasured to fair value as at the acquisition date through profit or loss.

Any contingent consideration to be transferred by the acquirer is recognised at fair value at the acquisition date. Subsequent changes to the fair value of the contingent consideration which is deemed to be an asset or liability, will be recognised in accordance with IFRS 9 either in profit or loss or as change to other comprehensive income. If the contingent consideration is classified as equity, it shall not be remeasured until it is finally settled within equity.

Goodwill is initially measured at cost being the excess of the consideration transferred over the acquiree's net identifiable assets acquired and liabilities assumed. If this consideration is lower than the fair value of the net assets of the subsidiary acquired, the difference is recognised in profit or loss.

After initial recognition, goodwill is measured at cost less any accumulated impairment losses. For the purpose of impairment testing, goodwill acquired in a business combination is, from the acquisition date, allocated to each of the Group's cash generating units that are expected to benefit from the combination, irrespective of whether other assets or liabilities of the acquiree are assigned to those units. Where goodwill forms part of a cash-generating unit and part of the operation within that unit is disposed of, the goodwill associated with the operation disposed of is included in the carrying amount of the operation when determining the gain or loss on disposal of the operation. Goodwill disposed of in this circumstance is measured based on the relative values of the operation disposed of and the portion of the cash-generating unit retained.

(Figures in tables are in thousands of Azerbaijani manats)

3. Summary of accounting policies (continued)

Fair value measurement

The Group measures financial instruments carried at FVPL and FVOCI at fair value at each balance sheet date.

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

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

The principal or the most advantageous market must be accessible by the 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 categorized 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 recognized 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 market place.

Initial measurement

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

Measurement categories of financial assets and liabilities

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

- Amortised cost;
- FVOCI;
- FVPL.

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

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.

(Figures in tables are in thousands of Azerbaijani manats)

3. Summary of accounting policies (continued)

Financial assets and liabilities (continued)

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

The Group only measures amounts due from credit institutions, loans to customers and investment securities at amortised cost if both of the following conditions are met:

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

The details of these conditions are outlined below.

Business model assessment

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

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

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

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

The SPPI test

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

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

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

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

Debt instruments at FVOCI

The Group measures debt instruments 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.

3. Summary of accounting policies (continued)

Financial assets and liabilities (continued)

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

The ECLs for debt instruments measured at FVOCI do not reduce the carrying amount of these financial assets in the consolidated 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.

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.

The Group occasionally issues loan commitments at below market interest rates drawdown. Such commitments are initially recognized at fair value and subsequently measured at the higher of the amount of the ECL allowance and the amount initially recognised less, when appropriate, the cumulative amount of income recognised.

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

The Group does not reclassify its financial assets subsequent to their initial recognition, apart from the exceptional circumstances in which the Group changes the business model for managing financial assets. Financial liabilities are never reclassified. The Group did not reclassify any of its financial assets and liabilities in 2019 and 2018.

Cash and cash equivalents

Cash and cash equivalents consist of cash on hand, amounts due from the CBAR, NBG and CBRT, excluding obligatory reserves, and amounts due from credit institutions with due on demand or up to 3 months from the date of origination and that are free from contractual encumbrances.

(Figures in tables are in thousands of Azerbaijani manats)

3. Summary of accounting policies (continued)

Repurchase and reverse repurchase agreements

Sale and repurchase agreements ("repos") are treated as secured financing transactions. Securities sold under sale and repurchase agreements are retained in the consolidated statement of financial position and, in case the transferee has the right by contract or custom to sell or re-pledge them, reclassified as securities pledged under sale and repurchase agreements. The corresponding liability is presented within amounts due to credit institutions or customers.

Securities purchased under agreements to resell ("reverse repo") are recorded as separate account on the consolidated statement of financial position if material or as cash and cash equivalents or loans to customers as appropriate. The difference between sale and repurchase price is treated as interest and accrued over the life of repo agreements using the effective yield method.

Securities lent to counterparties are retained in the consolidated statement of financial position. Securities borrowed are not recorded in the consolidated statement of financial position, unless these are sold to third parties, in which case the purchase and sale are recorded within gains less losses from trading securities in the consolidated statement of profit or loss. The obligation to return them is recorded at fair value as a trading liability.

Derivative financial instruments

In the normal course of business, the Group enters into various derivative financial instruments including futures, forwards, swaps and options in the foreign exchange and capital markets. Such financial instruments are held for trading and are recorded at fair value. The fair values are estimated based on quoted market prices or pricing models that take into account the current market and contractual prices of the underlying instruments and other factors. Derivatives are carried as assets when their fair value is positive and as liabilities when it is negative.

Gains and losses resulting from these instruments are included in the consolidated statement of profit or loss as net gains/(losses) from financial instruments at fair value through profit or loss or net gains/(losses) from foreign currencies, depending on the nature of the instrument.

An embedded derivative is a component of a hybrid instrument that also includes a non-derivative host contract with the effect that some of the cash flows of the combined instrument vary in a way similar to a stand-alone derivative. An embedded derivative causes some or all of the cash flows that otherwise would be required by the contract to be modified according to a specified interest rate, financial instrument price, commodity price, foreign exchange rate, index of prices or rates, credit rating or credit index, or other variable, provided that, in the case of a non-financial variable, it is not specific to a party to the contract. A derivative that is attached to a financial instrument, but is contractually transferable independently of that instrument, or has a different counterparty from that instrument, is not an embedded derivative, but a separate financial instrument.

Derivatives embedded in liabilities and non-financial host contacts are treated as separate derivatives and recorded at fair value if they met the definition of a derivative (as defined above), their economic characteristics and risks were not closely related to those of the host contract, and the host contract was not itself held for trading or designated at FVPL. The embedded derivatives separated from the host were carried at fair value in the trading portfolio with changes in fair value recognised in the consolidated statement of profit or loss.

Financial assets are classified based on the business model and SPPI assessments.

Borrowings

Issued financial instruments or their components are classified as liabilities, where the substance of the contractual arrangement results in the Group having an obligation either to deliver cash or another financial asset to the holder, or to satisfy the obligation other than by the exchange of a fixed amount of cash or another financial asset for a fixed number of own equity instruments. Such instruments include amounts due to banks and government funds, other borrowed funds, debt securities issued, subordinated debts and amounts due to customers. After initial recognition, borrowings are subsequently measured at amortised cost using the effective interest method. Gains and losses are recognised in profit or loss when the borrowings are derecognised as well as through the amortisation process.

If the Group purchases its own debt, it is removed from the statement of financial position and the difference between the carrying amount of the liability and the consideration paid is recognised in profit or loss.

3. Summary of accounting policies (continued)

Offsetting of financial instruments

Financial assets and liabilities are offset and the net amount is reported in the consolidated statement of financial position when there is a legally enforceable right to set off the recognised amounts and there is an intention to settle on a net basis, or to realise the asset and settle the liability simultaneously. The right of set-off must not be contingent on a future event and must be legally enforceable in all of the following circumstances:

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

These conditions are not generally met in master netting agreements, and the related assets and liabilities are presented gross in the consolidated statement of financial position.

Renegotiated loans

Where possible, the Group 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 Group 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. Restructuring of impaired loans does not result in derecognition of financial instrument. When assessing whether or not to derecognise a loan to a customer, amongst others, the Group 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 Group records a modification gain or loss, presented within interest revenue calculated using EIR in the consolidated statement of profit or loss, to the extent that an impairment loss has not already been recorded.

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.

3. Summary of accounting policies (continued)

Derecognition of financial assets and liabilities (continued)

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.

Taxation

The current income tax expense is calculated in accordance with the regulations of the Republic of Azerbaijan and of the countries in which the Group has offices and branches and where its subsidiaries are located.

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

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

Azerbaijan also has various operating taxes that are assessed on the Group's activities. These taxes are included as a component of general and administrative expenses.

Current and deferred tax are recognised in profit or loss, except when they relate to items that are recognised in other comprehensive income or directly in equity, in which case, the current and deferred tax are also recognised in other comprehensive income or directly in equity respectively. Where current tax or deferred tax arises from the initial accounting for a business combination, the tax effect is included in the accounting for the business combination.

Property and equipment

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

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

Depreciation of an asset, including construction in progress, begins when it is ready and available for use. Depreciation is calculated on a straight-line basis over the following estimated useful lives:

	Years
Buildings	20-50
Furniture and fixtures	4-10
Computers and other equipment	3-10
Vehicles	4-5
Other equipment	3-10
Leasehold improvements	4-7

The asset's residual values, useful lives and methods are reviewed, and adjusted as appropriate, at each financial year-end. Costs related to repairs and renewals are charged when incurred and included in general and administrative expenses, unless they qualify for capitalization.

3. Summary of accounting policies (continued)

Investment property

Investment property held is land and building with a useful life up to 50 years or a part of building held to earn rental income or for capital appreciation and which is not used by the Group or held for the sale in the ordinary course of business. Property that is being constructed or developed or redeveloped for future use as investment property is also classified as investment property.

Investment property is initially recognized at cost, including transaction costs, and subsequently is stated at cost less accumulated depreciation and any accumulated impairment losses. For disclosure purposes investment property is re-measured at fair value reflecting market conditions at the end of the reporting period. Fair value of the Group's investment property is determined on the base of various sources including reports of independent appraisers, who hold a recognized and relevant professional qualification and who have recent experience in valuation of property of similar location and category.

Earned rental income is recorded in the income statement within income arising from non-banking activities. Gains and losses resulting from changes in the fair value of investment property are recorded in the consolidated statement of profit or loss and presented within income or expense arising from non-banking activities.

Subsequent expenditure is capitalized only when it is probable that future economic benefits associated with it will flow to the Group and the cost can be measured reliably. All other repairs and maintenance costs are expensed when incurred. If an investment property becomes owner-occupied, it is reclassified to premises and equipment, and its carrying amount at the date of reclassification becomes its deemed cost to be subsequently depreciated.

Repossessed collateral

In certain circumstances, collateral is repossessed following the foreclosure on loans that are in default. Repossessed collateral is measured at the lower of carrying amount and net realizable value and reported within "Other assets".

Intangible assets

Intangible assets include internally developed digital products, banking license, other licenses and computer software.

Intangible assets are measured on initial recognition measured at cost, once capitalization criteria is met, less accumulated amortisation and provisions for impairment The cost of intangible assets acquired in a business combination is fair value as at the date of acquisition. Internally generated assets not fully completed as of reporting date, however meeting capitalisation criteria, are recognised as "Intangible assets in-progress". Group divides the process of generation of the asset into a research phase and a development phase, after which the cost related internally developed products is capitalised. Only development costs for internally generated asset are capitalised, which are subject to meeting specific criteria, as demonstration of technical feasibility, the effectiveness of performance initially intended by the management and provision of future cash benefit.

Following initial recognition, intangible assets are carried at cost less any accumulated amortisation and any accumulated impairment losses.

The useful lives of acquired intangible assets are assessed to be indefinite. Acquired intangible assets with definite lives are amortised over the useful economic lives of up to 10 years. The amortization period for the digital products is set at period of 5-8 years at the outset with subsequent reassessment of remaining life at the end of each year. The amortization of internally developed digital products starts when an asset is available for use in the condition necessary to operate as intended by management.

Intangible assets with indefinite useful lives are not amortised and assessed for impairment at least at each financial year-end whenever there is an indication that the intangible asset may be impaired.

Provisions

Provisions are recognised 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 amount of obligation can be made.

Retirement and other employee benefit obligations

The Group does not have any pension arrangements separate from the State pension system of the Republic of Azerbaijan, which requires current contributions by the employer calculated as a percentage of current gross salary payments; such expense is charged in the period the related salaries are earned. In addition, the Group has no significant post-employment benefits.

3. Summary of accounting policies (continued)

Share capital

Share capital

Ordinary shares and non-redeemable preference shares with discretionary dividends are both 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

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

Contingencies

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

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 and expense is recognised.

Interest and similar income and expense

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

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

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

Interest revenue on all financial assets at FVPL is recognised using the contractual interest rate in "Other interest revenue" in the consolidated statement of profit or loss.

Fee and commission income

The Group earns fee and commission income from several types 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.

(Figures in tables are in thousands of Azerbaijani manats)

3. Summary of accounting policies (continued)

Recognition of income and expenses (continued)

Fee income from providing transaction services

Fees arising from negotiating or participating in the negotiation of a transaction for a third party – such as where the Group's performance obligation is the arrangement of the acquisition of shares or other securities – are recognised on completion of the underlying transaction. Fees or components of fees that are linked to certain performance obligations are recognised after fulfilling the corresponding criteria. When the contract provides for a variable consideration, fee and commission income is only recognized to the extent that it is probable that a significant reversal in the amount of cumulative revenue recognized will not occur until the uncertainty associated with the variable consideration is subsequently resolved. Revenue is recognized when the Group's right to receive the payment is established.

Customer loyalty programs

The Group offers a number customer loyalty programs. Accounting for such programs varies depending on who is identified as the customer, and whether the Group acts as an agent or as a principal under the contract.

The Group has launched a loyalty program for its customers with incentives to sell their banking cards, which is a new product with conditions and a set of privileges unique to the Miles & Smiles Frequent Flyer Programme. According the programme the Group is a principal that obtains control of specified number of miles, so that is an only an inventory risk owner, as well as determines conversion rate of miles. Thus, the nature of Group's promise is a performance obligation to provide the specified miles to the customer, which are initially bought from airlines.

The Group assesses active miles as inventory in the form of materials to be consumed in the rendering of services. At each reporting period and recognizes them at lower cost and net realizable value.

The Group generally recognizes a liability for the accumulated miles that are expected to be utilized by the customers, which is reversed to profit or loss as the points expire. Thus, the revenues from rendering services using loyalty program are allocated to the obligation to satisfy the loyalty points i.e. miles and deferred until those points are accrued to customers individual airline accounts, so that transfers control of miles.

Dividend income

Revenue is recognised when the Group's right to receive the payment is established.

Foreign currency translation

The consolidated financial statements are presented in AZN, which is the Group's functional and presentation currency. Transactions in foreign currencies are initially recorded in the functional currency, converted at the rate of exchange ruling at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies are retranslated at the functional currency rate of exchange ruling at the reporting date. Gains and losses resulting from the translation of foreign currency transactions are recognised in current year profit as gains less losses from foreign currencies – translation differences. Non-monetary items that are measured in terms of historical cost in a foreign currency are translated using the exchange rates as at the dates of the initial transactions. Non-monetary items measured at fair value in a foreign currency are translated using the exchange rates at the date when the fair value was determined.

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

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

	2019	*2018*
1 US dollar	AZN 1.7000	AZN 1.7000
1 Euro	AZN 1.9035	AZN 1.9468
1 Georgian lari	AZN 0.5936	AZN 0.6367
1 Turkish lira	AZN 0.2858	AZN 0.3212

3. Summary of accounting policies (continued)

Standards issued but not yet effective

The new and amended standards and interpretations that are issued, but not yet effective, up to the date of issuance of the Group's financial statements are disclosed below. The Group intends 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 transactions 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 of 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 statements, 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 consolidated 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 earlier. The amendments are not expected to have a significant impact on the Group's consolidated financial statements.

4. Significant accounting judgements and estimates

Estimation uncertainty

In the process of applying the Bank's accounting policies, management has used its judgments and made estimates in determining the amounts recognized in the consolidated financial statements. The most significant use of judgments and estimates are as follows:

Impairment losses on financial assets

The measurement of impairment losses across all categories of financial assets requires judgement, in particular, the estimation of the amount and timing of future cash flows and collateral values when determining impairment losses and the assessment of a significant increase in credit risk. These estimates are driven by a number of factors, changes in which can result in different levels of allowances. The Group's ECL calculations are outputs of complex models with a number of underlying assumptions regarding the choice of variable inputs and their interdependencies. Elements of the ECL models that are considered accounting judgements and estimates include:

- The Group's internal credit grading model, which assigns PDs to the individual grades;
- The Group's criteria for assessing if there has been a significant increase in credit risk and so allowances for financial assets should be measured on a LTECL basis and the qualitative assessment;
- The segmentation of financial assets when their ECL is assessed on a collective basis;
- Development of ECL models, including the various formulae and the choice of inputs;
- Determination of associations between macroeconomic scenarios and, economic inputs and the effect on PDs, EADs and LGDs;
- Selection of forward-looking macroeconomic scenarios and their probability weightings, to derive the economic inputs into the ECL models.

More details are provided in Notes 8 and 24.

Fair value of financial instruments

Where the fair values of financial assets and financial liabilities recorded in the consolidated statement of financial position cannot be derived from active markets, they are determined using a variety of valuation techniques that include the use of mathematical models. The input to these models is taken from observable markets where possible, but where this is not feasible, a degree of judgment is required in establishing fair values. Additional details are provided in Note 25.

Impairment of banking license

The recoverable amount of banking license is measured annually, irrespective of whether there is any indication that it may be impaired. This requires an estimation of the value in use of the cash-generating unit. Estimating the value in use requires the Group to make an estimate of the expected future cash flows from the cash-generating unit and also to choose a suitable discount rate in order to calculate the present value of those cash flows. The Group reviews and validates at the end of each reporting period its decision to classify the useful life of an intangible asset as indefinite. If events and circumstances no longer support an indefinite useful life, the change from indefinite to finite life is accounted for as a change in accounting estimate under IAS 8, which requires such changes to be recognised prospectively.

Furthermore, reassessing the useful life of an intangible asset as finite rather than indefinite is an indicator that the asset may be impaired. The carrying amount of banking license at 31 December 2019 was AZN 16,709 thousand (31 December 2018: AZN 19,892 thousand). More details are provided in Note 11.

Impairment of digital products

At the end of each reporting period the Group assesses an impairment trigger of each digital product. If any such indication exists, the Group estimates the recoverable amount of the asset. The recoverable amount is the higher of the asset's fair value less costs of disposal and its value in use. At each reporting date the Group assesses whether the product still complies with the predetermined needs of the Group and whether the value in use corresponds with the carrying value. The impairment assessment requires an estimation of the value in use of the cash-generating unit.

(Figures in tables are in thousands of Azerbaijani manats)

4. Significant accounting judgements and estimates (continued)

Estimation uncertainty (continued)

Estimating the value in use requires the Group to make an estimate of the expected future cash flows from each cash-generating unit and also to choose a suitable discount rate in order to calculate the present value of those cash flows. Thus, in the measuring value in use the Group:

- Bases cash flow projections on reasonable and supportable assumptions that represent management's best estimate of the range of economic conditions that will exist over the remaining useful life of particular digital product;
- Bases cash flow projections on the most recent financial budgets/forecasts approved by management. Projections based on these budgets/forecasts shall cover a maximum period of five years, unless a longer period can be justified. Only remaining useful life of a product should be taken into account;
- Estimates cash flow projections beyond the period covered by the most recent budgets/forecasts by extrapolating the projections based on the budgets/forecasts using a steady or declining growth rate for subsequent years, unless an increasing rate can be justified;
- Estimates of future cash flows and the discount rate reflect consistent assumptions about price increases attributable to general inflation.

The carrying amount of digital products at 31 December 2019 was AZN 11,257 thousand (31 December 2018: AZN 11,377 thousand). More details are provided in Note 11.

Leases – estimating the incremental borrowing rate

The Group cannot readily determine the interest rate implicit in the lease, therefore, it uses its incremental borrowing rate (IBR) to measure lease liabilities. The IBR is the rate of interest that the Group would have to pay to borrow over a similar term, and with a similar security, the funds necessary to obtain an asset of a similar value to the right-of-use asset in a similar economic environment. The IBR therefore reflects what the Group 'would have to pay', which requires estimation when no observable rates are available (for example, when the Group do not enter into financing transactions) or when they need to be adjusted to reflect the terms and conditions of the lease (for example, when leases are not in the Group's functional currency).

The Group estimates the IBR using observable inputs (such as market interest rates) when available and is required to make certain entity-specific estimates (such as the Group's credit rating).

More details are provided in Note 3.

Taxation

Tax legislation in Azerbaijan, Turkey and Georgia is subject to varying interpretations, and changes can occur frequently. Management believes that as at 31 December 2019 and 2018 its interpretation of the relevant legislation is appropriate and that the Group's tax position will be sustained.

5. Cash and cash equivalents

Cash and cash equivalents comprise:

	2019	*2018*
Cash on hand	95,661	135,938
Current accounts with the CBAR, the NBG and the CBRT	499,615	257,234
Current accounts with other credit institutions	85,319	83,499
Time deposits with credit institutions up to 3 months	463,239	1,026,383
Reverse repurchase agreements with credit institutions up to 3 months	42,025	–
Less: allowance for impairment	(20)	(8)
Cash and cash equivalents	**1,185,839**	**1,503,046**

Current accounts with other credit institutions consist of non-interest bearing correspondent account balances with resident and non-resident banks in the amount of AZN 302 thousand (31 December 2018: AZN 83 thousand) and AZN 85,017 thousand (31 December 2018: AZN 83,416 thousand), respectively.

(Figures in tables are in thousands of Azerbaijani manats)

5. Cash and cash equivalents (continued)

As at 31 December 2019, the Group placed AZN 463,239 thousand in time deposits with CBAR and fourteen non-resident banks maturing through March 2020 with interest rates ranging between 0.37% and 13.70% p.a. (31 December 2018: AZN 1,026,383 thousand with one resident bank and fourteen non-resident banks maturing through March 2019 with interest rates ranging between 1% and 10% p.a.).

All balances of cash equivalents are allocated to Stage 1.

6. Amounts due from credit institutions

Amounts due from credit institutions comprise:

	2019	*2018*
Time deposits with credit institutions for more than 3 months	372,284	180,121
Loans to banks	62,819	18,583
Obligatory reserve with the CBAR, the NBG and the CBRT	97,229	83,981
Restricted deposits	92,623	52,518
	624,955	**335,203**
Less: allowance for impairment	(561)	(369)
Amounts due from credit institutions	**624,394**	**334,834**

As at 31 December 2019, time deposits with credit institutions mature between January 2020 and November 2021 (31 December 2018: between January 2019 and June 2022) with interest rates ranging between 1.92% and 2.65% p.a. (31 December 2018: between 1.3% and 11% p.a.).

As at 31 December 2019, the Group had outstanding amount of AZN 43,728 thousand (31 December 2018: AZN 17,415 thousand) of secured loan issued to two resident commercial banks (31 December 2018: one resident commercial bank) and AZN 19,091 thousand (31 December 2018: AZN 1,169 thousand) of unsecured loans issued to five non-resident commercial banks (31 December 2018: one resident commercial bank) with contractual maturity through December 2020 (31 December 2018: December 2019) and with interest rates ranging between 1.7% and 10% p.a. (31 December 2018: 1.9% and 10% p.a.).

Credit institutions in the Republic of Azerbaijan are required to maintain a mandatory reserve rates (with restriction on withdrawal) with the CBAR at the level of 0.5% (2018: 0.5%) and 1.0% (2018: 1.0%) of the previous month average of funds attracted from customers by a credit institution in AZN and foreign currencies, respectively.

Credit institutions in the Republic of Georgia are required to maintain a mandatory interest earning cash deposit with the NBG at the level of 5.0% (2018: 5.0%) and 25.0% (2018: 25.0%) of the average of funds attracted from customers and non-resident financial institutions for the appropriate two-week period in GEL and foreign currencies, respectively.

Credit institutions in the Turkish Republic are required to maintain a mandatory reserve rates for deposits with the CBRT in the range of 1.0% and 7.0% (2018: 1.5 and 8.0%) and 5.0% and 21.0% (2018: 4.0 and 20.0%) of average of funds attracted from customers by a credit institution in TL and foreign currencies, 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:

	Stage 1	*Stage 2*	*Stage 3*	*Total*
Gross carrying value as at 1 January 2019	**317,788**	**17,415**	**–**	**335,203**
New assets originated or purchased	466,844	–	–	**466,844**
Assets repaid	(171,148)	(3,201)	–	**(174,349)**
Foreign exchange adjustments	(2,743)	–	–	**(2,743)**
At 31 December 2019	**610,741**	**14,214**	**–**	**624,955**

	Stage 1	*Stage 2*	*Stage 3*	*Total*
ECL allowance as at 1 January 2019	**(369)**	**–**	**–**	**(369)**
New assets originated or purchased	(532)	–	–	**(532)**
Assets repaid	327	–	–	**327**
Foreign exchange adjustments	13	–	–	**13**
At 31 December 2019	**(561)**	**–**	**–**	**(561)**

6. Amounts due from credit institutions (continued)

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

	Stage 1	*Stage 2*	*Stage 3*	*Total*
Gross carrying value as at 1 January 2018	**570,111**	**21,918**	**871**	**592,900**
New assets originated or purchased	273,385	–	–	273,385
Assets repaid	(516,233)	(4,503)	(871)	(521,607)
Foreign exchange adjustments	(9,475)	–	–	(9,475)
At 31 December 2018	**317,788**	**17,415**	**–**	**335,203**

	Stage 1	*Stage 2*	*Stage 3*	*Total*
ECL allowance as at 1 January 2018	**(21)**	**–**	**(850)**	**(871)**
New assets originated or purchased	(423)	–	–	(423)
Assets repaid	198	–	850	1,048
Foreign exchange adjustments	(123)	–	–	(123)
At 31 December 2018	**(369)**	**–**	**–**	**(369)**

7. Investment securities

Investment securities comprise:

Debt securities at FVOCI	*2019*	*2018*
Bonds of the Ministry of Finance of the Republic of Azerbaijan	504,441	232,917
Certificate of deposits	316,508	486,919
Notes issued by the Central Bank of Azerbaijan Republic	117,933	367,229
AMF bonds	52,376	3,001
Corporate bonds	51,648	20,850
Other foreign governments' bonds	41,304	8,505
Bonds of financial institutions	17,232	13,789
US treasury bonds	4,336	292,717
Debt securities at FVOCI	**1,105,778**	**1,425,927**

Equity securities at FVOCI	*2019*	*2018*
Corporate Shares	2,189	–
Equity securities at FVOCI	**2,189**	**–**

Debt securities at amortized cost	*2019*	*2018*
Corporate bonds	12,003	11,821
Turkey Government Bonds	8,551	12,056
Bonds of financial institutions	18,258	8,650
	38,812	**32,527**
Less: allowance for impairment	(426)	(308)
Debt securities at amortized cost	**38,386**	**32,219**

As at 31 December 2019, debt securities at FVOCI in total amount of AZN 35,510 thousand are pledged as collateral for repurchase agreement with a non-resident bank.

(Figures in tables are in thousands of Azerbaijani manats)

7. Investment securities (continued)

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

Debt securities at FVOCI	*Stage 1*	*Stage 2*	*Stage 3*	*Total*
Gross carrying value as at 1 January 2019	**1,425,927**	–	–	**1,425,927**
New assets originated or purchased	838,504	–	–	**838,504**
Assets repaid	(1,163,667)	–	–	**(1,163,667)**
Transfers to Stage 2	(611)	611	–	–
Fair value increase	5,362	–	–	**5,362**
Foreign exchange adjustments	(320)	(28)	–	**(348)**
At 31 December 2019	**1,105,195**	**583**	–	**1,105,778**

Debt securities at FVOCI	*Stage 1*	*Stage 2*	*Stage 3*	*Total*
ECl allowance as at 1 January 2019	**(756)**	–	–	**(756)**
New assets originated or purchased	(722)	–	–	**(722)**
Assets repaid	665	–	–	**665**
Transfers to Stage 2	16	(16)	–	–
Changes to models and inputs used for ECL calculations	(5)	11	–	**6**
Foreign exchange adjustments	(26)	–	–	**(26)**
At 31 December 2019	**(828)**	**(5)**	–	**(833)**

Debt securities at FVOCI	*Stage 1*
Gross carrying value as at 1 January 2018	**405,530**
New assets originated or purchased	1,414,821
Assets repaid	(390,596)
Fair value decrease	(323)
Foreign exchange adjustments	(3,505)
At 31 December 2018	**1,425,927**

Debt securities at FVOCI	*Stage 1*
ECL as at 1 January 2018	**–**
New assets originated or purchased	(796)
Assets repaid	53
Changes to models and inputs used for ECL calculations	(13)
Foreign exchange adjustments	–
At 31 December 2018	**(756)**

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

Debt securities at amortised cost	*Stage 1*
Gross carrying value as at 1 January 2019	**32,527**
New assets originated	11,870
Assets repaid	(5,241)
Foreign exchange and other movements	(344)
At 31 December 2019	**38,812**

Debt securities at amortised cost	*Stage 1*
ECL as at 1 January 2019	**(308)**
New assets originated	(204)
Assets repaid	74
Changes to models and inputs used for ECL calculation	(20)
Foreign exchange and other movements	32
At 31 December 2019	**(426)**

7. Investment securities (continued)

Debt securities at amortised cost	***Stage 1***
Gross carrying value as at 1 January 2018	**40,568**
New assets originated	24,384
Assets repaid	(32,106)
Unwinding of discount (recognised in interest income)	253
Foreign exchange and other movements	(572)
At 31 December 2018	**32,527**

Debt securities at amortised cost	***Stage 1***
ECL as at 1 January 2018	**(563)**
New assets originated	(64)
Assets repaid	266
Foreign exchange and other movements	53
At 31 December 2018	**(308)**

8. Loans to customers

Loans to customers comprise:

	2019	*2018*
Legal entities	2,115,655	1,579,798
Individuals	248,254	200,984
Loans to customers (gross)	**2,363,909**	**1,780,782**
Less: allowance for impairment	(66,921)	(49,217)
Loans to customers (net)	**2,296,988**	**1,731,565**

Loans are made in the following industry sectors:

	2019	*2018*
Trade and services	889,367	708,472
Manufacturing	322,285	175,822
Individuals	248,254	200,984
Construction	223,634	110,103
Agriculture and food processing	167,688	125,994
Transport and telecommunication	159,608	124,999
Non-banking credit organizations	143,347	161,177
Mining	69,702	53,156
Energy	47,125	40,378
Real estate management	34,058	7,062
Leasing	24,781	22,516
Other	34,060	50,119
Total loans (gross)	**2,363,909**	**1,780,782**

As at 31 December 2019, loans granted to top 9 customers (2018: 6 customers) which individually exceeded 5% of the Group's equity, amounted to AZN 660,118 thousand (2018: AZN 300,344 thousand).

(Figures in tables are in thousands of Azerbaijani manats)

8. Loans to customers (continued)

Finance lease receivables

Included in loans to legal entities are finance lease receivables. The analysis of finance lease receivables at 31 December 2019 is as follows:

	Not later than 1 year	*Later than 1 year and not later than 5 years*	*Later than 5 years*
Gross investment in finance leases	3,913	6,130	–
Unearned future finance income on finance leases	(609)	(142)	–
Net investment in finance leases	**3,304**	**5,988**	**–**

The analysis of finance lease receivables at 31 December 2018 is as follows:

	Not later than 1 year	*Later than 1 year and not later than 5 years*	*Later than 5 years*
Gross investment in finance leases	5,593	4,043	–
Unearned future finance income on finance leases	(1,002)	(621)	–
Net investment in finance leases	**4,591**	**3,422**	**–**

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

	Stage 1	*Stage 2*	*Stage 3*	*Total*
Gross carrying value as at 1 January 2019	**1,284,414**	**331,099**	**165,269**	**1,780,782**
New assets originated or purchased	1,779,936	–	–	**1,779,936**
Assets repaid (excluding write-offs)	(960,214)	(205,421)	(7,585)	**(1,173,220)**
Transfers to Stage 1	29,394	(29,326)	(68)	–
Transfers to Stage 2	(498,329)	508,402	(10,073)	–
Transfers to Stage 3	(16,420)	(6,469)	22,889	–
Amounts written off	(42)	–	(7,509)	**(7,551)**
Foreign exchange adjustments	(15,543)	(193)	(302)	**(16,038)**
At 31 December 2019	**1,603,196**	**598,092**	**162,621**	**2,363,909**

	Stage 1	*Stage 2*	*Stage 3*	*Total*
ECL as at 1 January 2019	**(12,079)**	**(9,523)**	**(27,615)**	**(49,217)**
New assets originated or purchased	(17,506)	–	–	**(17,506)**
Assets repaid	4,680	2,691	3,041	**10,412**
Transfers to Stage 1	(794)	794	–	–
Transfers to Stage 2	10,582	(10,623)	41	–
Transfers to Stage 3	1,673	530	(2,203)	–
Impact on period end ECL of exposures transferred between stages during the period	691	(4,798)	(2,044)	**(6,151)**
Unwinding of discount (recognised in interest revenue)	–	–	(2,278)	**(2,278)**
Changes to models and inputs used for ECL calculations	(98)	(552)	(5,029)	**(5,679)**
Amounts written off	41	–	7,509	**7,550**
Recovery	–	–	(5,142)	**(5,142)**
Foreign exchange adjustments	708	391	(9)	**1,090**
At 31 December 2019	**(12,102)**	**(21,090)**	**(33,729)**	**(66,921)**

(Figures in tables are in thousands of Azerbaijani manats)

8. Loans to customers (continued)

Finance lease receivables (continued)

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

	Stage 1	*Stage 2*	*Stage 3*	*Total*
Gross carrying value as at 1 January 2018	**1,062,507**	**146,507**	**204,978**	**1,413,992**
New assets originated or purchased	1,184,286	–	–	**1,184,286**
Assets repaid (excluding write-offs)	(598,353)	(92,327)	(47,369)	**(738,049)**
Transfers to Stage 1	8,712	(8,712)	–	–
Transfers to Stage 2	(298,162)	298,162	–	–
Transfers to Stage 3	(4,522)	(13,581)	18,103	–
Unwinding of discount	10,774	1,490	–	**12,264**
Changes to contractual cash flows due to modifications not resulting in derecognition	–	(117)	–	**(117)**
Amounts written off	(1,096)	–	(10,443)	**(11,539)**
Foreign exchange adjustments	(79,732)	(323)	–	**(80,055)**
At 31 December 2018	**1,284,414**	**331,099**	**165,269**	**1,780,782**

	Stage 1	*Stage 2*	*Stage 3*	*Total*
ECL as at 1 January 2018	**(6,079)**	**(3,648)**	**(51,421)**	**(61,148)**
New assets originated or purchased	(19,177)	–	–	**(19,177)**
Assets repaid	4,230	1,330	23,436	**28,996**
Transfers to Stage 1	(328)	328	–	–
Transfers to Stage 2	8,238	(8,238)	–	–
Transfers to Stage 3	1,087	924	(2,011)	–
Impact on period end ECL of exposures transferred between stages during the period	273	(966)	(11,479)	**(12,172)**
Unwinding of discount (recognised in interest revenue)	(82)	(111)	(1,810)	**(2,003)**
Changes to models and inputs used for ECL calculations	(1,952)	909	(963)	**(2,006)**
Amounts written off	1,156	–	16,633	**17,789**
Foreign exchange adjustments	555	(51)	–	**504**
At 31 December 2018	**(12,079)**	**(9,523)**	**(27,615)**	**(49,217)**

Modified and restructured loans

The Group 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.

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 Group records a modification gain or loss, to the extent that an impairment loss has not already been recorded.

The table below includes Stage 2 and Stage 3 assets that were modified during the period, with the related modification loss suffered by the Group.

	2019	*2018*
Loans modified during the period		
Amortised cost before modification	36,162	–
Net modification loss	(312)	–

8. Loans to customers (continued)

Collateral and other credit enhancements

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

The main types of collateral obtained are as follows:

- For commercial lending, charges over real estate properties, cash, securities, equipment and trade receivables;
- For retail lending, mortgages over residential properties and life endowment insurance account;
- Guarantees from parent company for both commercial and retail lending.

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

The Group calculates LGD rate of certain Legal entities in Stage 3 using discounted value of collaterals. As at 31 December 2019, maximum exposure of such individually assessed loans amounted to AZN 154,836 thousand (2018: 160,072 thousand) for which ECL of AZN 32,884 thousand (2018: 24,694 thousand) was created. If these loans were not collateralized, ECL amount for these loans would be AZN 117,143 thousand (2018: 89,368) based on collective assessment.

9. Investment property

The movements in investment property were as follows:

	2019	*2018*
Opening balance at 1 January	**71,719**	**1,668**
Additions (subsequent expenditure)	174	97,061
Impairment loss	–	(13,546)
Amortisation for the period	(337)	(148)
Transfer of the cost to property and equipment	(25,900)	–
Transfer of the accumulated depreciation to property and equipment	41	–
Transfer of impairment loss to property and equipment	4,239	–
Foreign translation difference	(6,734)	(13,316)
Closing balance	**43,202**	**71,719**

In 2011, the Group acquired land for the amount of AZN 2,000 thousand as investment property which is held for long-term appreciation in value. As at 31 December 2019, the fair value of this investment property amounted to AZN 1,590 thousand (2018: AZN 1,590 thousand).

In June 2018, after the increase of share capital, PASHA Yatirim Bankasi A.S. purchased a real estate classified as investment property amounting to AZN 97,061 thousand. As at 31 December 2019, the fair value of this investment property amounted to AZN 41,441 thousand (2018: AZN 70,129 thousand). The Group reclassified part of investment property of AZN 21,620 thousand (Note 10), net of impairment and accumulated depreciation, to buildings and land within property and equipment, caused by using the part of the building by PASHA Yatirim Bankasi A.Ş. for own purposes as the new headquarter.

(Figures in tables are in thousands of Azerbaijani manats)

10. Property and equipment

The movements in property and equipment were as follows:

	Land	*Buildings*	*Furniture and fixtures*	*Computers and other equipment*	*Vehicles*	*Other equipment*	*Leasehold improve-ments*	*Total*
Cost								
31 December 2017	**415**	**4,107**	**12,606**	**9,676**	**1,287**	**642**	**3,161**	**31,894**
Additions	–	751	4,517	3,923	596	84	707	10,578
Disposals	–	–	(3)	(13)	(32)	(2)	–	(50)
Foreign currency translation difference	–	–	(65)	(266)	(35)	(19)	(44)	(429)
31 December 2018	**415**	**4,858**	**17,055**	**13,320**	**1,816**	**705**	**3,824**	**41,993**
Additions	–	3,931	4,609	2,095	367	626	2,790	14,418
Disposals	(115)	–	(1,126)	(573)	(29)	(173)	(1,170)	(3,186)
Transfers	17,586	8,314	28	(32)	–	4	–	25,900
Foreign currency translation difference	(804)	(535)	(431)	251	(55)	(7)	(104)	(1,685)
31 December 2019	**17,082**	**16,568**	**20,135**	**15,061**	**2,099**	**1,155**	**5,340**	**77,440**
Accumulated depreciation								
31 December 2017	–	(1,147)	(7,797)	(6,580)	(884)	(552)	(2,126)	(19,086)
Depreciation charge	–	(209)	(2,234)	(1,877)	(221)	(48)	(319)	(4,908)
Disposals	–	–	3	13	32	2	–	50
Foreign currency translation difference	–	–	35	99	5	17	31	187
31 December 2018	–	**(1,356)**	**(9,993)**	**(8,345)**	**(1,068)**	**(581)**	**(2,414)**	**(23,757)**
Depreciation charge	–	(448)	(2,981)	(2,328)	(298)	(56)	(527)	(6,638)
Disposals	–	–	1,097	568	29	168	1,168	3,030
Transfers	–	(41)	–	–	–	–	–	(41)
Transfer – impairment	(2,878)	(1,361)	–	–	–	–	–	(4,239)
Foreign currency translation difference	132	73	95	(122)	15	(19)	67	241
31 December 2019	**(2,746)**	**(3,133)**	**(11,782)**	**(10,227)**	**(1,322)**	**(488)**	**(1,706)**	**(31,404)**
Net book value								
31 December 2019	**14,336**	**13,435**	**8,353**	**4,834**	**777**	**667**	**3,634**	**46,036**
31 December 2018	**415**	**3,502**	**7,062**	**4,975**	**748**	**124**	**1,410**	**18,236**
31 December 2017	**415**	**2,960**	**4,809**	**3,096**	**403**	**90**	**1,035**	**12,808**

(Figures in tables are in thousands of Azerbaijani manats)

11. Intangible assets

The movements in intangible assets were as follows:

	Goodwill	*Banking license*	*Licenses*	*Computer software*	*Digital products*	*Total*
Cost						
31 December 2017	**3,642**	**37,823**	**11,450**	**11,830**	**–**	**64,745**
Additions	–	–	3,298	1,542	11,377	16,217
Disposals	–	–	–	(112)	–	(112)
Internal transfer	–	–	(563)	563	–	–
Foreign currency translation difference	–	(9,036)	15	(385)	–	(9,406)
31 December 2018	**3,642**	**28,787**	**14,200**	**13,438**	**11,377**	**71,444**
Additions	–	–	3,150	5,926	3,603	12,679
Disposals	–	–	(1,222)	(785)	–	(2,007)
Foreign currency translation difference	–	(2,192)	(6)	(114)	–	(2,312)
31 December 2019	**3,642**	**26,595**	**16,122**	**18,465**	**14,980**	**79,804**
Accumulated amortization						
31 December 2017	**(3,642)**	**(6,236)**	**(3,590)**	**(2,323)**	**–**	**(15,791)**
Amortisation charge	–	–	(1,934)	(1,613)	–	(3,547)
Disposals	–	–	–	111	–	111
Impairment	–	(2,659)	–	–	–	(2,659)
Transfer – impairment	–	–	175	(175)	–	–
Foreign currency translation difference	–	–	(5)	201	–	196
31 December 2018	**(3,642)**	**(8,895)**	**(5,354)**	**(3,799)**	**–**	**(21,690)**
Amortisation charge	–	–	(2,567)	(1,914)	(1,776)	(6,257)
Disposals	–	–	1,221	400		1,621
Impairment	–	(1,038)	–	–	(1,947)	(2,985)
Foreign currency translation difference	–	47	4	(123)	–	(72)
31 December 2019	**(3,642)**	**(9,886)**	**(6,696)**	**(5,436)**	**(3,723)**	**(29,383)**
Net book value						
31 December 2019	**–**	**16,709**	**9,426**	**13,029**	**11,257**	**50,421**
31 December 2018	**–**	**19,892**	**8,846**	**9,639**	**11,377**	**49,754**
31 December 2017	**–**	**31,587**	**7,860**	**9,507**	**–**	**48,954**

Digital products mainly represents the Group's internally developed software that is being used starting from 2019 (2018: under development).

Impairment testing of intangible assets with indefinite lives

Banking license acquired through business combination with indefinite lives has been allocated to one individual cash-generating unit for impairment testing which is PASHA Yatirim Bankasi A.Ş.

The carrying amount of the banking license acquired allocated to the cash-generating units is AZN 16,709 thousand (31 December 2018: AZN 19,892 thousand).

Key assumptions used in fair value calculation

As at 31 December 2019 and 2018, recoverable amount of cash generating unit have been determined based on value in use method. The valuation is based on the information about historical and prospective financials and strategic initiatives of the PASHA Yatirim Bankasi A.S, and other third party information available on the market.

(Figures in tables are in thousands of Azerbaijani manats)

11. Intangible assets (continued)

Key assumptions used in fair value calculation (continued)

The calculation of value in use is most sensitive to the following assumptions:

- Financial performance (including current and forecasted results);
- Cost of equity;
- ROE (including current and forecasted results);
- Growth rate of loan portfolio;
- GDP growth rate in Turkey;
- Leverage ratio;
- Period of discounted cash flow of 8 years;
- Long term inflation growth rate of 5% (2018: 5%).

The following rates are used by the Group for calculation of Cost of Equity:

		2019	*2018*
Cost of equity calculation			
US Risk-Free Rate	a	2.3%	2.9%
US Market risk premium	b	6.0%	5.1%
Country risk premium	c	0.0%	3.5%
Beta	d	1.00	0.82
Cost of equity USD	e = (a + b * d + c)	**8.3%**	**10.5%**
USA inflation rate	f	2.2%	2.3%
Turkey inflation rate	j	8.9%	7.0%
Cost of equity TRY	h = (1 + e) * ((1 + j) / (1 + f)) - 1	**15.4%**	**15.6%**

As a result of the valuation, recoverable amount of cash generating unit amounted to 161,815 AZN thousand (2018: AZN 182,341 thousand). Accordingly, the license was partially impaired by amount of AZN 1,038 thousand (2018: AZN 2,659 thousand). As at December 2019 and 2018, the impairment loss was mainly due to decrease in in return on equity.

Sensitivity for reasonably possible increase in discount rate by 1% (from 15.4% to 16.4%) (31 December 2018: from 15.6% to 16.6%) would result in additional impairment of AZN 15,701 thousand (31 December 2018: AZN 18,378 thousand) under the same assumption of the long-term Return on Equity.

12. Other assets and liabilities

Other assets comprise:

	2019	*2018*
Other financial assets		
Settlements on money transfers	6,498	6,065
Clearance cheque accounts	2,685	7,118
Accrued commission receivable on guarantees and letters of credit	1,066	901
Other	28	19
	10,277	**14,103**
Less: allowance for impairment of other financial assets	(315)	(492)
Total other financial assets	**9,962**	**13,611**
Other non-financial assets		
Repossessed collateral	12,264	13,929
Deferred expenses	2,017	2,441
Prepayments for acquisition of property, equipment and intangible assets	1,722	2,078
Purchased miles under loyalty programme	1,490	–
Other prepayments	2,476	3,055
Taxes, other than income tax	12	2
	19,981	**21,505**
Other assets	**29,943**	**35,116**

(Figures in tables are in thousands of Azerbaijani manats)

12. Other assets and liabilities (continued)

All balances of other financial assets are allocated to Stage 1.

As at 31 December 2019 and 2018, clearance cheque accounts consist of receivables from other banks for which cheques stand as collateral.

As at 31 December 2019 deferred expenses of AZN 935 thousand (31 December 2018: AZN 1,217 thousand) related to long term software support.

Other liabilities comprise:

	2019	*2018*
Other financial liabilities		
Settlements on money transfer	267	7,432
Clearance cheque accounts	2,685	7,118
Accrued expenses	3,870	3,027
Other	2,070	2,297
	8,892	**19,874**
Other non-financial liabilities		
Payable to employees	20,448	18,944
Deferred income	2,476	1,218
Taxes, other than income tax	453	326
Other provision	–	112
Other	67	825
	23,444	**21,425**
Other liabilities	**32,336**	**41,299**

13. Amounts due to banks and government funds

Amounts due to banks and government funds comprise:

	2019	*2018*
Long-term deposits from banks	330,447	25,485
Entrepreneurship Development Fund of the Republic of Azerbaijan	301,885	247,985
Short-term deposits from banks	87,309	197,664
Repurchase agreements	35,595	–
Correspondent accounts with other banks	35,073	25,340
Azerbaijan Mortgage and Credit Guarantee Fund	31,858	20,367
Long-term loans from banks	8,629	–
Amount due to IT Development Fund	4,250	4,914
Loan from the Ministry of Finance of Georgia	4,163	–
Agro Credit and Development Agency	3,691	–
State Agency on Mandatory Health Insurance	1,041	3,220
Other amount	18,202	–
Amounts due to banks and government funds	**862,143**	**524,975**

As at 31 December 2019, the Group attracted long-term deposits from both resident and non-resident commercial banks comprising AZN 330,447 thousand (31 December 2018: AZN 25,485) maturing through December 2022 with interest rates ranging between 1.50% and 4.25% p.a. (31 December 2018: December 2022 with interest rate 3.00% p.a.).

As at 31 December 2019, Entrepreneurship Development Fund of the Republic of Azerbaijan had current account amounting to AZN 56,353 thousand (31 December 2018: AZN 61,321 thousand). The Group had loans received from the Entrepreneurship Development Fund of the Republic of Azerbaijan amounting to AZN 245,532 thousand (31 December 2018: AZN 186,664 thousand), maturing through December 2029 (31 December 2018: through December 2028), and bearing interest rate of 1.0% p.a. The loans were acquired for the purposes of assistance in gradually improving entrepreneurship environment in Azerbaijan under the government program. The loans have been granted to local entrepreneurs at interest rate not higher than 6.00% p.a. (31 December 2018: not higher than 5.00% p.a.).

As at 31 December 2019, the Group attracted short-term deposits both resident and non-resident commercial banks comprising AZN 87,309 thousand (31 December 2018: AZN 197,664 thousand) maturing through January and December 2020 (31 December 2018: December 2019) and with interest rates ranging between 0.01% and 11.25% p.a. (31 December 2018: ranging between 0.10% and 7.00% p.a.).

(Figures in tables are in thousands of Azerbaijani manats)

13. Amounts due to banks and government funds (continued)

As at 31 December 2019, the Group entered into repurchase agreement with a non-resident bank and borrowed funds amounting to AZN 35,595 thousand (31 December 2018: nil), with interest rate of 1.25% p.a. The Group pledged its debt securities at FVOCI as collateral (Note 7).

As at 31 December 2019, the Group had loans refinanced from the Azerbaijan Mortgage and Credit Guarantee Fund amounting to AZN 31,858 thousand (31 December 2018: AZN 20,367 thousand), maturing through September 2049 (31 December 2018: through December 2048) and bearing interest rate of 1.00% and 4.00% p.a. (31 December 2018: 1.00% and 4.00% p.a.). The loans have been granted to borrowers at interest rate not higher than 8.00% p.a. (31 December 2018: not higher than 8.00% p.a.).

As at 31 December 2019, the Group had loans from resident banks amounting to AZN 8,629 thousand (31 December 2018: nil), maturing through August 2022 and with interest rate of 4.00% p.a.

As at 31 December 2019, the Group had loans refinanced from the IT Development Fund amounting to AZN 4,250 thousand (31 December 2018: AZN 4,914 thousand), maturing through June 2024 (31 December 2018: through October 2023) and bearing interest rate of 1.00% p.a. (31 December 2018: 1.00% p.a.). The loans have been granted to local entrepreneurs at interest rate of 5.00% p.a. (31 December 2018: 5.00% p.a.).

As at 31 December 2019, the Group had loans received from the Agro Credit and Development Agency amounting to AZN 3,691 thousand (31 December 2018: nil), maturing through November 2024 and bearing interest rate between 2.00% and 3.30% p.a. The loans have been granted to local entrepreneurs at interest rate of 7.00% p.a.

As at 31 December 2019, the Group had loans from Ministry of Finance of Georgia amounting to AZN 4,163 thousand (31 December 2018: nil), maturing through February 2020 and with interest rate of 8.10% and 8.30% p.a.

14. Amounts due to customers

The amounts due to customers include the following:

	2019	*2018*
Demand deposits	2,149,775	2,946,841
Time deposits	1,639,166	1,007,111
Amounts due to customers	**3,788,941**	**3,953,952**
Held as security against guarantees issued (Note 20)	42,014	23,352

An analysis of customer accounts by economic sector is as follows:

	2019	*2018*
Individuals	1,089,773	1,265,829
Trade and services	930,602	739,982
Investment holding companies	468,001	494,449
Transport and communication	385,421	382,365
Manufacturing	251,532	444,912
Construction	198,697	194,889
Insurance	166,626	123,068
Hotel business	62,938	46,220
Mining	56,633	117,200
Non banking credit organizations	39,762	20,426
Public organizations	38,845	24,906
Agriculture	31,502	19,390
Energy	16,584	9,573
Other	52,025	70,743
Amounts due to customers	**3,788,941**	**3,953,952**

As at 31 December 2019, customer deposits included balances with nine (31 December 2018: five) largest customers comprised AZN 1,751,160 thousand or 46% of the total customer deposits portfolio (31 December 2018: AZN 1,736,416 thousand or 44% of the total customer deposits portfolio).

(Figures in tables are in thousands of Azerbaijani manats)

15. Debt securities issued

As at 31 December 2019, PASHA Yatirim Bankasi A.S. had issued interest-bearing bonds with carrying amount of AZN 136,031 thousand (31 December 2018: AZN 102,300 thousand) maturing in February 2023 (31 December 2018: matured in December 2022). Bonds issued by the bank as at 31 December 2019, bear annual interest rates ranging from 1.7% to 11.4% (31 December 2018: from 3.0% to 30.0%).

16. Subordinated debts

As of 31 December 2019, the amount of subordinated debts represents USD denominated subordinated loan of AZN 27,111 thousand (31 December 2018: AZN 18,921 thousand) borrowed by the Group from its parent and entities under common control maturing through August 2024 and December 2025 (31 December 2018: August 2024) and with interest rates ranging from 3.0% to 5.9% (31 December 2018: 3.0%).

17. Derivative financial instruments

The Group enters into derivative financial instruments for trading purposes. The table below shows the fair values of derivative financial instruments, recorded as assets or liabilities, together with their notional amounts. The notional amount, recorded gross, is the amount of a derivative's underlying asset, reference rate or index and is the basis upon which changes in the value of derivatives are measured. The notional amounts indicate the volume of transactions outstanding at the year end and are not indicative of the credit risk.

	2019			*2018*		
	Notional amount	*Fair values*		*Notional amount*	*Fair value*	
		Asset	*Liability*		*Asset*	*Liability*
Interest rate contracts						
Forwards and swaps – foreign	59,771	250	(137)	24,647	264	(44)
Forwards and swaps – domestic	–	–	–	–	–	–
Foreign exchange contracts						
Forwards and swaps – foreign	6,743	38	–	31,685	722	(37)
Forwards and swaps – domestic	–	–	–	34,500	1,062	–
Options – foreign	–	–	–	–	–	–
Options – domestic	37,680	79	–	16,909	2	–
Futures – domestic	26,706	90	–	–	–	–
Total derivative assets/ (liabilities)		**457**	**(137)**		**2,050**	**(81)**

Foreign and domestic in the table above stand for counterparties where foreign means non-Azerbaijani entities and domestic means Azerbaijani entities.

As at 31 December 2019 and 2018, the Group has positions in the following types of derivatives:

Forwards and futures

Forwards and futures contracts are contractual agreements to buy or sell a specified financial instrument at a specific price and date in the future. Forwards are customised contracts transacted in the over-the-counter market. Futures contracts are transacted in standardised amounts on regulated exchanges and are subject to daily cash margin requirements.

Swaps

Swaps are contractual agreements between two parties to exchange movements in interest and foreign currency rates and equity indices, and (in the case of credit default swaps) to make payments with respect to defined credit events based on specified notional amounts.

Options

Options are contractual agreements that convey the right, but not the obligation, for the purchaser either to buy or sell a specific amount of a financial instrument at a fixed price, either at a fixed future date or at any time within a specified period.

(Figures in tables are in thousands of Azerbaijani manats)

18. Taxation

The corporate income tax expense comprises:

	2019	*2018*
Current tax charge	(21,603)	(24,854)
Deferred tax (charge)/charge – origination and reversal of temporary differences	(4,806)	3,841
Less: deferred tax recognised in other comprehensive income	1,083	82
Income tax expense	**(25,326)**	**(20,931)**

Deferred tax related to items charged or credited to other comprehensive income during the year is as follows:

	2019	*2018*
Net gains on investment securities FVOCI	(1,083)	(82)
Income tax (charged)/credited to other comprehensive income	**(1,083)**	**(82)**

The effective income tax rate differs from the statutory income tax rates. A reconciliation of the income tax expense based on statutory rates with actual is as follows:

	2019	*2018*
Profit before income tax expense	**102,423**	**94,984**
Statutory tax rate	20%	20%
Theoretical tax expense at the statutory rate	**(20,485)**	**(18,997)**
Tax effect of non-deductible expenses	(3,066)	(2,441)
Effect from change in tax legislation	(221)	154
Effect of difference in tax rate in foreign country	(452)	(102)
Tax effect of tax-exempt income	73	67
(Expired)/utilised tax losses carried forward	(867)	242
Other	(308)	146
Income tax expense	**(25,326)**	**(20,931)**

(Figures in tables are in thousands of Azerbaijani manats)

18. Taxation (continued)

Deferred tax assets and liabilities as at 31 December 2019 and 2018 and their movements for the respective years comprise:

			Origination and reversal of temporary differences				*Origination and reversal of temporary differences*			
	2017	*Effect of adoption of IFRS 9*	*In the statement of profit or loss*	*In other comprehensive income*	*Translation difference*	*2018*	*In the statement of profit or loss*	*In other comprehensive income*	*Translation difference*	*2019*
Tax effect of deductible temporary differences										
Tax losses carried forward	–	–	130	–	(7)	123	(117)	–	(6)	–
Trading securities	–	–	–	–	–	–	–	–	–	–
Amounts due from credit institutions	–	–	9	–	(2)	7	(22)	–	25	10
Loans to customers	235	–	822	–	(137)	920	1,131	–	63	2,114
Investment securities	21	–	–	–	–	21	88	(22)	14	101
Investment property	66	–	2,996	–	–	3,062	–	–	(328)	2,734
Property and equipment	–	–	169	–	(6)	163	(193)	–	30	–
Right of use assets	–	–	–	–	–	–	120	–	(2)	118
Intangible assets	–	–	84	–	–	84	324	–	(35)	373
Derivative financial liabilities	315	–	(315)	–	–	–	–	–	–	–
Lease liabilities	–	–	–	–	–	–	1,238	–	–	1,238
Provision for guarantees and letters of credit	–	–	–	–	–	–	–	–	–	–
Other liabilities	3,347	–	600	–	(143)	3,804	152	–	(87)	3,869
Deferred tax asset	**3,984**	**–**	**4,495**	**–**	**(295)**	**8,184**	**2,721**	**(22)**	**(326)**	**10,557**
Amounts due from credit institutions	(2,618)	–	2,026	–	–	(592)	(1,341)	–	–	(1,933)
Derivative financial assets	(325)	–	112	–	–	(213)	311	–	(140)	(42)
Investment securities	(1)	(48)	113	(82)	45	27	14	(1,061)	2	(1,018)
Loans to customers	(2,798)	(160)	(2,015)	–	10	(4,963)	(3,597)	–	(81)	(8,641)
Property and equipment	(100)	–	(440)	–	176	(364)	(236)	–	57	(543)
Intangible assets	(25)	–	(21)	–	2	(44)	(34)	–	3	(75)
Other assets	(886)	–	(732)	–	106	(1,512)	(338)	–	222	(1,628)
Lease liabilities	–	–	–	–	–	–	(88)	–	1	(87)
Right of use assets	–	–	–	–	–	–	(1,198)	–	–	(1,198)
Amounts due to banks and government funds	–	–	–	–	–	–	55	–	(60)	(5)
Amounts due to customers	–	–	–	–	–	–	–	–	–	–
Provision for guarantees and letters of credit	(330)	245	(147)	–	–	(232)	(229)	–	(155)	(616)
Banking license	(6,317)	–	532	–	1,611	(4,174)	237	–	595	(3,342)
Deferred tax liabilities	**(13,400)**	**37**	**(572)**	**(82)**	**1,950**	**(12,067)**	**(6,444)**	**(1,061)**	**444**	**(19,128)**
Net deferred tax assets/(liabilities)	**(9,416)**	**37**	**3,923**	**(82)**	**1,655**	**(3,883)**	**(3,723)**	**(1,083)**	**118**	**(8,571)**

As at 31 December 2019, the aggregate amount of temporary differences associated with investments in subsidiaries for which deferred tax liability have not been recognized was AZN 13,267 thousand (31 December 2018: AZN 22,710 thousand).

Deferred taxes in the consolidated statement of financial position as at 31 December 2019 and 2018 can be reconciled as follows:

	2019	*2018*
Deferred tax assets	4,466	4,003
Deferred tax liabilities	(13,037)	(7,886)
Net deferred tax liabilities	**(8,571)**	**(3,883)**

19. Equity

As at 31 December 2019 and 2018, the Bank's authorized, issued and fully paid capital amounted to AZN 333,000 thousand comprising of 10,000 ordinary shares with a par value of AZN 33,300 per ordinary share. Each ordinary share entitles one vote to the shareholder.

On 10 May 2018 Shareholders of the Bank declared dividends totalling AZN 61,414 thousand on ordinary shares (AZN 6,141 per share) which was paid as at 31 December 2018.

On 29 April 2019 Shareholders of the Bank declared dividends totalling AZN 45,232 thousand on ordinary shares (AZN 4,523 per share) which was paid as at 31 December 2019.

(Figures in tables are in thousands of Azerbaijani manats)

19. Equity (continued)

Additional paid-in capital

As at 31 December 2019, additional paid-in capital of AZN 343 thousand represents gain from fair value measurement of subordinated debts of AZN 8,531 thousand, borrowed from entities under common control.

Foreign currency translation reserve

Foreign currency translation reserve is used to record exchange difference arising from the translation of the financial statements of foreign subsidiaries.

Unrealised gains on investment securities

This reserve records fair value changes on investment securities.

20. Commitments and contingencies

Operating environment

Azerbaijan continues economic reforms and development of its legal, tax and regulatory frameworks. The future stability of the Azerbaijan economy is largely dependent upon these reforms and the effectiveness of economic, financial and monetary measures undertaken by the government as well as crude oil prices and stability of Azerbaijani manat.

The Azerbaijan economy has been negatively impacted by decline of oil prices and devaluation of Azerbaijani manat during 2015. This resulted in reduced access to capital, a higher cost of capital, inflation and uncertainty regarding economic growth.

In response to these challenges, the Central Bank of Azerbaijan Republic (the "CBAR") tightened monetary policy and introduced a number of measures to stabilize macroeconomic situation. In addition, Azerbaijani government announced plans to accelerate reforms and support to financial system. On 6 December 2016 President of the Republic of Azerbaijan approved "Strategic road maps for the national economy and main economic sectors of Azerbaijan".

During 2018 CBAR maintained monetary policy aimed at macroeconomic stability, including low one-digit inflation and steady AZN rate. At the same time the CBAR gradually reduced refinancing rate from 15% to 9.75%.

Furthermore, over 2019 the CBAR continued easing monetary conditions while maintaining stability of Azerbaijani manat. As a result, CBAR refinancing rate further declined from 9.75% to 7.5% and AZN rate remained unchanged.

Finally, on 28 February 2019 according to the Decree of the President of Azerbaijan Republic on problematic loans, the government provided funds for compensation to citizens, whose loans burden increased due to the devaluation of Azerbaijani manat in 2015. This measure significantly reduced amounts of non-performing loans as well as supported capital and liquidity in the banking system.

The Group's management is monitoring economic developments in the current environment and taking precautionary measures it considered necessary in order to support the sustainability and development of the Group's business in the foreseeable future.

Legal

In the ordinary course of business, the Group is subject to legal actions and complaints. Management believes that the ultimate liability, if any, arising from such actions or complaints will not have a material adverse effect on the financial condition or the results of future operations of the Group.

Taxation

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

Management believes that its interpretation of the relevant legislation as at 31 December 2019 is appropriate and that the Group's tax, currency and customs positions will be sustained.

(Figures in tables are in thousands of Azerbaijani manats)

20. Commitments and contingencies (continued)

Insurance

The Group has not currently obtained insurance coverage related to liabilities arising from errors or omissions.

Compliance with the CBAR ratios

CBAR requires banks to maintain certain prudential ratios computed based on statutory financial statements. As at 31 December 2019 and 2018, the Bank was in compliance with these ratios except for the followings:

a) Ratio of the share in one legal entity which should not exceed 10% of total capital. As at 31 December 2019 the Bank's ratio was 33.28 % (31 December 2018: 35.66%);

b) Ratio of the total share in other legal entities which should not exceed 40% of total capital. As at 31 December 2019 the Bank's ratio was 48.95% (31 December 2018: 52.46%).

Throughout the year the Bank submitted information regarding these breaches to the regulator on a monthly basis and no sanctions were imposed on the Bank. Management believes that the Bank will not face any sanctions against the Group in the future.

Financial commitments and contingencies

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

Financial commitments and contingencies comprise:

	2019	*2018*
Credit-related commitments		
Guarantees issued	629,296	549,196
Unused credit lines	216,417	133,479
Letters of credit	25,989	5,146
	871,702	**687,821**
Operating lease commitments		
Not later than 1 year	409	4,911
Later than 1 year but not later than 5 years	1,195	19,176
Later than 5 years	–	–
	1,604	**24,087**
Less: provision for ECL for credit related commitments	(10,550)	(6,425)
Commitments and contingencies (before deducting collateral)	**862,756**	**705,483**
Less: cash held as security against guarantees issued (Note 14)	(42,014)	(23,352)
Commitments and contingencies	**820,742**	**682,131**

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

	Stage 1	*Stage 2*	*Stage 3*	*Total*
ECL as at 1 January 2019	**(3,735)**	**(1,814)**	**(876)**	**(6,425)**
New exposures	(6,679)	(45)	–	**(6,724)**
Exposures derecognised or matured (excluding write-offs)	1,154	1,129	1,090	**3,373**
Transfers to Stage 1	(139)	139	–	–
Transfers to Stage 2	3,531	(3,531)	–	–
Transfers to Stage 3	369	–	(369)	–
Impact on period end ECL of exposures transferred between stages during the period	137	(224)	96	**9**
Changes to inputs used for ECL calculations	19	(1,015)	–	**(996)**
Foreign exchange adjustments	115	312	(214)	**213**
At 31 December 2019	**(5,228)**	**(5,049)**	**(273)**	**(10,550)**

(Figures in tables are in thousands of Azerbaijani manats)

20. Commitments and contingencies (continued)

Financial commitments and contingencies (continued)

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

	Stage 1	*Stage 2*	*Stage 3*	*Total*
ECL as at 1 January 2018	**(2,025)**	**(1,952)**	**(290)**	**(4,267)**
New exposures	(1,685)	(1,191)	–	**(2,876)**
Exposures derecognised or matured (excluding write-offs)	328	283	288	**899**
Transfers to Stage 1	(2,231)	2,231	–	–
Transfers to Stage 2	245	(245)	–	–
Transfers to Stage 3	–	(487)	487	–
Impact on period end ECL of exposures transferred between stages during the period	1,780	(506)	(1,364)	**(90)**
Changes to inputs used for ECL calculations	(319)	8	3	**(308)**
Foreign exchange adjustments	172	45	–	**217**
At 31 December 2018	**(3,735)**	**(1,814)**	**(876)**	**(6,425)**

21. Credit loss expense and other impairment and provisions

The table below shows the ECL charges on financial instruments recorded in the consolidated statement of profit or loss for the year ended 31 December 2019:

	Note	*Stage 1*	*Stage 2*	*Stage 3*	*Total*
Cash and cash equivalents		(13)	–	–	**(13)**
Due from credit Institutions	6	(205)	–	–	**(205)**
Investment securities at FVOCI	7	(46)	(5)	–	**(51)**
Investment securities at amortised cost	7	(150)	–	–	**(150)**
Loans to customers	8	(772)	(11,958)	(6,194)	**(18,924)**
Credit loss on financial assets		**(1,186)**	**(11,963)**	**(6,194)**	**(19,343)**
Other financial assets		–	–	(26)	**(26)**
Credit related commitments	20	(1,608)	(3,547)	817	**(4,338)**
Total credit loss expense		**(2,794)**	**(15,510)**	**(5,403)**	**(23,707)**

Allowance for impairment of other assets is deducted from the carrying amounts of the related assets. Provision for ECL for credit related commitments are recorded in liabilities.

The table below shows the ECL charges on financial instruments recorded in the consolidated statement of profit or loss for the year ended 31 December 2018:

	Note	*Stage 1*	*Stage 2*	*Stage 3*	*Total*
Cash and cash equivalents		(8)	–	–	**(8)**
Due from credit Institutions	6	(225)	–	850	**625**
Investment securities at FVOCI	7	(756)	–	–	**(756)**
Investment securities at amortised cost	7	202	–	–	**202**
Loans to customers	8	(7,629)	(5,713)	8,983	**(4,359)**
Credit loss on financial assets		**(8,416)**	**(5,713)**	**9,833**	**(4,296)**
Other financial assets		–	–	(492)	**(492)**
Credit related commitments	20	(1,882)	93	(586)	**(2,375)**
Total credit loss expense		**(10,298)**	**(5,620)**	**8,755**	**(7,163)**

(Figures in tables are in thousands of Azerbaijani manats)

22. Net fee and commission income

Net fee and commission income comprise:

	2019	*2018*
Servicing plastic card operations	18,275	11,674
Settlements operations	14,801	10,216
Guarantees and letters of credit	13,079	8,941
Cash operations	2,860	2,687
Securities operations	–	13
Other	749	352
Fee and commission income	**49,764**	**33,883**
Servicing plastic card operations	(16,746)	(11,212)
Settlements operations	(3,288)	(3,090)
Guarantees and letters of credit	(1,717)	(1,567)
Cash operations	(1,337)	(798)
Securities operations	(50)	(41)
Other	(1,004)	(670)
Fee and commission expense	**(24,142)**	**(17,378)**
Net fee and commission income	**25,622**	**16,505**

23. Personnel, general and administrative expenses

Personnel expenses comprise:

	2019	*2018*
Salaries and bonuses	(47,404)	(40,546)
Social security costs	(5,294)	(7,274)
Other employee related expenses	(4,870)	(3,735)
Personnel expenses	**(57,568)**	**(51,555)**

General and administrative expenses comprise:

	2019	*2018*
Charity and sponsorship	(11,838)	(1,774)
Professional services	(8,244)	(8,329)
Insurance	(4,715)	(1,971)
Software cost	(3,837)	(3,872)
Advertising costs	(3,341)	(1,731)
Impairment of repossessed collateral	(1,962)	(2,347)
Taxes, other than income tax	(1,605)	(576)
Utilities	(1,487)	(1,062)
Membership fees	(1,351)	(1,520)
Operating leases	(1,330)	(7,563)
Security expenses	(978)	(844)
Stationery	(959)	(660)
Communications	(938)	(561)
Transportation and business trip expenses	(908)	(659)
Repair and maintenance	(872)	(966)
Entertainment	(658)	(659)
Printing expenses	(69)	(43)
Other expenses	(433)	(515)
General and administrative expenses	**(45,525)**	**(35,652)**

(Figures in tables are in thousands of Azerbaijani manats)

24. Risk management

Introduction

Risk is inherent in the Group's activities but it is managed through a process of ongoing identification, measurement and monitoring, subject to risk limits and other controls. This process of risk management is critical to the Group's continuing profitability and each individual within the Group is accountable for the risk exposures relating to his or her responsibilities. The Group is exposed to credit risk, liquidity risk and market risk, the latter being subdivided into trading and non-trading risks. It is also subject to operating risks.

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

Risk management structure

The Supervisory Board is ultimately responsible for identifying and controlling risks; however, there are separate independent bodies responsible for managing and monitoring risks.

Supervisory Board

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

Audit Committee

The Audit Committee has the overall responsibility for the establishment and development of the audit mission and strategy. It is responsible for the fundamental audit issues and monitoring Internal Audit's activities.

Executive Board

The Executive Board has the responsibility to monitor the overall risk process within the Group.

Risk Committee

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

Risk Management

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

Bank Treasury

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

Internal Audit

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

Risk measurement and reporting systems

The Group's risks are measured using a method which reflects both the expected loss likely to arise in normal circumstances and unexpected losses, which are an estimate of the ultimate actual loss based on statistical models. The models make use of probabilities derived from historical experience, adjusted to reflect the economic environment.

The Group also runs worse case scenarios that would arise in the event that extreme events which are unlikely to occur do, in fact, occur.

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

(Figures in tables are in thousands of Azerbaijani manats)

24. Risk management (continued)

Introduction (continued)

Information compiled from all the businesses is examined and processed in order to analyse, control and identify early risks. This information is presented and explained to the Management Board, the Risk Committee, and the head of each business division. The report includes aggregate credit exposure, hold limit exceptions and liquidity ratios. On a monthly basis detailed reporting of industry, customer and geographic risks takes place. Senior management assesses the appropriateness of the allowance for credit losses on a quarterly basis. The Board of Directors receives a comprehensive risk report once a quarter which is designed to provide all the necessary information to assess and conclude on the risks of the Group.

For all levels throughout the Group, specifically tailored risk reports are prepared and distributed in order to ensure that all business divisions have access to extensive, necessary and up-to-date information.

A daily briefing is given to the Management Board and all other relevant employees of the Group on the utilisation of market limits and liquidity, plus any other risk developments.

Risk mitigation

Group actively uses collateral to reduce its credit risks.

Excessive risk concentration

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

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

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 Group 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.

For more detail on the maximum exposure to credit risk for each class of financial instrument, references shall be made to the specific notes. The effect of collateral and other risk mitigation techniques is shown in Note 8.

(Figures in tables are in thousands of Azerbaijani manats)

24. Risk management (continued)

Credit risk (continued)

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.

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. Both LTECL and 12mECL are calculated on either an individual basis or a collective basis, depending on the nature of the underlying portfolio of financial instruments.

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 recognized, the Group recognizes an allowance based on 12m ECL. Stage 1 loans also include facilities where the credit risk has improved and the loan has been reclassified from Stage 2.

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

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 revenue is subsequently recognised based on a credit-adjusted EIR. ECL are only recognised or released to the extent that there is a subsequent change in the lifetime expected credit losses.

Definition of default and cure

The Group considers a financial instrument defaulted and therefore Stage 3 (credit-impaired) for ECL calculations in all cases when the borrower becomes 90 days past due on its contractual payments. The Group considers amounts due from banks defaulted and takes immediate action when the required intraday payments are not settled by the close of business as outlined in the individual agreements.

As a part of a qualitative assessment of whether a customer is in default, the Group also considers a variety of instances that may indicate unlikeliness to pay. When such events occur, the Group carefully considers whether the event should result in treating the customer as defaulted and therefore assessed as Stage 3 for ECL calculations or whether Stage 2 is appropriate.

24. Risk management (continued)

Credit risk (continued)

Such events include:

- Default and Credit-impaired assets:
  - Loans with principal amount and/or accrued interest and/or any of other payment overdue by more than 90 days from the date specified in the contract;
  - 2 times within three years restructured loans that have been overdue (in principal amount and/or accrued interest and/or any of other payment) less than 30 days from the date specified in the contract at the moment of each particular restructuring;
  - "Non-healthy" restructured loans that were PAR 30 at the moment of restructuring; (originally in Stage 3), when NPV loss restructuring is more than 10%;
  - Any loan considered by management as non-performing (except non-performing loans that meet Stage 2 criteria).
- Existing of information that borrower will/has enter bankruptcy, insolvency or a similar condition.
- Default (according to IRB and External Rating).
- Default on other financial instruments of the same borrower.

It is the Group's policy to consider a financial instrument as 'cured' and therefore re-classified out of Stage 3 when none of the default criteria have been present for at least six consecutive months. The decision whether to classify an asset as Stage 2 or Stage 1 once cured depends on the updated credit grade, at the time of the cure, and whether this indicates there has been a significant increase in credit risk compared to initial recognition.

Internal rating and PD estimation process

The Group's Risk Department operates its internal rating models. The Group runs separate models for its key portfolios in which its corporate customers are rated based on Moody's model. Small and medium enterprises and consumer loans are scored from 1 to 20 and from 1 to 4 using internal grades, respectively. The models incorporate both qualitative and quantitative information and, in addition to information specific to the borrower, utilise supplemental external information that could affect the borrower's behaviour. Where practical, they also build on information from the national and international external rating agencies. PDs, incorporating forward looking information and the IFRS 9 stage classification of the exposure, are assigned for each grade. This is repeated for each economic scenario as appropriate.

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 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.
- Any publicly available information on the clients from external parties. This includes external rating grades issued by rating agencies.
- Any macro-economic or geopolitical information, e.g., GDP growth relevant for the specific industry and geographical segments where the client operates.
- 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.

24. Risk management (continued)

Credit risk (continued)

Consumer lending

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) and payment to income (PTI) ratios. Other key inputs into the models are GDP growth, changes in personal income/salary levels, personal indebtedness.

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

Internal rating grade for SME	Moody's based internal/external ratings for Corporate and Financial institutions	Internal rating description
1	Aaa	High grade
2-4	Aa1 to Aa3	
5-7	A1 to A3	
8-10	Baa1 to Baa3	Standard grade
11-13	Ba1 to Ba3	
14-16	B1 to B3	
17-19	Caa1 to Caa3	Sub-standard grade
20	Ca	
Default	C	Impaired

Internal rating for consumer loans is based on overdue days. High grade rating is used for Central Bank and Ministry of Finance of the Republic of Azerbaijan.

Exposure at default

The exposure at default (EAD) represents the gross carrying amount of the financial instruments subject to the impairment calculation, addressing both the client's ability to increase its exposure while approaching default and potential early repayments too. To calculate the EAD for a Stage 1 loan, the Group assesses the possible default events within 12 months for the calculation of the 12mECL. For Stage 2, Stage 3 financial assets, the exposure at default is considered for events over the lifetime of the instruments.

The Group determines EADs by modelling the range of possible exposure outcomes at various points in time, corresponding the multiple scenarios. The IFRS 9 PDs are then assigned to each economic scenario based on the outcome of Group 's models.

Loss given default

For corporate lending assets, LGD values are assessed semi-annually.

The credit risk assessment is based on a standardized LGD assessment framework that results in a certain LGD rate. These LGD rates take into account the expected EAD in comparison to the amount expected to be recovered or realised from any collateral held.

Where appropriate, further recent data is used in order to determine the IFRS 9 LGD rate for each group of financial instruments. When assessing forward-looking information, the expectation is based on multiple scenarios. Examples of key inputs involve changes in, collateral values including property prices for mortgages, commodity prices, payment status or other factors that are indicative of losses in the group.

The Group segments its retail lending products into smaller homogeneous portfolios, based on key characteristics that are relevant to the estimation of future cash flows. The applied data is based on historically collected loss data and involves a wider set of transaction characteristics (e.g., product type) as well as borrower characteristics.

LGD rates are estimated for the Stage 1, Stage 2, Stage 3 and POCI segment of each asset class.

Significant increase in credit risk

The Group continuously monitors all assets subject to ECLs. In order to determine whether an instrument or a portfolio of instruments is subject to 12mECL or LTECL, the Group assesses whether there has been a significant increase in credit risk since initial recognition.

24. Risk management (continued)

Credit risk (continued)

The Group also applies a secondary qualitative method for triggering a significant increase in credit risk for an asset, such as moving a customer/facility to the watch list, or the account becoming restructured due to credit event. In certain cases, the Group may also consider that events explained in "Definition of default" section above are a significant increase in credit risk as opposed to a default. Regardless of the change in credit grades, if contractual payments are more than 30 days past due, the credit risk is deemed to have increased significantly since initial recognition.

When estimating ECLs on a collective basis for a group of similar assets, the Group applies the same principles for assessing whether there has been a significant increase in credit risk since initial recognition.

Grouping financial assets measured on a collective basis

Dependent on the factors below, the Group calculates ECLs either on a collective or on an individual basis.

Asset classes where the Group calculates ECL on an individual basis include:

- PD for all corporate and small business lending;
- LGD for Stage 3 corporate and small business lending which are above predetermined threshold and are collateralized.

Asset classes where the Group calculates ECL on a collective basis include:

- PD and LGD for all consumer lending;
- LGD for all corporate and small business lending which are in Stage 1 and Stage 2;
- LGD for corporate and small business lending which are in Stage 3, neither are above predetermined threshold nor are collateralized.

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:

- GDP growth rates;
- Inflation;
- Monetary policy rate;
- Dynamics of real and nominal effective exchange rates;
- Real estate price.

The inputs and models used for calculating ECLs may not always capture all characteristics of the market at the date of the financial statements. To reflect this, qualitative adjustments or overlays are occasionally made as temporary adjustments when such differences are significantly material.

The Group obtains the forward-looking information from third party sources (external rating agencies, governmental bodies e.g. central Groups, and international financial institutions). Experts of the Group's Credit Risk Department determine the weights attributable to the multiple scenarios with the values of the key forward looking economic variables/assumptions used in each of the economic scenarios for the ECL calculations.

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

(Figures in tables are in thousands of Azerbaijani manats)

24. Risk management (continued)

Credit risk (continued)

Credit quality per class of financial assets

The credit quality of financial assets is managed by the Group internal credit ratings. 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 for the year ended 31 December 2019.

	Note		*High grade*	*Standard grade*	*Sub-standard grade*	*Impaired*	*Total*
Cash and cash equivalents, except for cash on hand	5	Stage 1	897,217	192,981	–	–	**1,090,198**
Amounts due from credit institutions	6	Stage 1	267,301	313,926	29,514	–	**610,741**
		Stage 2	–	–	14,214	–	**14,214**
Loans to customers	8	Stage 1	392,613	1,125,719	84,864	–	**1,603,196**
		Stage 2	39,296	236,529	322,267	–	**598,092**
		Stage 3	–	–	–	162,621	**162,621**
Investment securities:	7						
- Measured at FVOCI		Stage 1	938,957	168,427	–	–	**1,107,384**
		Stage 2	–	–	583	–	**583**
- Measured at amortised cost		Stage 1	–	38,812	–	–	**38,812**
Unused credit lines	20	Stage 1	21,312	149,191	16,053	–	**186,556**
		Stage 2	–	23,123	6,738	–	**29,861**
Letters of credit	20	Stage 1	13,495	10,774	205	–	**24,474**
		Stage 2	841	657	17	–	**1,515**
Guarantees issued	20	Stage 1	35,552	499,537	17,245	–	**552,334**
		Stage 2	4,090	35,700	36,201	–	**75,991**
		Stage 3	–	–	–	971	**971**
Other financial assets	12	Stage 1	–	10,277	–	–	**10,277**
Total			**2,610,674**	**2,805,653**	**527,901**	**163,592**	**6,107,820**

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 for the year ended 31 December 2018.

	Note		*High grade*	*Standard grade*	*Sub-standard grade*	*Impaired*	*Total*
Cash and cash equivalents, except for cash on hand	5	Stage 1	1,248,809	115,093	3,214	–	**1,367,116**
Amounts due from credit institutions	6	Stage 1	192,579	121,825	3,384	–	**317,788**
		Stage 2	–	–	17,415	–	**17,415**
Loans to customers	8	Stage 1	95,833	1,142,713	45,868	–	**1,284,414**
		Stage 2	64,416	100,837	165,846	–	**331,099**
		Stage 3	–	–	4,140	161,129	**165,269**
Investment securities	7						
- Measured at FVOCI		Stage 1	1,301,613	123,689	625	–	**1,425,927**
- Measured at amortised cost		Stage 1	–	32,527	–	–	**32,527**
Unused credit lines	20	Stage 1	–	111,012	3,740	–	**114,752**
		Stage 2	94	11,080	7,545	–	**18,719**
		Stage 3	–	–	8	–	**8**
Letters of credit	20	Stage 1	395	4,428	323	–	**5,146**
Guarantees issued	20	Stage 1	13,904	493,744	4,479	–	**512,127**
		Stage 2	3,503	20,088	13,399	–	**36,990**
		Stage 3	–	–	–	79	**79**
Other financial assets	12	Stage 1	–	14,103	–	–	**14,103**
Total			**2,921,146**	**2,291,139**	**269,986**	**161,208**	**5,643,479**

See Note 8 for more detailed information with respect to the allowance for impairment of loans to customers.

Financial guarantees, unused credit lines and letters of credit are assessed and a provision for expected credit losses is calculated in similar manner as for loans. See Note 20.

(Figures in tables are in thousands of Azerbaijani manats)

24. Risk management (continued)

Credit risk (continued)

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

	2019				*2018*			
	The Republic of Azerbaijan	*OECD countries*	*CIS and other non-OECD countries*	*Total*	*The Republic of Azerbaijan*	*OECD countries*	*CIS and other non-OECD countries*	*Total*
Financial assets								
Cash and cash equivalents	633,113	473,933	78,793	**1,185,839**	667,549	763,596	71,901	**1,503,046**
Trading securities	–	–	–	**–**	–	895	–	**895**
Amounts due from credit institutions	70,974	503,913	49,507	**624,394**	50,597	239,269	44,968	**334,834**
Investment securities	676,754	381,513	88,086	**1,146,353**	603,212	832,649	22,285	**1,458,146**
Derivative financial assets	121	86	250	**457**	1,064	722	264	**2,050**
Loans to customers	1,822,674	239,632	234,682	**2,296,988**	1,341,437	254,761	135,367	**1,731,565**
Other financial assets	7,276	2,686	–	**9,962**	6,735	6,876	–	**13,611**
	3,210,912	**1,601,763**	**451,318**	**5,263,993**	**2,670,594**	**2,098,768**	**274,785**	**5,044,147**
Financial liabilities								
Amounts due to banks and government funds	727,535	86,908	47,700	**862,143**	498,758	8,823	17,394	**524,975**
Amounts due to customers	3,689,076	9,395	90,470	**3,788,941**	3,892,304	8,484	53,164	**3,953,952**
Derivative financial liabilities	–	–	137	**137**	–	37	44	**81**
Debt securities issued	133,797	2,234	–	**136,031**	84,922	17,378	–	**102,300**
Subordinated debts	27,111	–	–	**27,111**	18,921	–	–	**18,921**
Lease liabilities	6,188	40	3,309	**9,537**	–	–	–	**–**
Other financial liabilities	3,887	3,998	1,007	**8,892**	12,552	7,118	204	**19,874**
	4,587,594	**102,575**	**142,623**	**4,832,792**	**4,507,457**	**41,840**	**70,806**	**4,620,103**
Net assets/(liabilities)	**(1,376,682)**	**1,499,188**	**308,595**	**431,201**	**(1,836,863)**	**2,056,928**	**203,979**	**424,044**

Liquidity risk and funding management

Liquidity risk is the risk that the Group will be unable to meet its payment obligations when they fall due under normal and stress circumstances. To limit this risk, management has arranged diversified funding sources in addition to its core deposit base, manages assets with liquidity in mind, and monitors future cash flows and liquidity on a daily basis. This incorporates an assessment of expected cash flows and the availability of high grade collateral which could be used to secure additional funding if required.

The Group maintains a portfolio of highly marketable and diverse assets that can be easily liquidated in the event of an unforeseen interruption of cash flow. In addition, the Group maintains obligatory reserves with the CBAR, NBG and Banking Regulation and Supervision Agency ("BRSA"), the amount of which depends on the level of customer funds attracted.

The liquidity position is assessed and managed by the Group based on certain liquidity ratios established by the CBAR. As at 31 December 2019 and 2018, these ratios were as follows:

	2019, %	*2018, %*
Instant Liquidity Ratio (30% is the minimum required by the CBAR) (assets receivable or realisable within one day/liabilities repayable on demand)	64	44

As at 31 December 2019, liquidity ratio of PASHA Bank Georgia JSC (average volume of liquid assets / average volume of liabilities) based on requirements established by the NBG was 52% (31 December 2018: 34%). Minimum required level of liquidity by NBG is 30%.

As at 31 December 2019, liquidity ratio of PASHA Yatirim Bankasi A.S. based on requirements established by the BRSA was 865% (31 December 2018: 865%). Minimum required level of liquidity by BRSA is 100%.

24. Risk management (continued)

Liquidity risk and funding management (continued)

Analysis of financial liabilities by remaining contractual maturities

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

Financial liabilities	*Less than 3 months*	*3 to 12 months*	*1 to 5 years*	*Over 5 years*	*Total 2019*
As at 31 December 2019					
Amounts due to banks and government funds	305,356	79,729	416,168	97,680	**898,933**
Amounts due to customers	2,802,903	592,092	351,914	98,453	**3,845,362**
Debt securities issued	3,425	3,502	140,590	–	**147,517**
Subordinated debts	281	1,104	24,621	9,792	**35,798**
Net settled derivative financial liabilities	137	–	–	–	**137**
Lease liabilities	1,471	4,338	4,582	108	**10,499**
Other financial liabilities	8,892	–	–	–	**8,892**
Total undiscounted financial liabilities	**3,122,465**	**680,765**	**937,875**	**206,033**	**4,947,138**

Financial liabilities	*Less than 3 months*	*3 to 12 months*	*1 to 5 years*	*Over 5 years*	*Total 2018*
As at 31 December 2018					
Amounts due to banks and government funds	197,228	108,757	151,777	86,531	**544,293**
Amounts due to customers	3,142,801	446,785	320,478	99,865	**4,009,929**
Debt securities issued	18,474	2,481	93,172	–	**114,127**
Subordinated debts	281	281	21,726	–	**22,288**
Derivative financial liabilities	37	–	–	–	**37**
Other financial liabilities	19,874	–	–	–	**19,874**
Total undiscounted financial liabilities	**3,378,695**	**558,304**	**587,153**	**186,396**	**4,710,548**

The table below shows the contractual expiry by maturity of the Group's credit related commitments.

	Less than 3 months	*3 to 12 months*	*1 to 5 years*	*Over 5 years*	*Maturity undefined*	*Total*
As at 31 December 2019	306,312	295,317	236,468	103	33,502	**871,702**
As at 31 December 2018	238,711	132,336	271,499	6,812	38,463	**687,821**

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

The Group's capability to repay its liabilities relies on its ability to realise an equivalent amount of assets within the same period of time. There is a significant concentration of deposits from organizations of related parties in the period of one year. Any significant withdrawal of these funds would have an adverse impact on the operations of the Group.

This level of funding will remain with the Group for the foreseeable future and that in the event of withdrawal of funds, the Group would be given sufficient notice so as to realise its liquid assets to enable repayment. Management believes that this level of funding will remain with the Group for the foreseeable future and that in the event of withdrawal of funds, the Group would be given sufficient notice so as to realise its liquid assets to enable repayment.

The maturity analysis does not reflect the historical stability of current accounts. Their liquidation has historically taken place over a longer period than indicated in the tables above. These balances are included in amounts due in less than three months in the tables above.

Included in amounts due to customers are term deposits of individuals. In accordance with the legislation, the Group is obliged to repay such deposits upon demand of a depositor.

(Figures in tables are in thousands of Azerbaijani manats)

24. Risk management (continued)

Operational risk

Operational risk is the risk of loss arising from systems failure, human error, fraud or external events. When controls fail to perform, operational risks can cause damage to reputation, have legal or regulatory implications, or lead to financial loss.

The Group cannot expect to eliminate all operational risks, but through a control framework and by monitoring and responding to potential risks, the Group is able to manage the risks. Controls include effective segregation of duties, access, authorisation and reconciliation procedures, staff education and assessment processes, including the use of internal audit.

Market risk

Market risk is the risk that the fair value or future cash flows of financial instruments will fluctuate due to changes in market variables such as interest rates, foreign exchanges, and equity prices. The Group manages exposures to market risk based of sensitivity analysis. The Group has no significant concentration of market risk.

Interest rate risk

Interest rate risk arises from the possibility that changes in interest rates will affect future cash flows or the fair values of financial instruments.

The sensitivity of current year profit is the effect of the assumed changes in interest rates on the net interest income for one year, based on the floating rate non-trading financial assets and financial liabilities held at 31 December 2019. The Group does not have substantial amount of floating rate non-trading financial instruments as at 31 December 2019 and 2018.

Currency risk

Currency risk is the risk that the value of a financial instrument will fluctuate due to changes in foreign exchange rates. The Group has set limits on positions by currency based on the local regulations. Positions are monitored on a daily basis.

The Assets and Liabilities Management Committee controls currency risk by management of the open currency position on the estimated basis of local currency devaluation and other macroeconomic indicators, which gives the Group an opportunity to minimize losses from significant currency rates fluctuations toward its national currency The Treasury Department performs daily monitoring of the Group's open currency position with the aim to match the requirements of the local regulators.

As at 31 December 2019, the Group had the following exposure to foreign currency exchange rate risk:

	AZN	*USD*	*EUR*	*GEL*	*TRY*	*Other*	*Total 2019*
Financial assets							
Cash and cash equivalents	461,280	452,908	149,909	14,940	43,127	63,675	**1,185,839**
Amounts due from credit institutions	48,327	443,009	133,058	–	–	–	**624,394**
Investment securities	527,330	485,076	114,456	14,873	4,618	–	**1,146,353**
Derivative financial assets	169	47	–	241	–	–	**457**
Loans to customers	866,769	918,023	306,609	63,296	57,456	84,835	**2,296,988**
Other financial assets	1,616	4,722	860	3	2,687	74	**9,962**
Total financial assets	**1,905,491**	**2,303,785**	**704,892**	**93,353**	**107,888**	**148,584**	**5,263,993**
The effect of derivatives	–	112,407	–	7,745	–	–	**120,152**
Financial liabilities							
Amounts due to banks and government funds	360,997	276,271	110,467	7,772	21,570	85,066	**862,143**
Amounts due to customers	1,335,710	1,804,717	538,325	45,203	2,981	62,005	**3,788,941**
Derivative financial liabilities	–	135	–	–	–	2	**137**
Debt securities issued	–	127,691	6,106	–	2,234	–	**136,031**
Subordinated debts	–	27,111	–	–	–	–	**27,111**
Lease liabilities	5,632	3,692	–	173	40	–	**9,537**
Other financial liabilities	1,616	1,507	1,183	590	3,953	43	**8,892**
Total financial liabilities	**1,703,955**	**2,241,124**	**656,081**	**53,738**	**30,778**	**147,116**	**4,832,792**
The effect of derivatives	–	6,809	–	–	3,388	551	**10,748**
Net position after the effect of derivatives	**201,536**	**168,259**	**48,811**	**47,360**	**73,722**	**917**	**540,605**

24. Risk management (continued)

Currency risk (continued)

As at 31 December 2018, the Group had the following exposure to foreign currency exchange rate risk:

	AZN	*USD*	*EUR*	*GEL*	*TRY*	*Other*	*Total 2018*
Financial assets							
Cash and cash equivalents	436,106	848,599	166,972	13,742	22,186	15,441	**1,503,046**
Trading securities	–	494	–	–	401	–	**895**
Amounts due from credit institutions	21,735	246,842	45,711	3,256	–	17,290	**334,834**
Investment securities	485,791	840,234	117,414	12,037	2,670	–	**1,458,146**
Derivative financial assets	1,064	722	–	264	–	–	**2,050**
Loans to customers	642,311	717,367	213,706	45,147	113,034	–	**1,731,565**
Other financial assets	2,074	499	3,934	7	7,095	2	**13,611**
Total financial assets	**1,589,081**	**2,654,757**	**547,737**	**74,453**	**145,386**	**32,733**	**5,044,147**
The effect of derivatives	34,529	15,380	–	–	557	–	**50,466**
Financial liabilities							
Amounts due to banks and government funds	276,508	160,773	71,266	4,463	11,221	744	**524,975**
Amounts due to customers	1,114,474	2,326,046	461,877	12,294	7,204	32,057	**3,953,952**
Other borrowed funds	–	–	–	44	37	–	**81**
Derivative financial liabilities	–	84,922	–	–	17,378	–	**102,300**
Debt securities issued	–	18,921	–	–	–	–	**18,921**
Other financial liabilities	10,902	3,680	1,110	156	4,026	–	**19,874**
Total financial liabilities	**1,401,884**	**2,594,342**	**534,253**	**16,957**	**39,866**	**32,801**	**4,620,103**
The effect of derivatives	–	35,181	–	–	15,240	–	**50,421**
Net position after the effect of derivatives	**221,726**	**40,614**	**13,484**	**57,496**	**90,837**	**(68)**	**424,089**

Currency risk sensitivity

The tables below indicate the currencies to which the Group had significant exposure at 31 December on its monetary assets and liabilities. The analysis calculates the effect of a reasonably possible movement of the currency rate against the Azerbaijani Manates, with all other variables held constant on the consolidated statement of profit or loss. The sensitivity analysis includes only outstanding foreign currency denominated monetary items and adjusts their translation at the end of the period for specified changes 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. The effect on equity does not differ from the effect on the consolidated statement of profit or loss. A negative amount in the table reflects a potential net reduction in the consolidated statement of profit or loss or equity, while a positive amount reflects a net potential increase. Impact on profit before tax based on assets value as at 31 December 2019 and 2018:

	2019		*2018*	
	USD/AZN +10%	*USD/AZN -3%*	*USD/AZN +14%*	*USD/AZN -3%*
Impact on profit before tax	16,826	(5,048)	5,686	(1,218)

	2019		*2018*	
	EUR/AZN +10%	*EUR/AZN -6%*	*EUR/AZN +14%*	*EUR/AZN -3%*
Impact on profit before tax	4,881	(2,929)	1,888	(405)

	2019		*2018*	
	GEL/AZN +15%	*GEL/AZN -15%*	*GEL/AZN +15%*	*GEL/AZN -15%*
Impact on profit before tax	7,104	(7,104)	8,624	(8,624)

	2019		*2018*	
	TRY/AZN +15%	*TRY/AZN -17%*	*TRY/AZN +20%*	*TRY/AZN -25%*
Impact on profit before tax	11,058	(12,532)	18,167	(22,709)

(Figures in tables are in thousands of Azerbaijani manats)

25. Fair values measurement

Fair value hierarchy

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

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

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:

		Fair value measurement using			
	Date of valuation	*Quoted prices in active markets (Level 1)*	*Significant observable inputs (Level 2)*	*Significant unobservable inputs (Level 3)*	*Total*
Assets measured at fair value					
Investment securities – at FVOCI	31 December 2019	168,561	939,406	–	**1,107,967**
Derivative financial assets	31 December 2019	–	457	–	**457**
Assets for which fair values are disclosed					
Cash and cash equivalents	31 December 2019	1,185,839	–	–	**1,185,839**
Amounts due from credit institutions	31 December 2019	–	624,394	–	**624,394**
Investment securities measured at amortised cost	31 December 2019	24,143	–	15,830	**39,973**
Loans to customers	31 December 2019	–	–	2,271,826	**2,271,826**
Investment property	31 December 2019	–	–	43,202	**43,202**
Other financial assets	31 December 2019	–	–	9,962	**9,962**

		Fair value measurement using			
	Date of valuation	*Quoted prices in active markets (Level 1)*	*Significant observable inputs (Level 2)*	*Significant unobservable inputs (Level 3)*	*Total*
Liabilities measured at fair value					
Derivative financial liabilities	31 December 2019	–	137	–	**137**
Liabilities for which fair values are disclosed					
Amounts due to banks and government funds	31 December 2019	–	862,071	–	**862,071**
Amounts due to customers	31 December 2019	–	–	3,789,139	**3,789,139**
Debt securities issued	31 December 2019	–	–	137,580	**137,580**
Subordinated debts	31 December 2019	–	–	27,111	**27,111**
Other financial liabilities	31 December 2019	–	–	8,892	**8,892**

(Figures in tables are in thousands of Azerbaijani manats)

25. Fair values measurement (continued)

Fair value hierarchy (continued)

	Date of valuation	Fair value measurement using: Quoted prices in active markets (Level 1)	Significant observable inputs (Level 2)	Significant unobservable inputs (Level 3)	Total
Assets measured at fair value					
Trading securities	31 December 2018	895	–	–	**895**
Investment securities – at FVOCI	31 December 2018	337,346	1,088,581	–	**1,425,927**
Derivative financial assets	31 December 2018	–	2,050	–	**2,050**
Assets for which fair values are disclosed					
Cash and cash equivalents	31 December 2018	1,503,046	–	–	**1,503,046**
Amounts due from credit institutions	31 December 2018	–	334,834	–	**334,834**
Investment securities measured at amortised cost	31 December 2018	19,585	–	13,487	**33,072**
Loans to customers	31 December 2018	–	–	1,682,643	**1,682,643**
Investment property	31 December 2018	–	–	71,719	**71,719**
Other financial assets	31 December 2018	–	–	13,611	**13,611**

	Date of valuation	Fair value measurement using: Quoted prices in active markets (Level 1)	Significant observable inputs (Level 2)	Significant unobservable inputs (Level 3)	Total
Liabilities measured at fair value					
Derivative financial liabilities	31 December 2018	–	81	–	**81**
Liabilities for which fair values are disclosed					
Amounts due to banks and government funds	31 December 2018	–	525,021	–	**525,021**
Amounts due to customers	31 December 2018	–	–	3,953,178	**3,953,178**
Debt securities issued	31 December 2018	–	–	103,096	**103,096**
Subordinated debt	31 December 2018	–	–	18,921	**18,921**
Other financial liabilities	31 December 2018	–	–	19,874	**19,874**

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.

	Carrying value 2019	*Fair value 2019*	*Unrecognized gain/(loss) 2019*	*Carrying value 2018*	*Fair value 2018*	*Unrecognized gain/(loss) 2018*
Financial assets						
Cash and cash equivalents	1,185,839	1,185,839	–	1,503,046	1,503,046	–
Amounts due from credit institutions	624,394	624,394	–	334,834	334,834	–
Investment securities measured at amortised cost	38,386	39,973	1,587	32,219	33,072	853
Loans to customers	2,296,988	2,271,826	(25,162)	1,731,565	1,682,643	(48,922)
Other financial assets	9,962	9,962	–	13,611	13,611	–
Financial liabilities						
Amounts due to banks and government funds	862,143	862,071	72	524,975	525,021	(46)
Amounts due to customers	3,788,941	3,789,139	(198)	3,953,952	3,953,178	774
Subordinated debts	27,111	27,111	–	18,921	18,921	–
Debt securities issued	136,031	137,580	(1,549)	102,300	103,096	(796)
Other financial liabilities	8,892	8,892	–	19,874	19,874	–
Total unrecognised change in unrealised fair value			**(19,930)**			**(48,137)**

(Figures in tables are in thousands of Azerbaijani manats)

25. Fair values measurement (continued)

Valuation techniques and assumptions

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

Assets for which fair value approximates carrying value

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

Derivatives

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

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

Fair value of unquoted instruments, loans to customers, customer deposits, amounts due from credit institutions and amounts due to banks and government funds, subordinated debts and other financial assets and liabilities is estimated by discounting future cash flows using rates currently available for debt on similar terms, credit risk and remaining maturities.

(Figures in tables are in thousands of Azerbaijani manats)

26. Maturity analysis of assets and liabilities

The table below shows an analysis of assets and liabilities according to when they are expected to be recovered or settled See Note 24 "Risk management" for the Group's contractual undiscounted repayment obligations.

	2019			*2018*		
	Within one year	*More than one year*	*Total*	*Within one year*	*More than one year*	*Total*
Cash and cash equivalents	1,185,839	–	**1,185,839**	1,503,046	–	**1,503,046**
Trading securities	–	–	**–**	895	–	**895**
Amounts due from credit institutions	573,209	51,185	**624,394**	334,834	–	**334,834**
Investment securities	831,184	315,169	**1,146,353**	1,194,736	263,410	**1,458,146**
Derivative financial assets	457	–	**457**	2,050	–	**2,050**
Loans to customers	974,567	1,322,421	**2,296,988**	792,469	939,096	**1,731,565**
Investment property	–	43,202	**43,202**	–	71,719	**71,719**
Property and equipment	–	46,036	**46,036**	–	18,236	**18,236**
Intangible assets	–	50,421	**50,421**	–	49,754	**49,754**
Right-of-use assets	3,968	5,174	**9,142**	–	–	**–**
Current income tax assets	3,198	–	**3,198**	–	–	**–**
Deferred income tax assets	–	4,466	**4,466**	–	4,003	**4,003**
Other assets	29,906	37	**29,943**	34,457	659	**35,116**
Total assets	**3,602,328**	**1,838,111**	**5,440,439**	**3,862,487**	**1,346,877**	**5,209,364**
Amounts due to banks and government funds	401,199	460,944	**862,143**	306,430	218,545	**524,975**
Amounts due to customers	3,372,364	416,577	**3,788,941**	3,569,598	384,354	**3,953,952**
Debt securities issued	2,614	133,417	**136,031**	20,610	81,690	**102,300**
Derivative financial liabilities	137	–	**137**	37	44	**81**
Current income tax liability	560	–	**560**	5,516	–	**5,516**
Deferred income tax liabilities	–	13,037	**13,037**	–	7,886	**7,886**
Subordinated debts	–	27,111	**27,111**	–	18,921	**18,921**
Lease liabilities	4,475	5,062	**9,537**	–	–	**–**
Provision for credit related guarantees and other assets	10,550	–	**10,550**	6,425	–	**6,425**
Other liabilities	30,350	1,986	**32,336**	41,299	–	**41,299**
Total liabilities	**3,822,249**	**1,058,134**	**4,880,383**	**3,949,915**	**711,440**	**4,661,355**
Net assets	**(219,921)**	**779,977**	**560,056**	**(87,428)**	**635,437**	**548,009**

Negative gap is due to significant concentration of amounts due to customers represented by related parties in the period of one year. Management believes that this level of funding will remain with the Group for the foreseeable future and that in the event of withdrawal of funds, the Group would be given sufficient notice so as to realise its liquid assets to enable repayment.

27. Related party disclosures

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

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

(Figures in tables are in thousands of Azerbaijani manats)

27. Related party disclosures (continued)

The volumes of related party transactions, outstanding balances at the year end, and related expense and income for the year are as follows:

	2019					2018				
	Share-Holders/ Ultimate owners	*Entities under common control*	*Key management personnel*	*Other*	*Total*	*Share-Holders/ Ultimate owners*	*Entities under common control*	*Key management personnel*	*Other*	*Total*
Cash and cash equivalents	–	297	–	–	297	–	60	–	–	60
Loans outstanding at 1 January, gross	–	130,098	4,284	33,897	168,279	–	110,974	3,380	24,285	138,639
Loans issued during the year	–	389,580	6,073	73,168	468,821	–	179,381	5,412	36,462	221,255
Loan repayments during the year	–	(68,720)	(4,626)	(71,663)	(145,009)	–	(155,271)	(3,354)	(26,835)	(185,460)
Interest accrual	–	2,003	75	–	2,078	–	–	186	126	312
Foreign currency translation difference	–	524	(788)	(64)	(328)	–	(4,986)	(1,340)	(141)	(6,467)
Loans outstanding at 31 December, gross	–	453,485	5,018	35,338	493,841	–	130,098	4,284	33,897	168,279
Less: allowance for impairment at 31 December	–	(5,598)	(143)	(543)	(6,284)	–	(1,172)	(114)	(191)	(1,477)
Loans outstanding at 31 December, net	–	447,887	4,875	34,795	487,557	–	128,926	4,170	33,706	166,802
Interest income on loans	–	12,345	416	3,163	15,924	–	7,761	368	1,918	10,047
Deposit at 1 January	–	269,800	5,358	93,762	368,920	–	436,436	4,978	94,685	536,099
Deposits received during the year	–	1,285,414	14,578	19,736	1,319,728	–	1,039,466	11,729	55,784	1,106,979
Deposits repaid during the year	–	(1,011,218)	(14,204)	(14,982)	(1,040,404)	–	(1,190,743)	(11,546)	(54,139)	(1,256,428)
Interest accrual	–	245	3	41	289	–	683	117	–	800
Foreign currency translation difference	–	(5,198)	469	(824)	(5,553)	–	(16,042)	80	(2,568)	(18,530)
Deposits at 31 December	–	539,043	6,204	97,733	642,980	–	269,800	5,358	93,762	368,920
Amounts due to banks and government funds	–	49,928	–	–	49,928	–	50,005	–	–	50,005
Current accounts	136,574	348,748	3,892	375,406	864,620	45,059	511,255	2,767	829,768	1,388,849
Subordinated debts	18,923	8,188	–	–	27,111	18,921	–	–	–	18,921
Debt securities issued	85,199	37,882	–	–	123,081	42,464	40,675	–	–	83,139
Other assets	25	498	–	26	549	–	334	14	3	351
Other liabilities	–	3,549	–	219	3,768	36	2,912	–	219	3,167
Lease liabilities	–	4,152	–	–	4,152	–	–	–	–	–
Right of use assets	–	4,029	–	–	4,029	–	–	–	–	–
Paid-in capital	–	343	–	–	343	–	–	–	–	–
Interest expense on deposits	(3,385)	(17,270)	(161)	(2,612)	(23,428)	(1,428)	(17,435)	(262)	(3,081)	(22,206)
Guarantees issued	–	18,799	–	11,725	30,524	–	6,766	–	6,173	12,939
Letters of credit issued	–	492	–	1,872	2,364	–	–	–	573	573
Unused credit lines	180	10,103	1,662	17,681	29,626	182	13,639	1,789	6,061	21,671
Interest income (except loans)	–	58	–	–	58	–	–	–	–	–
Fee and commission income	154	6,218	61	1,730	8,163	48	4,177	26	1,539	5,790
Fee and commission expense	(1,526)	(2,661)	–	(24)	(4,211)	(400)	(112)	–	(35)	(547)
Net gains/(losses) from foreign currencies: dealing	726	2,918	53	1,517	5,214	1,237	3,106	38	2,225	6,606
Net gains/(losses) from foreign currencies: translation differences	–	3,469	–	–	3,469	–	–	–	–	–
Net gains/(losses) from foreign currencies: operations with foreign currency derivatives	–	28	–	–	28	–	–	–	–	–
Other operating expenses	–	(3,014)	–	(40)	(3,054)	(59)	(2,713)	(5)	–	(2,777)
Other income	25	–	1	–	26	–	34	–	–	34

As at 31 December 2019, the Group has guarantees from its parent received as a collateral in respect of loans issued to borrowers in the amount of AZN 181,315 thousand (2018: AZN 89,765 thousand) and the Group incurred guarantee fee in the amount of AZN 1,530 thousand which was accounted as a part of effective interest rate.

Compensation to members of key management personnel was comprised of the following:

	2019	*2018*
Salaries and other benefits	(13,156)	(11,902)
Social security costs	(1,651)	(2,056)
Total key management compensation	**(14,807)**	**(13,958)**

(Figures in tables are in thousands of Azerbaijani manats)

28. Changes in liabilities arising from financing activities

	Note	*Debt securities issued*	*Subordinated debts*	*Total liabilities from financing activities*
Carrying amount at 31 December 2017		**81,765**	–	**81,765**
Proceeds from issue		146,132	18,700	**164,832**
Redemption		(110,453)	–	**(110,453)**
Foreign currency translation		(15,085)	–	**(15,085)**
Other		(59)	221	**162**
Carrying amount at 31 December 2018	15, 16	**102,300**	**18,921**	**121,221**
Proceeds from issue		103,825	8,772	**112,597**
Redemption		(70,901)	–	**(70,901)**
Fair value adjustment		–	(343)	**(343)**
Foreign currency translation		1,132	(281)	**851**
Other		(325)	42	**(283)**
Carrying amount at 31 December 2019	15, 16	**136,031**	**27,111**	**163,142**

29. Capital adequacy

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

During the past year, the Group had complied in full with all its externally imposed capital requirements.

The primary objectives of the Group's capital management are to ensure that the Group complies with externally imposed capital requirements and that the Group maintains strong credit ratings and healthy capital ratios in order to support its business and to maximise shareholders' value.

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

CBAR capital adequacy ratio

The CBAR requires banks to maintain a minimum capital adequacy ratio of 11.0% (31 December 2018: 10.0%) of risk-weighted assets for regulatory capital. As at 31 December 2019 and 2018 the Bank's capital adequacy ratio on this basis was as follows:

	2019	*2018*
Tier 1 capital	342,836	313,559
Tier 2 capital	87,684	121,482
Less: deductions from capital	(149,301)	(149,301)
Total regulatory capital	**281,219**	**285,740**
Risk-weighted assets	**2,363,195**	**2,099,493**
Capital adequacy ratio (Tier 1)	14.5%	14.9%
Capital adequacy ratio (Total Capital)	11.9%	11.8%

The requirement for minimum total capital adequacy ratio has been changed to 12% starting from 1 January 2020. The Bank was in compliance with the capital adequacy ratios at the end of each subsequent reporting months.

NBG capital adequacy ratio

The NBG requires banks to maintain a minimum total capital adequacy ratio of 24.8% (31 December 2018: 24.8%) and Tier 1 / Core Tier 1 Capital ratio of 9.4% (31 December 2018: 9.4%) of risk-weighted assets, computed based on Basel III requirements. As at 31 December 2019 the Bank's capital adequacy ratio on this basis was 26.1% (31 December 2018: 30.0%) and Tier 1 / Core Tier 1 Capital ratio was 19.1% (31 December 2018: 28.9%).

(Figures in tables are in thousands of Azerbaijani manats)

29. Capital adequacy (continued)

BRSA capital adequacy ratio

The BRSA requires banks to maintain a minimum total capital adequacy ratio of 8.0% (31 December 2018: 8.0%) of risk-weighted assets for regulatory capital. Capital adequacy standard ratio of PASHA Yatirim is calculated in accordance with BRSA. As at 31 December 2019 the bank's capital adequacy ratio was 32.0% (31 December 2018: 37.9%).

30. Events after the reporting period

On 30 January 2020, the World Health Organization (WHO) declared the coronavirus outbreak a "Public Health Emergency of International Concern". Subsequent to yearend there has been increased volatility in the global financial and commodity markets. Currently, Azerbaijani health authorities are taking necessary precautional measures. Management of the Group will further monitor possible effects of the outbreak on the Group's activities.

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