# Aregak Universal Credit Organisation CJSC

Financial Statements and Independent Auditor's Report
For the Year Ended December 31, 2017

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# Aregak Universal Credit Organisation CJSC

## STATEMENT OF MANAGEMENT'S RESPONSIBILITIES FOR THE PREPARATION AND APPROVAL OF THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2017

Management is responsible for the preparation of the financial statements that present fairly the financial position of Aregak Universal Credit Organisation CJSC (the "Company") as of 31 December 2017, and the results of its operations, cash flows and changes in shareholders' equity for the year then ended, in compliance with International Financial Reporting Standards ("IFRS").

In preparing the financial statements, management is responsible for:

- Properly selecting and applying accounting policies;
- Presenting information, including accounting policies, in a manner that provides relevant, reliable, comparable and understandable information;
- Providing additional disclosures when compliance with the specific requirements in IFRSs are insufficient to enable users to understand the impact of particular transactions, other events and conditions on the Company's financial position and financial performance;
- Making an assessment of the Company's ability to continue as a going concern.

Management is also responsible for:

- Designing, implementing and maintaining an effective and sound system of internal controls, throughout the Company;
- Maintaining adequate accounting records that are sufficient to show and explain the Company's transactions and disclose with reasonable accuracy at any time the financial position of the Company, and which enable them to ensure that the financial statements of the Company comply with IFRS;
- Maintaining statutory accounting records in compliance with Republic of Armenia legislation and accounting standards;
- Taking such steps as are reasonably available to them to safeguard the assets of the Company; and
- Preventing and detecting fraud and other irregularities.

The financial statements of the Company for the year ended 31 December 2017 were approved by Board of Directors on March 23, 2018.

On behalf of the Board of Directors:

**Mariam Yesayan**
Executive Director

**Armine Aghajanyan**
Finance Director

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March 23, 2018
Yerevan, Republic of Armenia

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# INDEPENDENT AUDITOR’S REPORT

To the Shareholder of Aregak Universal Credit Organisation CJSC:

## Opinion

We have audited the financial statements of Aregak Universal Credit Organisation CJSC (the “Company”), which comprise the statement of financial position as at 31 December 2017, and the statement of comprehensive income, statement of changes in equity and statement of cash flows for the year then ended, and notes to the financial statements, including a summary of significant accounting policies.

In our opinion, the accompanying financial statements present fairly, in all material respects, the financial position of the Company as at 31 December 2017, and its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards (“IFRSs”).

## Basis for Opinion

We conducted our audit in accordance with International Standards on Auditing (“ISAs”). Our responsibilities under those standards are further described in the *Auditor’s Responsibilities for the Audit of the Financial Statements* section of our report. We are independent of the Company in accordance with the International Ethics Standards Board for Accountants’ *Code of Ethics for Professional Accountants* (the “IESBA Code”) together with the ethical requirements that are relevant to our audit of the financial statements in Republic Armenia, and we have fulfilled our other ethical responsibilities in accordance with these requirements and 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 Those Charged with Governance for the Financial Statements

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

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

Those charged with governance are responsible for overseeing the Company’s financial reporting process.

## Auditor's Responsibilities for the Audit of the Financial Statements

Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISAs will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

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

- Identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company'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 Company's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the Company to cease to continue as a going concern.
- Evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation.

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

**Srbuhi Hakobyan**
Executive Director

**Arpine Ghevondyan**
Audit Director

March 23, 2018
Yerevan, Republic of Armenia

Deloitte Armenia CJSC

# Aregak Universal Credit Organisation CJSC

## Statement of Financial Position as at 31 December 2017
***(in thousands of Armenian Drams)***

| | Notes | 31 December 2017 | 31 December 2016 |
|---|---|---|---|
| **ASSETS** | | | |
| Cash and cash equivalents | 5 | 276,685 | 72,204 |
| Term deposits | 6 | 2,292,052 | 978,561 |
| Loans to customers | 7 | 17,084,456 | 15,710,460 |
| Available-for-sale financial assets | 8 | | |
| - Held by the Company | | 406,783 | 288,087 |
| - Pledged under repurchase agreements | | - | 100,579 |
| Held to maturity investments | 9 | | |
| - Held by the Company | | 368,513 | 677,607 |
| - Pledged under repurchase agreements | | - | 88,746 |
| Property, equipment and intangible assets | 10 | 515,936 | 596,890 |
| Other assets | 11 | 282,372 | 318,426 |
| **TOTAL ASSETS** | | **21,226,797** | **18,831,560** |
| **LIABILITIES** | | | |
| Repurchase agreements | 12 | - | 191,117 |
| Loans and borrowings | 13 | 2,150,776 | 2,189,032 |
| Current income tax liability | | 300,965 | 231,622 |
| Deferred income tax liability | 19 | 162,990 | 194,507 |
| Dividends payable | 14 | 200,282 | 137,767 |
| Other liabilities | | 117,543 | 87,605 |
| **TOTAL LIABILITIES** | | **2,932,556** | **3,031,650** |
| **EQUITY** | | | |
| Share capital | 14 | 3,445,000 | 3,445,000 |
| Additional paid-in capital | | - | 390,660 |
| Available-for-sale fair value reserve | | 23,800 | 17,083 |
| Retained earnings | | 14,825,441 | 11,947,167 |
| **TOTAL EQUITY** | | **18,294,241** | **15,799,910** |
| **TOTAL LIABILITIES AND EQUITY** | | **21,226,797** | **18,831,560** |

**Signed on behalf of the Board of Directors on March 23, 2018.**

**Mariam Yesayan**
Executive Director

**Armine Aghajanyan**
Finance Director

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The notes on pages 8-40 form an integral part of these financial statements.

# Aregak Universal Credit Organisation CJSC

## Statement of Profit or Loss and Other Comprehensive Income for the Year Ended 31 December 2017
***(in thousands of Armenian Drams)***

| | Notes | 2017 | 2016 |
|---|---|---|---|
| Interest income | 15 | 5,022,249 | 4,382,598 |
| Interest expense | 15 | (302,007) | (303,715) |
| **Net interest income** | | **4,720,242** | **4,078,883** |
| Net recovery/(charge) of provision for impairment of loans to customers | 7 | 235,542 | (772,773) |
| **Net interest income after net change in provision for impairment of loans to customers** | | **4,955,784** | **3,306,110** |
| Fee and commission expense | | (6,787) | (11,487) |
| Foreign exchange translation losses | | (8) | (151) |
| Other operating income | 16 | 241,004 | 447,401 |
| Staff costs | 17 | (995,219) | (947,098) |
| Administrative and other operating expenses | 18 | (647,849) | (654,056) |
| **Profit before tax** | | **3,546,925** | **2,140,719** |
| Income tax expense | 19 | (719,029) | (439,310) |
| **PROFIT FOR THE YEAR** | | **2,827,896** | **1,701,409** |
| **Other comprehensive income** | | | |
| Net change in fair value of available-for sale financial assets, net of income tax | | 6,717 | 17,083 |
| **TOTAL COMPREHENSIVE INCOME FOR THE YEAR** | | **2,834,613** | **1,718,492** |

The notes on pages 8-40 form an integral part of these financial statements.

## Statement of Changes in Equity for the Year Ended 31 December 2017
***(in thousands of Armenian Drams)***

| | Notes | Share capital | Additional paid-in capital | Available-for-sale fair value revaluation reserve | Retained earnings | Total |
|---|---|---|---|---|---|---|
| **Balance at 1 January 2016** | | **3,445,000** | **390,660** | - | **10,540,925** | **14,376,585** |
| Profit for the year | | - | - | - | 1,701,409 | **1,701,409** |
| Other comprehensive income | | - | - | 17,083 | - | **17,083** |
| Total comprehensive income for the year | | - | - | 17,083 | 1,701,409 | **1,718,492** |
| Dividends declared | | - | - | - | (295,167) | **(295,167)** |
| **Balance at 31 December 2016** | | **3,445,000** | **390,660** | **17,083** | **11,947,167** | **15,799,910** |
| Profit for the year | | - | - | - | 2,827,896 | **2,827,896** |
| Other comprehensive income | | - | - | 6,717 | - | **6,717** |
| Total comprehensive income for the year | | - | - | 6,717 | 2,827,896 | **2,834,613** |
| Dividends declared | 14 | - | - | - | (340,282) | **(340,282)** |
| Transfer of additional-paid-in-capital reserve to retained earnings | 14 | - | (390,660) | - | 390,660 | **-** |
| **Balance at 31 December 2017** | | **3,445,000** | - | **23,800** | **14,825,441** | **18,294,241** |

The notes on pages 8-40 form an integral part of these financial statements.

## Statement of Cash Flows for the Year Ended 31 December 2017
***(in thousands of Armenian Drams)***

| | Notes | 2017 | 2016 |
|---|---|---|---|
| **Cash flows from operating activities** | | | |
| Interest received | | 4,995,238 | 4,320,563 |
| Interest paid | | (340,380) | (427,676) |
| Fees and commissions paid | | (6,787) | (11,487) |
| Net income received from foreign exchange translations | | (18) | (127) |
| Other operating income received | | 240,590 | 439,352 |
| Other payments | | (38,076) | (35,489) |
| Staff costs paid | | (960,535) | (945,578) |
| Administrative and other operating expenses paid | | (489,858) | (547,662) |
| Income tax paid | | (682,882) | (520,666) |
| **Cash flows from operating activities before changes in operating assets** | | **2,717,292** | **2,271,230** |
| Net increase in loans to customers | | (1,148,506) | (1,241,044) |
| **Net cash from operating activities** | | **1,568,786** | **1,030,186** |
| **Cash flows from investing activities** | | | |
| Purchase of held-to-maturity financial assets | | (148,308) | (744,838) |
| Redemption of held-to-maturity financial assets | | 560,000 | |
| Purchase of available-for-sale financial assets | | - | (344,085) |
| Placement of term deposits | | (1,300,000) | - |
| Acquisition of property, equipment and intangible assets | | (7,421) | (25,133) |
| Proceeds from disposal of property, equipment and intangible assets | | 183 | 7,725 |
| **Net cash used in investing activities** | | **(895,546)** | **(1,106,331)** |
| **Cash flows from financing activities** | | | |
| Proceeds from repurchase agreements | | - | 191,000 |
| Repayment of repurchase agreements | | (191,000) | - |
| Dividends paid | 14 | (277,767) | (343,147) |
| **Net cash used in financing activities** | | **(468,767)** | **(152,147)** |
| **Effect of exchange rate changes on cash and cash equivalents** | | **8** | **29** |
| **Net increase / (decrease) in cash and cash equivalents** | | **204,481** | **(228,292)** |
| Cash and cash equivalents at the beginning of the year | 5 | 72,204 | 300,467 |
| **Cash and cash equivalents at the end of the year** | 5 | **276,685** | **72,204** |

The notes on pages 8-40 form an integral part of these financial statements.

## 1. Introduction

These financial statements have been prepared in accordance with International Financial Reporting Standards for the year ended 31 December 2016 for Aregak Universal Credit Organisation CJSC (the "Company").

The Company was established in the Republic of Armenia (the "RA") as a closed joint stock company in 2006. The Company is wholly-owned by UMCOR Armenia Foundation and ultimately controlled by the United Methodist Committee on Relief of the General Board of Global Ministers of the United Methodist Church (UMCOR). Till 1 December 2015 the Company were wholly-owned and ultimately controlled by the UMCOR. As of 1 December 2015 UMCOR made 100% share transfer, subject to no consideration, to UMCOR Armenia Foundation.

**Principal activity.** The principal activity of the Company is provision of micro and medium loans, individual business and consumer loans in the RA and Nagorno-Karabakh.

The activities of the Company are regulated by the Central Bank of the RA (the "CBA"). The Company has a credit organisation license. The Company has 27 branches and three representative offices from which it conducts business throughout the RA and Nagorno-Karabakh. The majority of the assets and liabilities are located in the RA.

**Registered address and place of business*.*** The registered address of the head office is 4/6 Amiryan Street, 152 office, Yerevan 0010, Republic of Armenia.

## 2. Significant accounting policies

**Statement of compliance.** These financial statements have been prepared in accordance with International Financial Reporting Standards ("IFRS") under the historical cost convention.

**Basis of preparation**. These financial statements have been prepared on the assumption that the Company is a going concern and will continue in operation for the foreseeable future. These financial statements are presented in millions of thousands of Armenian Drams ("AMD thousand"), unless otherwise indicated.

The financial statements have been prepared on the historical cost basis except for certain properties and financial instruments that are measured at revalued amounts or fair values at the end of each reporting period, as explained in the accounting policies below.

Historical cost is generally based on the fair value of the consideration given in exchange for goods and services.

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, regardless of whether that price is directly observable or estimated using another valuation technique. In estimating the fair value of an asset or a liability, the Company takes into account the characteristics of the asset or liability if market participants would take those characteristics into account when pricing the asset or liability at the measurement date. Fair value for measurement and/or disclosure purposes in these financial statements is determined on such a basis, except for share-based payment transactions that are within the scope of IFRS 2, leasing transactions that are within the scope of IAS 17, and measurements that have some similarities to fair value but are not fair value, such as net realisable value in IAS 2 or value in use in IAS 36.

In addition, for financial reporting purposes, fair value measurements are categorised into Level 1, 2 or 3 based on the degree to which the inputs to the fair value measurements are observable and the significance of the inputs to the fair value measurement in its entirety, which are described as follows:

- Level 1 inputs are quoted prices (unadjusted) in active markets for identical assets or liabilities that the entity can access at the measurement date;
- Level 2 inputs are inputs, other than quoted prices included within Level 1, that are observable for the asset or liability, either directly or indirectly; and
- Level 3 inputs are unobservable inputs for the asset or liability.

**Functional currency*.*** The functional currency of Credit organisation is the currency of the primary economic environment in which the entity operates. The functional currency of the Company and the Company's presentation currency is the national currency of the RA, Armenian Dram ("AMD").

In preparing the financial statements of the Company, transactions in currencies other than the Company's functional currency (foreign currencies) are recognized at the rates of exchange prevailing at the dates of the transactions. At the end of each reporting date, monetary items denominated in foreign currencies are retranslated at the rates prevailing at that date. Non-monetary items carried at fair value that are denominated in foreign currencies are retranslated at the rates prevailing at the date when the fair value was determined. Non-monetary items that are measured in terms of historical cost in a foreign currency are not retranslated.

(in thousands of Armenian Drams)

Exchange differences are recognized in the statement of profit or loss and other comprehensive income in the period in which they arise. The relevant exchange rates are as follows:

| | Average Rate | | Spot Rate | |
|---|---|---|---|---|
| | | | 31 December | 31 December |
| | 2017 | 2016 | 2017 | 2016 |
| AMD/1 US Dollar | 482.63 | 480.45 | 484.10 | 483.94 |
| AMD/1 Euro | 546.15 | 531.86 | 580.10 | 512.20 |

**Offsetting.** Financial assets and financial liabilities are offset and the net amount reported in the statement of financial position only when there is a legally enforceable right to offset the recognised amounts and there is an intention to settle on a net basis, or to realise the assets and settle the liability simultaneously. Income and expense is not offset in the statement of profit or loss unless required or permitted by any accounting standard or interpretation, and as specifically disclosed in the accounting policies of the Company.

**Income and expense recognition*.*** Interest income from a financial asset is recognized when it is probable that the economic benefits will flow to the Company and the amount of income can be measured reliably. Interest income and expense are recognized on an accrual basis using the effective interest method. The effective interest method is a method of calculating the amortized cost of a financial asset or a financial liability (or group of financial assets or financial liabilities) and of allocating the interest income or interest expense over the relevant period.

The effective interest rate is the rate that exactly discounts estimated future cash receipts (including all fees on points paid or received that form an integral part of the effective interest rate, transaction costs and other premiums or discounts) through the expected life of the debt instrument, or (where appropriate) a shorter period, to the net carrying amount on initial recognition.

Once a financial asset or a group of similar financial assets has been written down (partly written down) as a result of an impairment loss, interest income is thereafter recognised using the rate of interest used to discount the future cash flows for the purpose of measuring the impairment loss.

Interest earned on assets at fair value is classified within interest income.

Penalty income is recognised based on actual cash basis. Based on management evaluations difference between accrual and cash basis are almost equal.

**Income on repurchase agreements*.*** Gain/loss on the sale of the above instruments is recognized as interest income or expense in the statement of profit or loss based on the difference between the repurchase price accreted to date using the effective interest method and the sale price when such instruments are sold to third parties. When the reverse repo/repo is fulfilled on its original terms, the effective yield/interest between the sales and repurchase price negotiated under the original contract is recognized using the effective interest method.

**Financial instruments.** The Company recognizes financial assets and liabilities in its statement of financial position when it becomes a party to the contractual obligations of the instrument. Regular way purchases and sales of financial assets and liabilities are recognized using settlement date accounting. Regular way purchases or sales are purchases or sales of financial assets that require delivery of assets within the time frame established by regulation or convention in the marketplace.

Financial assets and financial liabilities are initially measured at fair value. Transaction costs that are directly attributable to the acquisition or issue of financial assets and financial liabilities (other than financial assets and financial liabilities at fair value through profit or loss) are added to or deducted from the fair value of the financial assets or financial liabilities, as appropriate, on initial recognition. Transaction costs directly attributable to the acquisition of financial assets or financial liabilities at fair value through profit or loss are recognized immediately in profit or loss.

***Financial assets.*** Financial assets are classified into the following specified categories: financial assets 'at fair value through profit or loss' ("FVTPL"), 'held to maturity' ("HTM") investments, 'available-for-sale' ("AFS") financial assets and 'loans and receivables'. The classification depends on the nature and purpose of the financial assets and is determined at the time of initial recognition.

*Held to maturity investments* are non-derivative financial assets with fixed or determinable payments and fixed maturity dates that the Company has the positive intent and ability to hold to maturity. Held to maturity investments are measured at amortised cost using the effective interest method less any impairment.

If the Company were to sell or reclassify more than an insignificant amount of held to maturity investments before maturity (other than in certain specific circumstances), the entire category would be tainted and would have to be reclassified as available-for-sale. Furthermore, the Company would be prohibited from classifying any financial asset as held to maturity during the current financial year and following two financial years.

*Available-for-sale financial assets* are non-derivatives that are either designated as available-for-sale or are not classified as (a) loans and receivables, (2) held to maturity investments or (c) financial assets at fair value through profit or loss.

Government bonds by the Company that are traded in an active market are classified as AFS and are stated at fair value. Fair value is determined in the manner described (see Note 23). Gains and losses arising from changes in fair value are recognised in other comprehensive income and accumulated in the investments revaluation reserve, with the exception of other-than-temporary impairment losses, interest calculated using the effective interest method, dividend income and foreign exchange gains and losses on monetary assets, which are recognised in profit or loss. Where the investment is disposed of or is determined to be impaired, the cumulative gain or loss previously accumulated in the investments revaluation reserve is reclassified to profit or loss.

*Loans and receivables.* Trade receivables, loans, and other receivables that have fixed or determinable payments that are not quoted in an active market (including balances with the CBA, due from banks, loans to customers and other financial assets) are classified as 'loans and receivables'. Loans and receivables are measured at amortised cost using the effective interest method, less any impairment. Interest income is recognised by applying the effective interest rate, except for short-term receivables when the recognition of interest would be immaterial.

*Staff loans originated at interest rates different from market rates* are re-measured at origination to their fair value, being future interest payments and principal repayment(s) discounted at market interest rates for similar instruments. The difference is deferred as prepaid employee benefits and charged to profit or loss as staff benefits to the periods when the employee services are provided. Amortisation of prepaid employee benefits calculated based on the difference between the actual interest expense and notional market interest expense.

*Securities repurchase, and reverse repurchase agreements and securities lending transactions.* In the normal course of business, the Company enters into financial assets sale and purchase back agreements ("repos") and financial assets purchase and sale back agreements ("reverse repos"). Repos and reverse repos are utilized by the Company as an element of its treasury management.

A repo is an agreement to transfer a financial asset to another party in exchange for cash or other consideration and a concurrent obligation to reacquire the financial assets at a future date for an amount equal to the cash or other consideration exchanged plus interest. These agreements are accounted for as financing transactions. Financial assets sold under repo are retained in the financial statements and consideration received under these agreements is recorded as collateralized deposit received within depositary instruments with banks.

Assets purchased under reverse repos are recorded in the financial statements as cash placed on deposit collateralized by securities and other assets and are classified within due from banks and/or loans to customers.

The Company enters into securities repurchase agreements and securities lending transactions under which it receives or transfers collateral in accordance with normal market practice. Under standard terms for repurchase transactions in the RA and other CIS states, the recipient of collateral has the right to sell or repledge the collateral, subject to returning equivalent securities on settlement of the transaction.

The transfer of securities to counterparties is only reflected on the statement of financial position if the risks and rewards of ownership are also transferred.

*Impairment of financial assets.* Financial assets, other than those at FVTPL, are assessed for indicators of impairment at the end of each reporting period. Financial assets are considered to be impaired when there is objective evidence that, as a result of one or more events that occurred after the initial recognition of the financial asset, the estimated future cash flows of the investment have been affected.

For listed and unlisted equity investments classified as AFS, a significant or prolonged decline in the fair value of the security below its cost is considered to be objective evidence of impairment.

For all other financial assets, objective evidence of impairment could include:

- Significant financial difficulty of the issuer or counterparty; or
- Breach of contract, such as default or delinquency in interest or principal payments;
- Default or delinquency in interest or principal payments; or
- It is becoming probable that the borrower will enter bankruptcy or financial re-organization; or
- Disappearance of an active market for that financial asset because of financial difficulties.

For certain categories of financial asset, such as loans and receivables, assets that are assessed not to be impaired individually are, in addition, assessed for impairment on a collective basis. Objective evidence of impairment for a portfolio of loans and receivables could include the Company's past experience of collecting payments, an increase in the number of delayed payments in the portfolio, as well as observable changes in national or local economic conditions that correlate with default on receivables.

For financial assets carried at amortised cost, the amount of the impairment loss recognised is the difference between the asset's carrying amount and the present value of estimated future cash flows, discounted at the financial asset's original effective interest rate.

For financial assets carried at cost, the amount of the impairment loss is measured as the difference between the asset's carrying amount and the present value of the estimated future cash flows discounted at the current market rate of return for a similar financial asset. Such impairment loss will not be reversed in subsequent periods.

The carrying amount of the financial asset is reduced by the impairment loss directly for all financial assets with the exception of loans and receivables, where the carrying amount is reduced through the use of an allowance account. When a loan or a receivable is considered uncollectible, it is written off against the allowance account. Subsequent recoveries of amounts previously written off are credited against the allowance account. Changes in the carrying amount of the allowance account are recognised in profit or loss.

When an AFS financial asset is considered to be impaired, cumulative gains or losses previously recognised in other comprehensive income are reclassified to profit or loss in the period.

For financial assets measured at amortized cost, if, in a subsequent period, the amount of the impairment loss decreases and the decrease can be related objectively to an event occurring after the impairment was recognized, the previously recognized impairment loss is reversed through profit or loss to the extent that the carrying amount of the investment at the date the impairment is reversed does not exceed what the amortized cost would have been had the impairment not been recognized.

In respect of AFS equity securities, impairment losses previously recognized in profit or loss are not reversed through profit or loss. Any increase in fair value subsequent to an impairment loss is recognized in other comprehensive income and accumulated under the heading of investments revaluation reserve.

In respect of AFS debt securities, impairment losses are subsequently reversed through profit or loss if an increase in the fair value of the investment can be objectively related to an event occurring after the recognition of the impairment loss.

*Renegotiated loans.* Where possible, the Company 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 renegotiated loan will continue to be disclosed as impaired until there is sufficient evidence to demonstrate a significant reduction in the risk of non-payment of future cash flows, and there are no other indicators of impairment. For loans that are assessed for impairment on a collective basis, the evidence typically comprises a history of payment performance against the original or revised terms, as appropriate to the circumstances. For loans that are assessed for impairment on an individual basis, all available evidence is assessed on a case-by-case basis.

A renegotiated loan is presented as impaired and impairment losses are measured when:

- there has been a change in contractual cash flows as a result of a concession which the lender would otherwise not consider, and
- it is probable that without the concession, the borrower would be unable to meet contractual payment obligations in full.

When determining whether a loan that is restructured should be derecognized and a new loan recognized, management consider the extent to which the changes to the original contractual terms result in the renegotiated loan, considered as a whole, being a substantially different financial instrument. Factors that may indicate that the revised loan is a substantially different financial instrument include change in guarantees or loan covenants provided less significant changes to collateral arrangements, the addition of repayment provisions or prepayment premium clauses.

Loans that have been identified as renegotiated retain this designation until maturity or derecognition.

*Write off of loans.* Loans and advances are written off against the allowance for impairment losses when deemed uncollectible. Loans and advances are written off after management has exercised all possibilities available to collect amounts due to the Company and after the Company has sold all available collateral. Subsequent recoveries of amounts previously written off are reflected as an offset to the charge for impairment of financial assets in the statement of profit or loss/ statement of profit or loss and other comprehensive income in the period of recovery.

*Derecognition of financial assets.* The Company derecognizes a financial asset only when the contractual rights to the cash flows from the asset expire, or when it transfers the financial asset and substantially all the risks and rewards of ownership of the asset to another party. If the Company neither transfers nor retains substantially all the risks and rewards of ownership and continues to control the transferred asset, the Company recognizes its retained interest in the asset and an associated liability for amounts it may have to pay. If the Company retains substantially all the risks and rewards of ownership of a transferred financial asset, the Company continues to recognise the financial asset and also recognises a collateralised borrowing for the proceeds received.

On derecognition of a financial asset in its entirety, the difference between the asset's carrying amount and the sum of the consideration received and receivable and the cumulative gain of loss that had been recognized in other comprehensive income and accumulated in equity is recognized in profit or loss.

***Financial liabilities.*** Financial liabilities are classified as either financial liabilities 'at FVTPL' or 'other financial liabilities'.

*Financial liabilities at FVTPL.* Financial liabilities are classified as at FVTPL when the financial liability is (i) contingent consideration that may be paid by an acquirer as part of a business combination to which IFRS 3 applies, (ii) held for trading, or (iii) it is designated as at FVTPL.

A financial liability is classified as held for trading if:

- It has been incurred principally for the purpose of repurchasing it in the near term; or
- On initial recognition it is part of a portfolio of identified financial instruments that the Company manages together and has a recent actual pattern of short-term profit-taking; or
- It is a derivative that is not designated and effective as a hedging instrument.

A financial liability other than a financial liability held for trading or contingent consideration that may be paid by an acquirer as part of a business combination may be designated as at FVTPL upon initial recognition if:

- Such designation eliminates or significantly reduces a measurement or recognition inconsistency that would otherwise arise; or
- The financial liability forms part of a group of financial assets or financial liabilities or both, which is managed, and its performance is evaluated on a fair value basis, in accordance with the Company's documented risk management or investment strategy, and information about the grouping is provided internally on that basis; or
- It forms part of a contract containing one or more embedded derivatives, and IAS 39 *Financial Instruments: Recognition and Measurement* permits the entire combined contract (asset or liability) to be designated as at FVTPL.

Financial liabilities at FVTPL are stated at fair value, with any gains or losses arising on remeasurement recognised in profit or loss. The net gain or loss recognised in profit or loss incorporates any interest paid on the financial liability and is included in the 'interest expenses' line item in the statement of profit or loss and other comprehensive income/statement of profit or loss. Fair value is determined in the manner described (see Note 23).

*Other financial liabilities*. Other financial liabilities (including depository instruments with the CBA, deposits by banks and customers, repurchase agreements, debt securities issued, other borrowed funds, subordinated debt and other financial liabilities) are initially measured at fair value, net of transaction costs.

Other financial liabilities are subsequently measured at amortised cost using the effective interest method, with interest expense recognised on an effective yield basis.

The effective interest method is a method of calculating the amortised cost of a financial liability and of allocating interest expense over the relevant period. The effective interest rate is the rate that exactly discounts estimated future cash payments (including all fees and points paid or received that form an integral part of the effective interest rate, transaction costs and other premiums or discounts) through the expected life of the financial liability, or (where appropriate) a shorter period, to the net carrying amount on initial recognition.

*Derecognition of financial liabilities.* The Company derecognises financial liabilities when, and only when, the Company's obligations are discharged, cancelled or have expired. 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. The difference between the carrying amount of the financial liability derecognized and the consideration paid and payable is recognized in profit and loss.

**The Company as lessee.** Operating lease payments are recognised as an expense on a straight-line basis over the lease term, except where another systematic basis is more representative of the time pattern in which economic benefits from the *l*eased asset are consumed. Contingent rentals arising under operating leases are recognised as an expense in the period in which they are incurred.

**Cash and cash equivalents.** Cash and cash equivalents consist of cash on hand, unrestricted balances on corresponded and term deposits with the CBA with original maturity of less or equal to 90 days and amounts due from credit institutions with original maturity of less or equal to 90 days and are free from contractual encumbrances.

**Term deposits.** Term deposits at banks include deposits held with banks with original maturities of more than three months. Term deposits at banks are carried at amortised cost using the effective interest method.

(in thousands of Armenian Drams)

**Repossessed assets.** In certain circumstances, assets are repossessed following the foreclosure on loans that are in default. Repossessed assets are measured at the lower of carrying amount and fair value less costs to sell.

**Loans to customers.** Loans to customers are recorded when the Company advances money to purchase or originate an unquoted non-derivative receivable from a customer due on fixed or determinable dates and has no intention of trading the receivable. Loans to customers are carried at amortised cost.

**Premises and equipment.** Property and equipment is carried at historical cost less accumulated depreciation and any recognized impairment loss, if any.

Depreciation is charged on the carrying value of property and equipment and is designed to write off assets over their useful economic lives. Depreciation is calculated on a straight-line basis at the following useful lives:

| | Useful lives in years |
|---|---|
| - Buildings | 20 to 30 |
| - leasehold improvements | 20 to 30 |
| - motor vehicles | 5 to 10 |
| - communication devices and computers | 3 to 10 |
| - office equipment | 5 to 10 |
| - computer software | 5 to 10 |
| - other | 5 to 20 |

Leasehold improvements are depreciated over the shorter of the lease term and their useful lives unless it is reasonably certain that the Company will obtain ownership by the end of the lease term or renew the lease term.

An item of property and equipment is derecognized upon disposal or when no future economic benefits are expected to arise from the continued use of the asset. Any gain or loss arising on the disposal or retirement of an item of property and equipment is determined as the difference between the sales proceeds and the carrying amount of the asset and is recognized in profit or loss.

**Intangible assets.** Acquired intangible assets are stated at cost less accumulated amortisation and impairment losses.
Acquired computer software licenses are capitalised on the basis of the costs incurred to acquire and bring to use the specific software.
Amortisation is charged to profit or loss on a straight-line basis over the estimated useful lives of intangible assets. The estimated useful life is up to 10 years.

**Impairment of tangible and intangible assets other than goodwill:** At the end of each reporting period, the Company reviews the carrying amounts of its tangible and intangible assets to determine whether there is any indication that those assets have suffered an impairment loss. If any such indication exists, the recoverable amount of the asset is estimated in order to determine the extent of the impairment loss (if any). Where it is not possible to estimate the recoverable amount of an individual asset, the Company estimates the recoverable amount of the cash-generating unit to which the asset belongs. When a reasonable and consistent basis of allocation can be identified, corporate assets are also allocated to individual cash-generating units, or otherwise they are allocated to the smallest group of cash-generating units for which a reasonable and consistent allocation basis can be identified.

**Loans and borrowings.** Loans and borrowings are carried at amortised cost using the effective interest method.

**Taxation.** Income tax expense represents the sum of the tax currently payable and deferred tax.

*Current tax.* The tax currently payable is based on taxable profit for the year. Taxable profit before tax as reported in the statement of profit or loss and other comprehensive income because of items of income or expense that are taxable or deductible in other years and items that are never taxable or deductible. The Company's current tax is calculated using tax rates that have been enacted or substantively enacted by the end of the reporting period.

*Deferred tax.* Deferred tax is recognised on temporary differences between the carrying amounts of assets and liabilities in the financial statements and the corresponding tax bases used in the computation of taxable profit. Deferred tax liabilities are generally recognised for all taxable temporary differences. Deferred tax assets are generally recognised for all deductible temporary differences to the extent that it is probable that taxable profits will be available against which those deductible temporary differences can be utilised. Such deferred tax assets and liabilities are not recognised if the temporary difference arises from the initial recognition (other than in a business combination) of assets and liabilities in a transaction that affects neither the taxable profit nor the accounting profit. In addition, deferred tax liabilities are not recognised if the temporary difference arises from the initial recognition of goodwill.

Deferred tax liabilities are recognised for taxable temporary differences associated with investments in subsidiaries and associates, and interests in joint ventures, except where the Company is able to control the reversal of the temporary difference and it is probable that the temporary difference will not reverse in the foreseeable future. Deferred tax assets arising from deductible temporary differences associated with such investments and interests are only recognised to the extent that it is probable that there will be sufficient taxable profits against which to utilise the benefits of the temporary differences and they are expected to reverse in the foreseeable future.

The carrying amount of deferred tax assets is reviewed at the end of each reporting period and reduced to the extent that it is no longer probable that sufficient taxable profits will be available to allow all or part of the asset to be recovered.

Deferred tax liabilities and assets are measured at the tax rates that are expected to apply in the period in which the liability is settled or the asset realised, based on tax rates (and tax laws) that have been enacted or substantively enacted by the end of the reporting period.

The measurement of deferred tax liabilities and assets reflects the tax consequences that would follow from the manner in which the Company expects, at the end of the reporting period, to recover or settle the carrying amount of its assets and liabilities.

*Current and deferred tax for the year.* 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.

**Provisions for liabilities and charges.** Provisions are recognised when the Company has a present obligation (legal or constructive) as a result of a past event, it is probable that the Company will be required to settle the obligation, and a reliable estimate can be made of the amount of the obligation.

The amount recognised as a provision is the best estimate of the consideration required to settle the present obligation at the end of the reporting period, taking into account the risks and uncertainties surrounding the obligation. When a provision is measured using the cash flows estimated to settle the present obligation, its carrying amount is the present value of those cash flows (when the effect of the time value of money is material).

When some or all of the economic benefits required to settle a provision are expected to be recovered from a third party, a receivable is recognised as an asset if it is virtually certain that reimbursement will be received and the amount of the receivable can be measured reliably.

**Share capital.** Ordinary shares are classified as equity. Incremental costs directly attributable to the issue of ordinary shares and share options are recognised as a deduction from equity, net of any tax effects.

**Dividends.** The ability of the Company to declare and pay dividends is subject to the rules and regulations of the Armenian legislation. Dividends in relation to ordinary shares are reflected as an appropriation of retained earnings in the period when they are declared.

**Collateral.** The Company obtains collateral in respect of customer liabilities where this is considered appropriate. The collateral normally takes the form of a lien over the customer's assets and gives the Company a claim on these assets for both existing and future customer liabilities.

## 3. Critical Accounting Estimates, and Judgements in Applying Accounting Policies

In the application of the Company's accounting policies the Company management is required to make judgements, estimates and assumptions about the carrying amounts of assets and liabilities that are not readily apparent from other sources. The estimates and associated assumptions are based on historical experience and other factors that are considered to be relevant. Actual results may differ from these estimates.

The estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the period in which the estimate is revised if the revision affects only that period, or in the period of the revision and future periods if the revision affects both current and future periods.

**Critical judgements in applying accounting policies.** The following are the critical judgements, apart from those involving estimations (see below), that the Company management has made in the process of applying the Company's accounting policies and that have the most significant effect on the amounts recognised in the financial statements.

**Held to maturity financial assets.** The Company management has reviewed the Company's held to maturity financial assets in the light of its capital maintenance and liquidity requirements and has confirmed the Company's positive intention and ability to hold those assets to maturity. The carrying amount of the held to maturity financial assets is AMD 368,513 thousand. Details of these assets are set out (see Note 9).

**Key sources of estimation uncertainty.** The following are the key assumptions concerning the future, and other key sources of estimation uncertainty at the end of the reporting period, that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year.

**Valuation of financial instruments.** As described (see Note 23), the Company uses valuation techniques that include inputs that are not based on observable market date to estimate the fair value of certain types of financial instruments. In Note 23 provides detailed information about the key assumptions used in the determination of the fair value of financial instruments, as well as the detailed sensitivity analysis for these assumptions. The Company management believes that the chosen valuation techniques and assumptions used are appropriate in determining the fair value of financial instruments.

**Impairment losses on loans and advances.** The Company regularly reviews its loans and receivables to assess for impairment. The Company's loan impairment provisions are established to recognize incurred impairment losses in its portfolio of loans and receivables. The Company considers accounting estimates related to allowance for impairment of loans and receivables a key source of estimation uncertainty because (i) they are highly susceptible to change from period to period as the assumptions about future default rates and valuation of potential losses relating to impaired loans and receivables are based on recent performance experience, and (ii) any significant difference between the Company's estimated losses and actual losses would require the Company to record provisions which could have a material impact on its financial statements in future periods.

The Company uses a combination of objective and collective assessment in determining the allowance for impairment required at any reporting date. The Company does not have individually significant loans.

Objective evidence that financial assets are impaired can include default or delinquency by a borrower, breach of loan covenants or conditions, restructuring of a loan or advance on terms that the Company would not otherwise consider, indications that a borrower or issuer will enter bankruptcy, deterioration in the value of collateral, or other observable data relating to a Company of assets such as adverse changes in the payment status of borrowers in the Company, or economic conditions that correlate with defaults in the Company.

If the Company determines that no objective evidence of impairment exists for an individually assessed loan or receivable, whether significant or not, it includes the loan in a Company of loans and receivables with similar credit risk characteristics and collectively assesses them for impairment. Loans and receivables that are individually assessed for impairment and for which an impairment loss is or continues to be recognised are not included in a collective assessment of impairment.

The collectively assessed loans and receivables are grouped based on similar credit risk characteristics and their past due status and assessed accordingly. The Company estimates changes in future cash flows based on past performance, past customer behaviour, observable data indicating an adverse changes in the payment status of borrowers in the group, and economic conditions that correlate with defaults on assets in the Company. Management uses estimates based on historical loss experience for assets with credit risk characteristics and objective evidence of impairment similar to those in the group of loans.

The allowances for impairment of financial assets in the financial statements have been determined on the basis of existing economic and political conditions. The Company is not in a position to predict what changes in conditions will take place in the Republic of Armenia and what effect such changes might have on the adequacy of the allowances for impairment of financial assets in future periods.

As at 31 December 2017 and 2016 the gross loans and receivables totalled AMD 17,507,719 thousand and AMD 16,437,355 thousand, respectively, and allowance for impairment losses amounted to AMD 423,263 thousand and AMD 726,895 thousand, respectively.

Changes in these estimates could affect the loan impairment provision. For example, to the extent that the net present value of the estimated cash flows differs by one percent, the loan impairment allowance on business loans and individual loans as of 31 December 2017 would be AMD 8,382 and AMD 162,463 thousand lower/higher (31 December 2016: AMD 8,237 and AMD 148,867 thousand lower/higher).

**Useful lives of property, equipment and intangible assets:** Items of property and equipment are stated at cost less accumulated depreciation and less any accumulated depreciation losses. The Company reviews the estimated useful lives of property and equipment at the end of each annual reporting period. The estimation of the useful life of an item of property and equipment is a matter of management judgment based upon experience with similar assets. In determining the useful life of an asset, management considers the expected usage, estimated technical obsolescence, physical wear and tear and the physical environment in which the asset is operated. Changes in any one of these conditions or estimates may result in adjustments to future depreciation rates.

## 4. Adoption of New or Revised Standards and Interpretations

### Amendments to IFRSs affecting amounts reported in the financial statements

In the current year, the following new and revised Standards and Interpretations have been adopted and have affected the amounts reported in these consolidated financial statements:

**Amendments to IAS 7 *Disclosure Initiative***

The Company has applied these amendments for the first time in the current year. The amendments require an entity to provide disclosures that enable users of financial statements to evaluate changes in liabilities arising from financing activities, including both cash and non-cash changes.

The Company's liabilities arising from financing activities consist of loans and borrowings (Note 13). A reconciliation between the opening and closing balances of these items is provided in Note 13. Consistent with the transition provisions of the amendments, the Company has not disclosed comparative information for the prior period. Apart from the additional disclosure in Note 13, the application of these amendments has had no impact on the Company's financial statements.

### New and revised IFRSs in issue but not yet effective

The Company has not applied the following new and revised IFRSs that have been issued but are not yet effective:

IFRS 9 *Financial Instruments*[1];

IFRS 15 *Revenue from Contracts with Customers (and the related Clarifications)*[1];

IFRS 16 Leases[2];

IFRIC 22 *Foreign Currency Transactions and Advance Consideration*[1];

[1] Effective for annual periods beginning on or after 1 January 2018, with earlier application permitted.
[2] Effective for annual periods beginning on or after 1 January 2019, with earlier application permitted.

**IFRS 9 *Financial Instruments***

IFRS 9 issued in November 2009 introduced new requirements for the classification and measurement of financial assets. IFRS 9 was subsequently amended in October 2010 to include requirements for the classification and measurement of financial liabilities and for derecognition, and in November 2013 to include the new requirements for general hedge accounting. Another revised version of IFRS 9 was issued in July 2014 mainly to include a) impairment requirements for financial assets and b) limited amendments to the classification and measurement requirements by introducing a 'fair value through other comprehensive income' (FVTOCI) measurement category for certain simple debt instruments.

The key requirements of IFRS 9 are:

- **Classification and measurement of financial assets**. All recognised financial assets that are within the scope of IFRS 9 are required to be subsequently measured at amortised cost or fair value. Specifically, debt investments that are held within a business model whose objective is to collect the contractual cash flows, and that have contractual cash flows that are solely payments of principal and interest on the principal outstanding are generally measured at amortised cost at the end of subsequent accounting periods. Debt instruments that are held within a business model whose objective is achieved both by collecting contractual cash flows and selling financial assets, and that have contractual terms that give rise on specified dates to cash flows that are solely payments of principal and interest on the principal amount outstanding, are generally measured at FVTOCI. All other debt investments and equity investments are measured at their fair value at the end of subsequent accounting periods. In addition, under IFRS 9, entities may make an irrevocable election to present subsequent changes in the fair value of an equity investment (that is not held for trading nor contingent consideration recognised by an acquirer in a business combination) in other comprehensive income, with only dividend income generally recognised in profit or loss.

- **Classification and measurement of financial liabilities.** With regard to the measurement of financial liabilities designated as at fair value through profit or loss, IFRS 9 requires that the amount of change in the fair value of a financial liability that is attributable to changes in the credit risk of that liability is presented in other comprehensive income, unless the recognition of such changes in other comprehensive income would create or enlarge an accounting mismatch in profit or loss. Changes in fair value attributable to a financial liability's credit risk are not subsequently reclassified to profit or loss. Under IAS 39, the entire amount of the change in the fair value of the financial liability designated as fair value through profit or loss is presented in profit or loss.

- **Impairment.** In relation to the impairment of financial assets, IFRS 9 requires an expected credit loss model, as opposed to an incurred credit loss model under IAS 39. The expected credit loss model requires an entity to account for expected credit losses and changes in those expected credit losses at each reporting date to reflect changes in credit risk since initial recognition. In other words, it is no longer necessary for a credit event to have occurred before credit losses are recognised.

- **Hedge accounting.** The new general hedge accounting requirements retain the three types of hedge accounting mechanisms currently available in IAS 39. Under IFRS 9, greater flexibility has been introduced to the types of transactions eligible for hedge accounting, specifically broadening the types of instruments that qualify for hedging instruments and the types of risk components of non-financial items that are eligible for hedge accounting. In addition, the effectiveness test has been overhauled and replaced with the principle of an 'economic relationship'. Retrospective assessment of hedge effectiveness is also no longer required. Enhanced disclosure requirements about an entity's risk management activities have also been introduced.

Based on an analysis of the Company's financial assets and financial liabilities as at 31 December 2017 on the basis of the facts and circumstances that exist at that date, the management of the Company has assessed the impact of IFRS 9 to the Company's financial statements as follows:

*Classification and measurement*

- Government treasury bonds classified as held-to-maturity investments and loans carried at amortised cost as disclosed in Notes 9 and 7 respectively: these are held within a business model whose objective is to collect the contractual cash flows that are solely payments of principal and interest on the principal outstanding. Accordingly, these financial assets will continue to be subsequently measured at amortised cost upon the application of IFRS 9;
- Government treasury bonds classified as available-for-sale investments carried at fair value as disclosed in Note 8: these are held within a business model whose objective is to collect the contractual cash flows that are solely payments of principal and interest on the principal outstanding. Accordingly, the bonds will be subsequently measured at amortised cost upon the application of IFRS 9, and the fair value gains or losses accumulated in the investment revaluation reserve will subsequently reclassified to profit or loss;
- All other financial assets and financial liabilities will continue to be measured on the same bases as is currently adopted under IAS 39.

*Impairment*

Financial assets measured at amortised cost, (see classification and measurement section above), amounts due from customers will be subject to the impairment provisions of IFRS 9. In general, the management anticipates that the application of the expected credit loss model of IFRS 9 will result in earlier recognition of credit losses for the respective items and will increase the amount of loss allowance recognised for these items.

The Company expects to apply the simplified approach to recognise lifetime expected credit losses for its trade receivables, as required or permitted by IFRS 9. The management has not concluded on the possible effects of the application of impairment under IFRS 9 on its loan to customers portfolio and expects the effects may be material to the financial statements.

**IFRS 15 *Revenue from Contracts with Customers***

IFRS 15 establishes a single comprehensive model for entities to use in accounting for revenue arising from contracts with customers. IFRS 15 will supersede the current revenue recognition guidance including IAS 18 *Revenue*, IAS 11 *Construction Contracts* and the related Interpretations when it becomes effective.

The core principle of IFRS 15 is that an entity should recognise revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. Specifically, the Standard introduces a 5-step approach to revenue recognition:

- Identify the contract with the customer;
- Identify the performance obligations in the contract;
- Determine the transaction price;
- Allocate the transaction price to the performance obligations in the contracts;
- Recognise revenue when (or as) the entity satisfies a performance obligation.

Under IFRS 15, an entity recognises revenue when or as a performance obligation is satisfied, i.e. when 'control' of the goods or services underlying the particular performance obligation is transferred to the customer. Far more prescriptive guidance has been added in IFRS 15 to deal with specific scenarios. Furthermore, extensive disclosures are required by IFRS 15.

In April 2016, the IASB issued *Clarifications to IFRS 15* in relation to the identification of performance obligations, principal versus agent considerations, as well as licensing application guidance.

The Company recognises revenue from the following major sources:

- Interest income from loans to customers, including penalty income
- Interest income from term deposits
- Interest income from government bonds

The management of the Company has assessed the main revenue streams and has assessed that the performance obligations are satisfied over time and that the method currently used to recognize revenue will continue to be appropriate under IFRS 15.

**IFRS 16 *Leases***

IFRS 16 introduces a comprehensive model for the identification of lease arrangements and accounting treatments for both lessors and lessees. IFRS 16 will supersede the current lease guidance including IAS 17 Leases and the related interpretations when it becomes effective.

IFRS 16 distinguishes leases and service contracts on the basis of whether an identified asset is controlled by a customer. Distinctions of operating leases (off balance sheet) and finance leases (on balance sheet) are removed for lessee accounting and is replaced by a model where a right-of-use asset and a corresponding liability have to be recognised for all leases by lessees (i.e. all on balance sheet) except for short-term leases and leases of low value assets.

The right-of-use asset is initially measured at cost and subsequently measured at cost (subject to certain exceptions) less accumulated depreciation and impairment losses, adjusted for any remeasurement of the lease liability. The lease liability is initially measured at the present value of the lease payments that are not paid at that date. Subsequently, the lease liability is adjusted for interest and lease payments, as well as the impact of lease modifications, amongst others. Furthermore, the classification of cash flows will also be affected as operating lease payments under IAS 17 are presented as operating cash flows; whereas under the IFRS 16 model, the lease payments will be split into a principal and an interest portion which will be presented as financing and operating cash flows respectively.

In contrast to lessee accounting, IFRS 16 substantially carries forward the lessor accounting requirements in IAS 17, and continues to require a lessor to classify a lease either as an operating lease or a finance lease.

Furthermore, extensive disclosures are required by IFRS 16.

As at 31 December 2017, the Company has non-cancellable operating lease commitments of AMD 250,904 thousand. IAS 17 does not require the recognition of any right-of-use asset or liability for future payments for these leases; instead, certain information is disclosed as operating lease commitments in Note 22. A preliminary assessment indicates that these arrangements will meet the definition of a lease under IFRS 16, and hence the Company will recognise a right-of-use asset and a corresponding liability in respect of all these leases unless they qualify for low value or short-term leases upon the application of IFRS 16. The new requirement to recognise a right-of-use asset and a related lease liability is expected to have a significant impact on the amounts recognised in the Company's financial statements and the management is currently assessing its potential impact. It is not practicable to provide a reasonable estimate of the financial effect until the management completes the review.

**IFRIC 22 *Foreign Currency Transactions and Advance Consideration***

IFRIC 22 addresses how to determine the 'date of transaction' for the purpose of determining the exchange rate to use on initial recognition of an asset, expense or income, when consideration for that item has been paid or received in advance in a foreign currency which resulted in the recognition of a non-monetary asset or non-monetary liability (e.g. a non-refundable deposit or deferred revenue).

The Interpretation specifies that the date of transaction is the date on which the entity initially recognises the non-monetary asset or non-monetary liability arising from the payment or receipt of advance consideration. If there are multiple payments or receipts in advance, the Interpretation requires an entity to determine the date of transaction for each payment or receipt of advance consideration.

The Interpretation is effective for annual periods beginning on or after 1 January 2018 with earlier application permitted. Entities can apply the Interpretation either retrospectively or prospectively. Specific transition provisions apply to prospective application.

The management of the Company does not anticipate that the application of this IFRIC will have a material impact on the Company's financial statements as the Company currently uses the approach prescribed in IFRIC 22.

(in thousands of Armenian Drams)

## 5. Cash and Cash Equivalents

For the purposes of the statement of cash flows, cash and cash equivalents include cash on hand and in banks, net of outstanding bank overdrafts, if any. Cash and cash equivalents at the end of the reporting period as shown in the statement of cash flows can be reconciled to the related items in the statement of financial position as follows:

| | 31 December 2017 | 31 December 2016 |
|---|---|---|
| Cash on hand | 11,983 | 4,239 |
| Bank balances payable on demand | 114,603 | 67,965 |
| Placements with banks with original maturities of less than three months | 150,099 | - |
| **Total cash and cash equivalents** | **276,685** | **72,204** |

All cash and cash equivalents are classified as current and not impaired (31 December 2016: current and not impaired).

The information on interest rates is presented in Note 0.

## 6. Term Deposits

| | 31 December 2017 | 31 December 2016 |
|---|---|---|
| Placements with banks with original maturities of more than three months | | |
| – Largest 10 Armenian banks | 1,041,997 | 978,561 |
| – Other Armenian banks | 1,250,055 | - |
| **Total Term Deposits** | **2,292,052** | **978,561** |

All term deposits are classified as current and not impaired (31 December 2016: current and not impaired).

The information on interest rates and maturities is presented in Note 0.

## 7. Loans to Customers

| | 31 December 2017 | 31 December 2016 |
|---|---|---|
| **Business loans** | | |
| Loans to small companies and sole entrepreneurs | 870,578 | 896,772 |
| **Loans to individuals** | | |
| Micro and medium loans | 13,672,207 | 12,997,624 |
| Consumer and staff loans | 2,964,934 | 2,542,959 |
| Less: Provision for loan impairment | (423,263) | (726,895) |
| **Total loans to customers** | **17,084,456** | **15,710,460** |

Movements in the provision for loan impairment during 2017 are as follows:

| | Business loans | Loans to individuals | Total |
|---|---|---|---|
| **Provision for loan impairment at 1 January 2017** | **73,059** | **653,836** | **726,895** |
| Net recovery of provision for impairment of loans to customers | (83,110) | (152,432) | (235,542) |
| Recovery of amounts previously written-off as uncollectible | 73,535 | 430,542 | 504,077 |
| Amounts written-off as uncollectible | (31,090) | (541,077) | (572,167) |
| **Provision for loan impairment at 31 December 2017** | **32,394** | **390,869** | **423,263** |

Movements in the provision for loan impairment during 2016 are as follows:

(in thousands of Armenian Drams)

| | Business loans | Loans to individuals | Total |
|---|---|---|---|
| **Provision for loan impairment at 1 January 2016** | **65,616** | **644,756** | **710,372** |
| Net charge of provision for impairment of loans to customers | 74,695 | 698,078 | 772,773 |
| Recovery of amounts previously written-off as uncollectible | 31,158 | 216,365 | 247,523 |
| Amounts written-off as uncollectible | (98,410) | (905,363) | (1,003,773) |
| **Provision for loan impairment at 31 December 2016** | **73,059** | **653,836** | **726,895** |

Loans overdue for more than 270 days are classified as impaired and written off from portfolio.

Loans to customers were issued primarily to customers located within the RA who operate in the following economic sectors:

| | 31 December 2017 | | 31 December 2016 | |
|---|---|---|---|---|
| | Amount | % | Amount | % |
| Agriculture | 10,727,612 | 61 | 10,694,527 | 65 |
| Trade | 3,131,369 | 18 | 2,610,692 | 16 |
| Consumer and staff loans | 2,964,934 | 17 | 2,542,959 | 15 |
| Food industry | 123,063 | 1 | 120,979 | 1 |
| Light industry | 73,607 | 0 | 75,677 | 1 |
| Other | 487,134 | 3 | 392,521 | 2 |
| **Total loans to customers (before impairment)** | **17,507,719** | **100** | **16,437,355** | **100** |

Information about exposure to credit risk and collateral held at 31 December 2017 is as follows:

| | Business loans | Loans to individuals | Total |
|---|---|---|---|
| Loans guaranteed by other parties | 774,537 | 16,036,466 | 16,811,003 |
| Loans collateralized by residential property | 24,719 | - | 24,719 |
| No collateral or other credit enhancement | 71,322 | 600,675 | 671,997 |
| **Total loans to customers** | **870,578** | **16,637,141** | **17,507,719** |

Information about exposure to credit risk and collateral held at 31 December 2016 is as follows:

| | Business loans | Loans to individuals | Total |
|---|---|---|---|
| Loans guaranteed by other parties | 867,230 | 14,908,705 | 15,775,935 |
| Loans collateralized by residential property | 29,542 | - | 29,542 |
| No collateral or other credit enhancement | - | 631,878 | 631,878 |
| **Total loans to customers** | **896,772** | **15,540,583** | **16,437,355** |

Staff loans in the amount AMD 542,118 thousand are included in loans to individuals (2016: AMD 604,129 thousand).

The above disclosure represents the lower of the carrying value of the loan or collateral taken. The carrying value of loans was allocated based on liquidity of the assets taken as collateral. Micro and medium loans are secured by individual guarantees given by the members of a group of borrowers formed for the purpose of obtaining loans from the Company. The maturity of the loan portfolio is presented in Note 0, which shows the remaining period from the reporting date to the contractual maturity of the loans.

During the year ended 31 December 2017 and 2016, the Company did not obtain any assets by taking possession of collateral for loans to customers.

(in thousands of Armenian Drams)

For loans that are neither past due nor impaired, the fair value of collateral was estimated at the inception of the loans and was not adjusted for subsequent changes to the reporting date. The recoverability of these loans is primarily dependent on the creditworthiness of the borrowers rather than the value of collateral, and the Company does not necessarily update the valuation of collateral as at each reporting date.

Analysis by credit quality of loans outstanding at 31 December 2017 is as follows:

| | Gross loans | Provision for impairment | Net loans | Provision for impairment to gross loans |
|---|---|---|---|---|
| **Business loans** | | | | |
| *Neither past due nor impaired* | | | | |
| - up to AMD 10,000 thousand per borrower | 848,570 | 14,835 | 833,735 | 1.75% |
| - above AMD 10,000 thousand per borrower | - | - | - | - |
| **Total neither past due nor impaired** | **848,570** | **14,835** | **833,735** | **1.75%** |
| *Past due but not impaired* | | | | |
| - less than 30 days overdue | 3,497 | 1,207 | 2,290 | 34.52% |
| - 30 to 90 days overdue | 2,636 | 1,499 | 1,137 | 56.87% |
| - 91 to 180 days overdue | 4,115 | 3,226 | 889 | 78.40% |
| - 181 to 360 days overdue | 11,760 | 11,628 | 132 | 98.88% |
| **Total past due but not impaired** | **22,008** | **17,560** | **4,448** | **79.79%** |
| **Total business loans** | **870,578** | **32,395** | **838,183** | **3.72%** |
| **Individual loans** | | | | |
| *Neither past due nor impaired* | | | | |
| - up to AMD 10,000 thousand per borrower | 16,164,394 | 121,547 | 16,042,848 | 0.75% |
| - above AMD 10,000 thousand per borrower | 92,334 | 360 | 91,974 | 0.39% |
| **Total neither past due nor impaired** | **16,256,728** | **121,907** | **16,134,822** | **0.75%** |
| *Past due but not impaired* | | | | |
| - less than 30 days overdue | 83,443 | 24,668 | 58,775 | 29.56% |
| - 30 to 90 days overdue | 81,410 | 49,012 | 32,397 | 60.20% |
| - 91 to 180 days overdue | 101,169 | 83,379 | 17,790 | 82.42% |
| - 181 to 360 days overdue | 114,391 | 111,902 | 2,489 | 97.82% |
| **Total past due but not impaired** | **380,413** | **268,961** | **111,451** | **70.70%** |
| **Total individual loans** | **16,637,141** | **390,868** | **16,246,273** | **2.35%** |
| **Total loans** | **17,507,719** | **423,263** | **17,084,456** | **2.42%** |

Analysis by credit quality of loans outstanding at 31 December 2016 is as follows:

(in thousands of Armenian Drams)

| | Gross loans | Provision for impairment | Net loans | Provision for impairment to gross loans |
|---|---|---|---|---|
| **Business loans** | | | | |
| *Neither past due nor impaired* | | | | |
| - up to AMD 10,000 thousand per borrower | 829,013 | 15,858 | 813,155 | 1.91% |
| - above AMD 10,000 thousand per borrower | - | - | - | - |
| **Total neither past due nor impaired** | **829,013** | **15,858** | **813,155** | **1.91%** |
| *Past due but not impaired* | | | | |
| - less than 30 days overdue | 6,552 | 2,568 | 3,984 | 39.19% |
| - 30 to 90 days overdue | 13,145 | 8,675 | 4,470 | 65.99% |
| - 91 to 180 days overdue | 18,444 | 16,846 | 1,598 | 91.34% |
| - 181 to 360 days overdue | 29,618 | 29,112 | 506 | 98.29% |
| **Total past due but not impaired** | **67,759** | **57,201** | **10,558** | **84.42%** |
| **Total business loans** | **896,772** | **73,059** | **823,713** | **8.15%** |
| **Individual loans** | | | | |
| *Neither past due nor impaired* | | | | |
| - up to AMD 10,000 thousand per borrower | 14,755,185 | 111,590 | 14,643,595 | 0.76% |
| - above AMD 10,000 thousand per borrower | 81,140 | 308 | 80,832 | 0.38% |
| **Total neither past due nor impaired** | **14,836,325** | **111,898** | **14,724,427** | **0.75%** |
| *Past due but not impaired* | | | | |
| - less than 30 days overdue | 120,593 | 41,456 | 79,137 | 34.38% |
| - 30 to 90 days overdue | 135,468 | 85,172 | 50,296 | 62.87% |
| - 91 to 180 days overdue | 172,642 | 146,654 | 25,988 | 84.95% |
| - 181 to 360 days overdue | 275,555 | 268,656 | 6,899 | 97.50% |
| **Total past due but not impaired** | **704,258** | **541,938** | **162,320** | **76.95%** |
| **Total individual loans** | **15,540,583** | **653,836** | **14,886,747** | **4.21%** |
| **Total loans** | **16,437,355** | **726,895** | **15,710,460** | **4.42%** |

In disclosures above, impaired loans are not included as loans for more than 270 days are classified as impaired and written off from portfolio.

The Company applied the portfolio provisioning methodology prescribed by IAS 39, *Financial Instruments: Recognition and Measurement*, and created portfolio provisions for impairment losses that were incurred but have not been specifically identified with any individual loan by the end of the reporting period. The Company's policy is to classify each loan as 'neither past due nor impaired' until specific objective evidence of impairment of the loan is identified. The impairment provisions may exceed the total gross amount of individually impaired loans as a result of this policy and the portfolio impairment methodology. The primary factors that the Company considers in determining whether a loan is impaired are its overdue status and realizability of related collateral, if any.

Post-crisis the Company has experienced an objective improvement in the credit quality of its loan portfolio. The improvement of the credit quality of the portfolio is driven, among other factors, by the improvements in payment pattern and collections, observed decrease in the number of delayed payments in the portfolio. The recent years have shown continued improvements in the reported national economic conditions, which have positively effected the default rates in the loan portfolio. The post-crisis improved external conditions supplemented by the strengthened collection rates have resulted in the decrease of the provision for incurred losses as at reporting date. In particular, the macro-economic conditions have positively affected the performance of the non-overdue and less than 30 days overdue loans.

(in thousands of Armenian Drams)

## 8. Available-for-sale financial assets

As at December 31, 2017 available-for-sale financial assets of AMD 406,783 thousand were comprised of Government securities of the Republic of Armenia (December 31, 2016: AMD 388,666 thousand). As at December 31, 2017 none of these assets (December 31, 2016: AMD 100,579 thousand) were pledged against Company's liabilities (2016: AMD 100,579 thousand under repurchase agreements, see Note 12). Government debt securities bear fixed coupon interest rates between 8 to 10 % p.a. (2016: between 8 to 10 % p.a.) and expire between 2019 to 2021 (2016: between 2019 to 2021). The fair value of these instruments is measured using valuation techniques applying current market rates to discounted future cash flows. None of the available for sale assets are past due nor impaired.

## 9. Held to maturity investments

As at December 31, 2017 held for maturity investments of AMD 368,513 thousand were comprised of Government securities of the Republic of Armenia (December 31, 2016: AMD 766,353 thousand). As at December 31, 2017 none of these assets (December 31, 2016: AMD 88,746 thousand) were pledged against Company's liabilities (2016: AMD 88,746 thousand pledged under repurchase agreements, see Note 12). Government debt securities bear fixed coupon interest rates at 9% p.a. (2016: 9% p.a.) and expire between 2018 to 2019 (2016: between 2017 to 2019). None of the held for maturity investments are past due nor impaired.

## 10. Property, equipment and intangible assets

| | **Buildings** | **Motor vehicles** | **Communi-cation devices and computers** | **Office equipment** | **Computer software** | **Other** | **Total** |
|---|---|---|---|---|---|---|---|
| ***Cost*** | | | | | | | |
| At 1 January 2016 | 487,049 | 150,470 | 233,814 | 84,161 | 103,214 | 54,709 | 1,113,417 |
| Additions | - | - | 4,204 | 3,983 | 5,690 | 11,255 | 25,132 |
| Disposals | - | (35,507) | (1,113) | (515) | - | (949) | (38,084) |
| Transfer | - | - | (70) | (10,614) | - | 10,684 | - |
| **At 31 December 2016** | **487,049** | **114,963** | **236,835** | **77,015** | **108,904** | **75,699** | **1,100,465** |
| Additions | - | - | 3,252 | 1,439 | 1,247 | 1,483 | 7,421 |
| Disposals | - | - | (1,003) | (604) | - | (780) | (2,387) |
| **At 31 December 2017** | **487,049** | **114,963** | **239,084** | **77,850** | **110,151** | **76,402** | **1,105,499** |
| ***Depreciation and amortization*** | | | | | | | |

| | | | | | | | |
|---|---|---|---|---|---|---|---|
| At 1 January 2016 | (110,425) | (61,920) | (131,402) | (57,571) | (64,807) | (15,223) | (441,348) |
| Depreciation and amortizations | (23,370) | (15,280) | (28,121) | (6,387) | (20,014) | (6,278) | (99,450) |
| Disposals | - | 34,646 | 1,113 | 515 | - | 949 | 37,223 |
| Transfer | - | - | - | 6,538 | - | (6,538) | - |
| **At 31 December 2016** | **(133,795)** | **(42,554)** | **(158,410)** | **(56,905)** | **(84,821)** | **(27,090)** | **(503,575)** |
| Depreciation and amortizations | (23,369) | (15,023) | (21,202) | (4,977) | (15,986) | (7,818) | (88,375) |
| Disposals | - | - | 1,003 | 604 | - | 780 | 2,387 |
| **At 31 December 2017** | **(157,164)** | **(57,577)** | **(178,609)** | **(61,278)** | **(100,807)** | **(34,128)** | **(589,563)** |
| ***Carrying amount:*** | | | | | | | |
| **At 31 December 2017** | **329,885** | **57,386** | **60,475** | **16,572** | **9,344** | **42,274** | **515,936** |
| **At 31 December 2016** | **353,254** | **72,409** | **78,425** | **20,110** | **24,083** | **48,609** | **596,890** |
| **At 1 January 2016** | **376,624** | **88,550** | **102,412** | **26,590** | **38,407** | **39,486** | **672,069** |

As of 31 December 2017 included in property, equipment and intangible assets are fully depreciated assets totalling AMD 176,192 thousand (2016: AMD 107,801 thousand).

## 11. Other assets

| | 31 December 2017 | 31 December 2016 |
|---|---|---|
| **Other financial assets** | | |
| Receivables | 15,523 | 4,554 |
| **Other non-financial assets** | | |
| Expenses of future periods | 229,968 | 283,056 |
| Prepayments | 23,632 | 10,966 |
| Repossessed assets | 5,455 | 10,616 |
| Inventory | 7,794 | 9,234 |
| **Total other assets** | **282,372** | **318,426** |

The Company started granted staff loans originated at interest rates different from market rates. For the accounting of the Company's staff loans issued at fair value as at 31 December 2017 and 2016 the loans were discounted with the application of 20% rate, which according to the Company's management is a market rate taking into account possible credit risk.

Expenses of future periods represent employee benefits represented by effects of loans granted below market rates, that are deferred over the periods during which employee services are received.

## 12. Repurchase agreements

The Company has transactions under repurchase agreements. The securities lent or sold under repurchase agreements are transferred to a third party in exchange for cash received by the Company. These financial assets may be repledged or resold by counterparties in the absence of default by the Company, but the counterparty has an obligation to return the securities at the maturity of the contract. The Company has determined that it retains substantially all the risks and rewards of these securities and therefore has not derecognised them. These transactions are conducted under terms that are usual and customary to standard lending, and securities borrowing and lending activities, as well as requirements determined by exchanges where the Company acts as intermediary.

(in thousands of Armenian Drams)

| | 31 December 2017 | 31 December 2016 |
|---|---|---|
| Fair value of own financial assets available-for-sale pledged under repurchase agreement, Note 8 | - | 100,579 |
| Amortized cost of own financial assets held to maturity and pledged under repurchase agreements, Note 9 | - | 88,746 |
| **Total financial assets transferred and pledged under repurchase agreements** | **-** | **189,325** |
| **Carrying amount of associated liabilities** | **-** | **191,117** |

Accrued interest expense under repurchase agreements is AMD 529 thousand as for 2017 (2016: AMD 440 thousand).

## 13. Loans and Borrowings

| | 31 December 2017 | 31 December 2016 |
|---|---|---|
| ***Non-current*** | | |
| Unsecured loan from the Shareholder | 2,011,907 | 2,012,139 |
| ***Current*** | | |
| Unsecured loan from the Shareholder | 138,869 | 176,893 |
| **Total loans and borrowings** | **2,150,776** | **2,189,032** |

Terms and conditions of outstanding loans were as follows:

| | | | | 31 December 2017 | | 31 December 2016 | |
|---|---|---|---|---|---|---|---|
| | Currency | Nominal interest rate | Year of maturity | Fair value | Carrying amount | Fair value | Carrying amount |
| Unsecured loans from Shareholder | AMD | 15.00% | 2019 | 2,278,494 | 2,150,776 | 2,262,751 | 2,189,032 |

## 14. Share Capital

At 31 December 2017 the total authorised number of ordinary shares is 100,000 shares (31 December 2016: 100,000 shares). Issued and outstanding share capital comprises 17,225 ordinary shares (31 December 2016: 17,225 shares) with a par value of AMD 200,000 per share (31 December 2016: AMD 200,000 per share) aggregating to AMD 3,445,000 thousand (31 December 2016: AMD 3,445,000 thousand). During 2017 no ordinary shares were issued (2016: nil).

The holders of ordinary shares are entitled to receive dividends as declared from time to time and are entitled to one vote per share at annual general meetings of the Company. During 2017 the Company declared AMD 340,282 thousand dividends (2016: AMD 295,167 thousand):

| | 2017 | 2016 |
|---|---|---|
| **Dividends payable at 1 January** | **137,767** | **185,747** |
| Dividends declared during the year | 340,282 | 295,167 |
| Dividends paid during the year | (277,767) | (343,147) |
| **Dividends payable at 31 December** | **200,282** | **137,767** |
| **Dividends per share declared during the year** | **19.8** | **17.1** |

All dividends are declared and paid in Armenian Drams.

During the year by the Resolution of the Shareholder the Company transferred its additional paid in capital to retained earnings in the amount of AMD 390,660 thousand. The brought forward additional paid in capital reserve represented the effect of shareholder loan received at below market rates in prior periods.

(in thousands of Armenian Drams)

## 15. Interest Income and Expense

| | 2017 | 2016 |
|---|---|---|
| **Interest income** | | |
| Loans to customers | 4,831,566 | 4,184,248 |
| Term deposits | 113,289 | 153,608 |
| Held-to-maturity financial assets | 32,932 | 18,013 |
| Available-for-sale financial assets | 44,462 | 26,729 |
| **Total interest income** | **5,022,249** | **4,382,598** |
| **Interest expense** | | |
| Repurchase agreements | (529) | (440) |
| Loans and borrowings | (301,478) | (303,275) |
| **Total interest expense** | **(302,007)** | **(303,715)** |
| **Net interest income** | **4,720,242** | **4,078,883** |

## 16. Other Operating Income

| | 2017 | 2016 |
|---|---|---|
| Fines and penalties | 240,590 | 439,352 |
| Gain from disposal of property and equipment | 183 | 6,863 |
| Other | 231 | 1,186 |
| **Total operating income** | **241,004** | **447,401** |

## 17. Staff Costs

| | 2017 | 2016 |
|---|---|---|
| Employee compensation | 894,140 | 843,831 |
| Benefit from staff loans provided at rates below market | 53,698 | 54,676 |
| Health insurance | 25,578 | 25,248 |
| Other benefits | 21,803 | 23,343 |
| **Total staff costs** | **995,219** | **947,098** |

Amortisation of prepaid employee benefits calculated based on the difference between the actual interest expense and notional market interest expense included in employee compensation.

## 18. Administrative and Other Operating Expenses

| | 2017 | 2016 |
|---|---|---|
| Operating lease expense | 141,024 | 159,976 |
| Depreciation and amortisation | 88,376 | 99,450 |
| Security | 81,332 | 80,317 |
| Board related expenses | 59,743 | 63,066 |
| Repairs and maintenance | 51,154 | 54,040 |
| Taxes other than income | 37,767 | 36,572 |
| Expenses related to loan disbursement and collection | 33,786 | 26,148 |
| Communication and information services | 32,631 | 35,160 |
| Advertising and marketing | 17,953 | 12,668 |
| Travel expenses | 14,245 | 14,282 |
| Professional expenses | 13,216 | 16,777 |
| Obligatory fees | 12,177 | 10,913 |
| Office supplies | 9,989 | 11,097 |
| Staff training expenses | 7,966 | 838 |
| Insurance | 1,671 | 1,843 |
| Other operating expenses | 44,819 | 30,909 |

(in thousands of Armenian Drams)

| | | |
|---|---|---|
| **Total administrative and other operating expenses** | **647,849** | **654,056** |

## 19. Income Taxes

***(a) Components of income tax expense***

Income tax expense comprises the following:

| | 2017 | 2016 |
|---|---|---|
| Current tax expense | 752,225 | 601,680 |
| Deferred tax benefit | (33,196) | (162,370) |
| **Income tax expense for the year** | **719,029** | **439,310** |

***(b) Reconciliation between the tax expense and profit or loss multiplied by applicable tax rate***

The income tax rate applicable to the Company's income for the financial year ended 31 December 2017 is 20% (31 December 2016: 20%). Reconciliation between the expected and the actual taxation charge is provided below.

| | 2017 | 2016 |
|---|---|---|
| **Profit before tax** | 3,546,926 | 2,140,719 |
| Tax charge at statutory rate | (709,385) | (428,144) |
| Tax effect of items which are not deductible or assessable for taxation purposes: | | |
| - Non-deductible expenses | (12,916) | (15,544) |
| - Income exempt from taxation | 3,272 | 4,378 |
| **Income tax expense for the year** | **(719,029)** | **(439,310)** |

The effective tax rate for the year 2017 is 20.27% (2016: 20.52%).

***(c) Deferred taxes analysed by type of temporary difference***

Differences between IFRS and statutory taxation regulations in the RA give rise to temporary differences between the carrying amount of assets and liabilities for financial reporting purposes and their tax bases. The tax effect of the movements in these temporary differences is detailed below and is recorded at the rate of 20%.

| | 1 January 2017 | (Charged)/credited to profit or loss | Recognized in other comprehensive income | 31 December 2017 |
|---|---|---|---|---|
| **Tax effect of temporary differences** | | | | |
| Term deposits | (2,093) | (3,040) | - | (5,133) |
| Loans to customers | (195,587) | 25,836 | - | (169,751) |
| Other assets | (3,624) | 3,624 | - | - |
| Available for sale investments | (4,271) | | (1,679) | (5,950) |
| Other liabilities | 11,068 | 6,776 | - | 17,844 |
| **Deferred income tax liability** | **(194,507)** | **33,196** | **(1,679)** | **(162,990)** |

The tax effect of the movements in the temporary differences for the year ended 31 December 2016 are:

(in thousands of Armenian Drams)

| | 1 January 2016 (restated) | (Charged)/credited to profit or loss | Recognized in other comprehensive income | 31 December 2016 |
|---|---|---|---|---|
| **Tax effect of temporary differences** | | | | |
| Term deposits | (2,547) | 454 | - | (2,093) |
| Loans to customers | (357,340) | 161,753 | - | (195,587) |
| Other assets | (3,265) | (359) | - | (3,624) |
| Available for sale investments | | | (4,271) | (4,271) |
| Other liabilities | 10,546 | 522 | - | 11,068 |
| **Deferred income tax liability** | **(352,606)** | **162,370** | **(4,271)** | **(194,507)** |

| **Deferred income tax assets/(liabilities)** | **2017** | **2016** |
|---|---|---|
| As at January 1 – deferred tax assets | 11,068 | 10,546 |
| As at January 1 – deferred tax liabilities | (205,575) | (363,152) |
| Change in deferred income tax balances recognized in profit or loss | 33,196 | 162,370 |
| Changes in deferred income tax balances recognized in other comprehensive income | (1,679) | (4,271) |
| **As at December 31 – deferred tax assets** | **17,844** | **11,068** |
| **As at December 31 – deferred tax liabilities** | **(180,834)** | **(205,575)** |

## 20. Financial Risk Management

The risk management function within the Company is carried out in respect of financial risks, operational risks and legal risks. Financial risk comprises market risk (including currency risk, interest rate risk and other price risk), credit risk and liquidity risk. The primary objectives of the financial risk management function are to establish risk limits, and then ensure that exposure to risks stays within these limits. The operational and legal risk management functions are intended to ensure proper functioning of internal policies and procedures to minimise operational and legal risks.

The risk management policies aim to identify, analyse and manage the risks faced by the Company, to set appropriate risk limits and controls, and to continuously monitor risk levels and adherence to limits. Risk management policies and procedures are reviewed regularly to reflect changes in market conditions, products and services offered and emerging best practice.

The Board of Directors has overall responsibility for the oversight of the risk management framework, overseeing the management of key risks and reviewing its risk management policies and procedures as well as approving significantly large exposures.

Management is responsible for monitoring and implementation of risk mitigation measures and making sure that the Company operates within the established risk parameters. The Risk Manager is responsible for the overall risk management and compliance functions, ensuring the implementation of common principles and methods for identifying, measuring, managing and reporting both financial and non-financial risks. She reports directly to the Board of Directors through Risk Management Committee.

Credit, market and liquidity risks both at the portfolio and transactional levels are managed and controlled through a system of Credit Committees, Head of Operations, Finance Manager and Finance Director. In order to facilitate efficient and effective decision-making, the Management established a hierarchy of credit committees depending on the type and amount of the credits.

Both external and internal risk factors are identified and managed throughout the Company. Particular attention is given to identifying the full range of risk factors and determination of the level of assurance over the current risk mitigation procedures. Apart from the standard credit and market risk analysis, the Risk Manager monitors financial and non-financial risks by holding regular meetings with operational and other units and relative staff in order to obtain expert judgments in their areas of expertise.

***Credit risk.*** The Company takes on exposure to credit risk, which is the risk that one party to a financial instrument will cause a financial loss for the other party by failing to discharge an obligation. Exposure to credit risk arises as a result of the Company's lending and other transactions with counterparties giving rise to financial assets.

The Company's maximum exposure to credit risk is reflected in the carrying amounts of financial assets on the statement of financial position. The Company structures the levels of credit risk it undertakes by placing limits on the amount of risk accepted in relation to one borrower, or groups of borrowers, and to geographical and industry segments.

Limits on the level of credit risk by product and industry sector are approved regularly by management. Such risks are monitored on a revolving basis and subject to an annual or more frequent review. The Company has policies and procedures for the management of credit exposures (both for recognised financial assets and unrecognised contractual commitments), including guidelines to limit portfolio concentration and the establishment of a Credit Committee which actively monitors credit risk. The credit policy is reviewed and approved by Board of Directors.

The credit policy establishes:

- Procedures for review and approval of loan credit applications
- Methodology for the credit assessment of borrowers (corporate and retail)
- Methodology for the credit assessment of counterparties
- Methodology for the evaluation of collateral
- Credit documentation requirements
- Procedures for the ongoing monitoring of loans and other credit exposures.

The Company operational department follows up on past due balances. Management therefore considers it appropriate to provide ageing and other information about credit risk as disclosed in Note 7.

***Collateral and other credit enhancements.*** Exposure to credit risk is also assessed and managed, in part, by obtaining, controlling and monitoring collateral in the form of mortgage interests over property, pledge of assets and securities and other collateral including personal guarantees as disclosed in Note 7.

While collateral is an important mitigating factor in assessing the credit risk, it is the Company policy to establish that loans are within the customer's capacity to repay rather to rely solely on security. Collateral is considered as a secondary source of repayment. In limited cases, depending on the customer's standing or on the type of product or amounts, the facilities may be unsecured.

The principal types of collateral accepted by the Company are as follows:

- Residential real estate
- Other collateral
- Personal guarantees

As at 31 December 2017 the Company has no debtors or groups of connected debtors (31 December 2016: nil), credit risk exposure to whom exceeds 10% of maximum credit risk exposure.

***Allowance for loan losses – reserve policy.*** The Company establishes an allowance for loan losses that represents its estimate of losses incurred in its risk exposures. The Company utilises the loan loss methodology in its financial statements contained in IAS 39 *Financial Instruments: Recognition and Measurement.*

***Credit risks concentration.*** Credit risk is the most important risk for the Company's business; management therefore carefully manages its exposure to credit risk. Credit exposures arise principally in lending activities that lead to loans and advances, and investment activities that bring Government treasury bills into the Company's asset portfolio. The credit risk is managed and controlled by Credit Committees, Head of Operations and Finance Manager and reported to management regularly.

The maximum exposure to credit risk is generally reflected in the carrying amounts of financial assets on the statement of financial position. The impact of possible netting of assets and liabilities to reduce potential credit exposure is not significant.

Concentration of credit risk for Loans to customers is disclosed in Note 7.

**Loans with renegotiated terms:** Loans with renegotiated terms are loans that have been restructured due to deterioration in the borrower's financial position and where the Company has made concessions that it would not otherwise consider. Once the loan is restructured, it remains in this category independent of satisfactory performance after restructuring.

(in thousands of Armenian Drams)

The table below shows the carrying amount of renegotiated financial assets:

| | 31 December 2017 | 31 December 2016 |
|---|---|---|
| Loans to customers | - | 16,621 |

**Maximum exposure of credit risk:** The Company's maximum exposure to credit risk varies significantly and is dependent on both individual risks and general market economy risks.

The following table presents the maximum exposure to credit risk of balance sheet financial assets. For the financial assets in the balance sheet, the maximum exposure is equal to the carrying amount of those assets prior to any offset or collateral.

| | 31 December 2017 | 31 December 2016 |
|---|---|---|
| Cash and cash equivalent | 264,702 | 67,965 |
| Term deposits | 2,292,052 | 978,561 |
| Loans to customers | 17,084,456 | 15,710,460 |
| Available-for-sale financial assets | 406,783 | 388,666 |
| Held-to-maturity financial assets | 368,513 | 766,353 |
| Other receivables | 15,523 | 4,544 |
| **Total non-derivative financial assets** | **20,432,029** | **17,916,549** |

***Market risk.*** The Company is exposed to market risks. Market risks arise from open positions in (a) currency, (b) interest rate and (c) equity products, all of which are exposed to general and specific market movements.

The objective of market risk management is to manage and control market risk exposures within acceptable parameters, whilst optimizing the return on risk.

The Company manages its market risk by setting open position limits in relation to interest rate maturity and currency positions. These are monitored on a regular basis and reviewed and approved by the Board of Directors through the Risk Management Committee.

In addition, the Company uses stress scenarios to model the financial impact of a variety of exceptional market scenarios on the loan portfolio and the overall financial position.

***Currency risk.*** In respect of currency risk, management sets limits on the level of exposure by currency and in total, which are monitored periodically.

The table below summarises the Company's exposure to foreign currency exchange rate risk at the end of the reporting period:

| | 31 December 2017 | | |
|---|---|---|---|
| | **AMD** | **USD** | **Total** |
| **Non-derivative financial assets** | | | |
| Cash and cash equivalents | 271,639 | 5,046 | 276,685 |
| Term deposits | 2,292,052 | - | 2,292,052 |
| Loans to customers | 17,084,456 | - | 17,084,456 |
| Investments available-for-sale | 406,783 | - | 406,783 |
| Investments held to maturity | 368,513 | - | 368,513 |
| Other receivables | 15,523 | | 15,523 |
| **Total non-derivative financial assets** | **20,438,966** | **5,046** | **20,444,012** |
| **Non-derivative financial liabilities** | | | |
| Borrowed funds | 2,150,776 | - | 2,150,776 |
| Other financial liabilities | 15,249 | - | 15,249 |
| **Total non-derivative financial liabilities** | **2,166,025** | **-** | **2,166,025** |
| **Open balance sheet position** | **18,272,941** | **5,046** | **18,277,987** |

(in thousands of Armenian Drams)

| | 31 December 2016 | | |
|---|---|---|---|
| | **AMD** | **USD** | **Total** |
| **Non-derivative financial assets** | | | |
| Cash and cash equivalents | 66,178 | 6,026 | 72,204 |
| Term deposits | 978,561 | - | 978,561 |
| Loans to customers | 15,710,460 | - | 15,710,460 |
| Investments available-for-sale | 388,666 | - | 388,666 |
| Investments held to maturity | 766,353 | - | 766,353 |
| Other receivables | 4,544 | | 4,544 |
| **Total non-derivative financial assets** | **17,914,762** | **6,026** | **17,920,788** |
| **Non-derivative financial liabilities** | | | |
| Repurchase agreements | 191,117 | - | 191,117 |
| Borrowed funds | 2,189,032 | - | 2,189,032 |
| Other financial liabilities | 19,439 | - | 19,439 |
| **Total non-derivative financial liabilities** | **2,399,588** | **-** | **2,399,588** |
| **Open balance sheet position** | **15,515,174** | **6,026** | **15,521,200** |

**Currency risk sensitivity:** The following table details the Company's sensitivity to a 20% increase and decrease in the AMD against the USD, 20% is the sensitivity rate used when reporting foreign currency risk internally to key management personnel and represents management's assessment of the reasonably possible change in foreign exchange rates. The sensitivity analysis includes only outstanding foreign currency denominated monetary items and adjusts their translation at the period end for a 20% change in foreign currency rates. The sensitivity analysis includes external loans where the denomination of the loan is in a currency other than the functional currency of the lender or the borrower. A positive number below indicates an increase in profit and equity where the AMD strengthens 20% against USD.

| | **31 December 2017** | **31 December 2016** |
|---|---|---|
| Impact on profit or loss | (1,009) | (1,205) |
| Impact on equity | (1,009) | (1,205) |

***Interest rate risk.*** The Company takes on exposure to the effects of fluctuations in the prevailing levels of market interest rates on its financial position and cash flows. Interest margins may increase as a result of such changes but may reduce or create losses in the event that unexpected movements arise. Management monitors periodically and sets limits on the level of mismatch of interest rate repricing that may be undertaken.

The table below summarises the Company's exposure to interest rate risks. The table presents the aggregated amounts of the Company's financial assets and liabilities at carrying amounts, categorised by the earlier of contractual interest repricing or maturity dates.

(in thousands of Armenian Drams)

| | 31 December 2017 | | | | | | |
|---|---|---|---|---|---|---|---|
| | **Weighted average effective interest rate** | **Up to 1 month** | **1 month to 3 months** | **3 months to 1 year** | **1 year to 5 years** | **Over 5 years** | **Total** |
| **Non-derivative financial assets** | | | | | | | |
| *Fixed interest rate instruments* | | | | | | | |
| Cash and cash equivalents | 5.08% | 56,429 | 150,099 | - | - | - | **206,528** |
| Due from banks | 7.88% | 957,521 | 661,145 | 673,386 | - | - | **2,292,052** |
| Loans to customers | 30.16% | 1,085,482 | 2,215,051 | 8,200,852 | 5,555,236 | 27,835 | **17,084,456** |
| Investments available-for-sale | 12.62% | - | - | - | 406,783 | - | **406,783** |
| Investments held to maturity | 7.48% | - | - | 195,327 | 173,186 | - | **368,513** |
| **Total fixed interest bearing financial assets** | | **2,099,432** | **3,026,295** | **9,069,565** | **6,135,205** | **27,835** | **20,358,332** |
| *Non-interest bearing financial assets* | | | | | | | |
| Cash and cash equivalents | | 70,157 | - | - | - | - | **70,157** |
| Other assets | | 15,523 | - | - | - | - | **15,523** |
| **Total non-interest bearing financial assets** | | **85,680** | **-** | **-** | **-** | **-** | **85,680** |
| **Total non-derivative financial assets** | | **2,185,112** | **3,026,295** | **9,069,565** | **6,135,205** | **27,835** | **20,444,012** |
| **Non-derivative financial liabilities and commitments** | | | | | | | |
| *Fixed interest rate instruments* | | | | | | | |
| Borrowed funds | 15.53% | 149,611 | - | 139,221 | 1,861,944 | - | **2,150,776** |
| **Total fixed interest bearing financial liabilities** | | **149,611** | **-** | **139,221** | **1,861,944** | | **2,150,776** |
| *Non-interest bearing financial liabilities and commitments* | | | | | | | |
| Other financial liabilities | | 14,929 | 320 | - | - | - | **15,249** |
| **Total non-interest bearing financial liabilities and commitments** | | **14,929** | **320** | **-** | **-** | **-** | **15,249** |
| **Total non-derivative financial liabilities and commitments** | | **164,540** | **320** | **139,221** | **1,861,944** | **-** | **2,166,025** |
| Interest sensitivity gap | | 1,949,821 | 3,026,295 | 8,930,344 | 4,273,261 | 27,835 | |
| **Cumulative interest sensitivity gap** | | **1,949,821** | **4,976,116** | **13,906,460** | **18,179,721** | **18,207,556** | **18,207,556** |
| Liquidity gap | | 2,020,572 | 3,025,975 | 8,930,344 | 4,273,261 | 27,835 | |
| **Cumulative liquidity gap** | | **2,020,572** | **5,046,547** | **13,976,891** | **18,250,152** | **18,277,987** | **18,277,987** |

(in thousands of Armenian Drams)

| | 31 December 2016 | | | | | | |
|---|---|---|---|---|---|---|---|
| | **Weighted average effective interest rate** | **Up to 1 month** | **1 month to 3 months** | **3 months to 1 year** | **1 year to 5 years** | **Over 5 years** | **Total** |
| **Non-derivative financial assets** | | | | | | | |
| *Fixed interest rate instruments* | | | | | | | |
| Cash and cash equivalents | 0.02% | 63,643 | - | - | - | - | **63,643** |
| Due from banks | 10.82% | 417,267 | 379,130 | 182,164 | - | - | **978,561** |
| Loans to customers | 30.70% | 1,173,954 | 2,128,864 | 7,453,191 | 4,899,759 | 54,692 | **15,710,460** |
| Investments available-for-sale | 12.61% | - | - | - | 388,666 | - | **388,666** |
| Investments held to maturity | 8.87% | 199,033 | 353,843 | - | 213,477 | - | **766,353** |
| **Total fixed interest bearing financial assets** | | **2,099,432** | **3,026,295** | **9,069,565** | **6,135,205** | **27,835** | **20,358,332** |
| *Non-interest bearing financial assets* | | | | | | | |
| Cash and cash equivalents | | 8,561 | - | - | - | - | **8,561** |
| Other assets | | 4,544 | - | - | - | - | **4,544** |
| **Total non-interest bearing financial assets** | | **13,105** | **-** | **-** | **-** | **-** | **13,105** |
| **Total non-derivative financial assets** | | **1,867,002** | **2,861,837** | **7,635,355** | **5,501,902** | **54,692** | **17,920,788** |
| **Non-derivative financial liabilities and commitments** | | | | | | | |
| *Fixed interest rate instruments* | | | | | | | |
| Repurchased agreements | 11.82% | 191,117 | - | - | - | - | **191,117** |
| Borrowed funds | 15.53% | 188,172 | - | 139,166 | 1,861,693 | - | **2,189,031** |
| **Total fixed interest bearing financial liabilities** | | **379,289** | **-** | **139,166** | **1,861,693** | **-** | **2,380,148** |
| *Non-interest bearing financial liabilities and commitments* | | | | | | | |
| Other financial liabilities | | 14,319 | 5,120 | - | - | - | **19,439** |
| **Total non-interest bearing financial liabilities and commitments** | | **14,319** | **5,120** | **-** | **-** | **-** | **19,439** |
| **Total non-derivative financial liabilities and commitments** | | **393,608** | **5,120** | **139,166** | **1,861,693** | **-** | **2,399,587** |
| Interest sensitivity gap | | 1,474,608 | 2,861,837 | 7,496,189 | 3,640,209 | 54,692 | |
| **Cumulative interest sensitivity gap** | | **1,474,608** | **4,336,445** | **11,832,634** | **15,472,842** | **15,527,535** | **15,527,535** |
| Liquidity gap | | 1,473,394 | 2,856,717 | 7,496,189 | 3,640,209 | 54,692 | |
| **Cumulative liquidity gap** | | **1,473,394** | **4,330,111** | **11,826,300** | **15,466,509** | **15,521,201** | **15,521,201** |

***Geographical risk concentrations.*** All financial assets and liabilities are located within the RA as at 31 December 2017 and 2016.

***Liquidity risk.*** Liquidity risk is the risk that an entity will encounter difficulty in meeting obligations associated with financial liabilities.

The Company seeks to maintain a stable funding base primarily consisting of amounts due to other financial institutions. The Company holds the funds in deposits, in order to be able to respond quickly and smoothly to unforeseen liquidity requirements.

The liquidity management of the Company requires consideration of the level of liquid assets necessary to settle obligations as they fall due; maintaining access to a range of funding sources; maintaining funding contingency plans; and monitoring liquidity ratios against regulatory requirements. These ratios are:

- Idle cash ratio which is calculated as the ratio cash and cash equivalents divided by the outstanding loan portfolio. The ratio was 1.62% at 31 December 2017 (31 December 2016: 0.46%);
- Highly liquid assets to total assets ratio which is calculated as the ratio cash and cash equivalents divided by total assets. The ratio was 1.30% at 31 December 2017 (31 December 2016: 0.38%);
- Current ratio which is calculated as the ratio of current assets to current liabilities. The ratio was 15.73 at 31 December 2017 (31 December 2016: 12.68);
- Quick ratio which is calculated as the ratio of cash and cash equivalents divided by current liabilities. The ratio was 0.0.30 at 31 December 2017 (31 December 2016: 0.07).

The Company maintains liquidity management with the objective of ensuring that funds will be available at all times to honour all cash flow obligations as they become due. The liquidity policy is reviewed and approved by the Board of Directors through the Risk Management Committee.

The Company seeks to actively support a diversified and stable funding base comprising long-term and short-term loans from banks and other lending institutions, in order to be able to respond quickly and smoothly to unforeseen liquidity requirements.

The liquidity management policy requires:

- Projecting cash flows by currencies and considering the level of liquid assets necessary in relation thereto
- Maintaining a diverse range of funding sources
- Managing the concentration and profile of debts
- Maintaining debt financing plans
- Maintaining a portfolio of highly marketable assets that can easily be liquidated as protection against any interruption to cash flow
- Maintaining liquidity and funding contingency plans
- Monitoring liquidity ratios against benchmarks.

The table below shows liabilities at 31 December 2017 and 2016 by their remaining contractual maturity. The amounts of liabilities disclosed in the liquidity table are the contractual undiscounted cash flows. Such undiscounted cash flows differ from the amount included in the statement of financial position because the amount in the statement of financial position is based on discounted cash flows. When the amount payable is not fixed, the amount disclosed is determined by reference to the conditions existing at the end of the reporting period. Foreign currency payments are translated using the spot exchange rate at the end of the reporting period.

The management of the Company does not anticipate significant differences between expected and contractual maturities of financial instruments.

(in thousands of Armenian Drams)

| | 31 December 2017 | | | | | | |
|---|---|---|---|---|---|---|---|
| | **Weighted average effective interest rate** | **Up to 1 month** | **1 month to 3 months** | **3 months to 1 year** | **1 year to 5 years** | **Total** | **Carrying amount** |
| *Fixed interest rate instruments* | | | | | | | |
| Borrowed funds | 15.53% | 150,442 | - | 150,442 | 2,312,283 | **2,613,167** | **2,150,776** |
| **Total fixed interest bearing financial liabilities** | | **150,442** | **-** | **150,442** | **2,312,283** | **2,613,167** | **2,150,776** |
| *Non-interest bearing financial liabilities* | | | | | | | |
| Other financial liabilities | | 14,929 | 320 | - | - | **15,249** | **15,249** |
| **Total non-interest bearing financial liabilities** | | **14,929** | **320** | **-** | **-** | **15,249** | **15,249** |
| **Total financial liabilities** | | **165,371** | **320** | **150,442** | **2,312,283** | **2,628,416** | **2,166,025** |

| | 31 December 2016 | | | | | | |
|---|---|---|---|---|---|---|---|
| | **Weighted average effective interest rate** | **Up to 1 month** | **1 month to 3 months** | **3 months to 1 year** | **1 year to 5 years** | **Total** | **Carrying amount** |
| *Fixed interest rate instruments* | | | | | | | |
| Liabilities under repurchase agreements | 11.82% | 191,117 | - | - | - | **191,117** | **191,117** |
| Borrowed funds | 15.53% | 189,292 | - | 150,442 | 2,613,167 | **2,952,901** | **2,189,032** |
| **Total fixed interest bearing financial liabilities** | | **380,409** | **-** | **150,442** | **2,613,167** | **3,144,018** | **2,380,149** |
| *Non-interest bearing financial liabilities* | | | | | | | |
| Other financial liabilities | | 14,319 | 5,120 | - | - | **19,439** | **19,439** |
| **Total non-interest bearing financial liabilities** | | **14,319** | **5,120** | - | - | **19,439** | **19,439** |
| **Total financial liabilities** | | **394,278** | **5,120** | **150,442** | **2,613,167** | **3,163,457** | **2,399,588** |

(in thousands of Armenian Drams)

## 21. Management of Capital

The Company's objectives when managing capital are: (a) to comply with the capital requirements set by the CBA, (b) to safeguard the Company's ability to continue as a going concern in order to provide returns for shareholders and benefits for other stakeholders and to maintain an optimal capital structure to reduce the cost of capital. In order to maintain or adjust the capital structure, the Company may adjust the amount of dividends paid to shareholders, return capital to shareholders, issue new shares or sell assets to reduce debt. The amount of capital that the Company managed as of 31 December 2017 was AMD 18,294,241 thousand (31 December 2016: AMD 15,799,910 thousand).

Under the current capital requirements set by the CBA, credit organisations have to maintain a minimum share capital and total capital of AMD 150,000 thousand. The Company is in compliance with the statutory capital requirements during the years ended 31 December 2017 and 2016.

## 22. Contingencies and Commitments

***Legal proceedings.*** From time to time and in the normal course of business, claims against the Company may be received. On the basis of its own estimates and both internal professional advice management is of the opinion that no material losses will be incurred in respect of claims and accordingly no provision has been made in these financial statements.

***Tax legislation.*** The taxation system in the RA is relatively new and is characterised by frequent changes in legislation, official pronouncements and court decisions, which are sometimes unclear, contradictory and subject to varying interpretation. Taxes are subject to review and investigation by tax authorities, which have the authority to impose fines and penalties. A tax year remains open for review by the tax authorities during the three subsequent calendar years.

These circumstances may create tax risks in the RA that are more significant than in other countries. Management believes that it has provided adequately for tax liabilities based on its interpretations of applicable Armenian tax legislation, official pronouncements and court decisions. However, the interpretations of the relevant authorities could differ and the effect on these financial statements, if the authorities were successful in enforcing their interpretations, could be significant.

***Insurance.*** The insurance industry in the RA is in a developing state and many forms of insurance protection common in other parts of the world are not yet generally available. The Company does not have full coverage for its premises and equipment, business interruption, or third-party liability in respect of property or environmental damage arising from accidents on its property or relating to operations. Until the Company obtains adequate insurance coverage, there is a risk that the loss or destruction of certain assets could have a material adverse effect on operations and financial position.

***Capital expenditure commitments.*** At 31 December 2017 and 2016 the Company had no contractual capital expenditure commitments in respect of premises and equipment.

**Operating lease commitments.** Operating leases relate to leases of office premises with lease terms of between 1 and 5 years. Operating lease contracts contain clauses for market rental reviews. The Company does not have an option to purchase the leased property at the expiry of the lease periods.

During the period the rent expense recognised was AMD 141,024 thousand (2016: AMD 159,976 thousand).

The Company has the following non-cancellable operating lease commitments:

| | 31 December 2017 | 31 December 2016 |
|---|---|---|
| Less than 1 year | 86,388 | 85,550 |
| Later than 1 year and not later than 5 years | 164,516 | 163,934 |
| **Total operating lease commitments** | **250,904** | **249,484** |

***Compliance with the CBA regulations.*** The Company is subject to certain statutory regulations set by the CBA related primarily to its operations. Non-compliance with such regulations may result in negative consequences for the Company including penalties imposed by the CBA. The Company was in compliance with these regulations as at 31 December 2017 and 2016.

***Operating environment.*** Emerging markets such as Armenia are subject to different risks than more developed markets, including economic, political and social, and legal and legislative risks. Laws and regulations affecting businesses in Armenia continue to change rapidly tax and regulatory frameworks are subject to varying interpretations. The future economic direction of Armenia is heavily influenced by the fiscal and monetary policies adopted by the government, together with developments in the legal, regulatory, and political environment. Armenia continues to undergo political and economic changes. As an emerging market, Armenia does not possess a developed business and regulatory infrastructure that generally exists in a more mature free market economy. In addition, economic conditions continue to limit the volume of activity in the financial markets, which may not be reflective of the values for financial instruments. The main obstacle to further economic development is a low level of economic and institutional development, along with a centralized economic base, regional instability and international economic crisis.

Adverse changes arising from systemic risks in global financial systems, including any tightening of the credit environment could slow or disrupt the Republic of Armenia's economy, may adversely affect the Company's access to capital and cost of capital for the Company and, more generally, its business, results of operations, financial condition and prospects. Moreover, there are still uncertainties about the economic situation of countries, collaborating with Armenia, due to the forecasted slowdown in the world economy, which may lead to the shortage of money transfers from abroad, as well as to the decline in the prices of mining products, upon which the economy of Armenia is significantly dependent. In times of more severe market stress, the situation of Armenian economy and of the Company may be exposed to deterioration. However, as the number of variables and assumptions involved in these uncertainties is large, management cannot make a reliable estimate of the amounts by which the carrying amounts of assets and liabilities of the Company may be affected.

The financial statements of the Company do not include the effects of adjustments, if any, which might have been considered necessary, had the effects of the factors described above become observable and reliably measurable in Armenia.

## 23. Fair Value of Financial Instruments

IFRS defines fair value as 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 estimates presented herein are not necessarily indicative of the amounts the Company could realize in a market exchange from the sale of its full holdings of a particular instrument.

However, judgment is required to interpret market data to determine the estimated fair value. Republic of Armenia continues to display some characteristics of an emerging market and economic conditions continue to limit the volume of activity in the financial markets. Market quotations may be outdated or reflect distress sale transactions and therefore not represent fair values of financial instruments. Management has used all available market information in estimating the fair value of financial instruments.

**Fair value of the financial assets and financial liabilities that are measured at fair value on a recurring basis.** Some of the Company's financial assets and financial liabilities are measured at fair value at the end of each reporting period. The following table gives information about how the fair values of these financial assets and financial liabilities are determined (in particular, the valuation technique(s) and inputs used).

| | Fair value as at | | | | | |
|---|---|---|---|---|---|---|
| **Financial assets/ liabilities** | **31 December 2017** | **31 December 2016** | **Fair value Hierarchy** | **Valuation technique(s) and key input(s)** | **Significant unobservable input(s)** | **Relationship of unobservable inputs to fair value** |
| Government securities of the Republic of Armenia held by the Company | 406,783 | 288,087 | Level 2 | Discounted cash flows. The predetermined cash flows are discounted at a rate that reflects market yield for specific time to maturity | N/A | N/A |
| Government securities of the Republic of Armenia pledged under repurchase agreement | - | 100,579 | Level 2 | Discounted cash flows. The predetermined cash flows are discounted at a rate that reflects market yield for specific time to maturity | N/A | N/A |

(in thousands of Armenian Drams)

**Fair value of financial assets and financial liabilities that are not measured at fair value on a recurring basis (but fair value disclosures are required).** Except as detailed in the following table, the management considers that the carrying amounts of financial assets and financial liabilities recognised in the financial statements approximate their fair values.

| | 31 December 2017 | | 31 December 2016 | |
|---|---|---|---|---|
| | **Carrying amount** | **Fair value** | **Carrying amount** | **Fair value** |
| ***Financial assets*** | | | | |
| *Loans and receivables:* | | | | |
| - loans to customers | 17,084,456 | 19,110,863 | 15,710,460 | 16,771,611 |
| - trade and other receivables | 15,523 | 15,523 | 4,554 | 4,554 |
| *Held-to-maturity investments:* | | | | |
| - government treasury bills | 368,513 | 375,274 | 766,353 | 767,575 |
| ***Financial liabilities*** | | | | |
| *Financial liabilities held at amortised cost:* | | | | |
| - repurchase agreements | - | - | 191,117 | 191,117 |
| - loans from related parties | 2,150,776 | 2,278,494 | 2,189,032 | 2,262,751 |
| - loans from other entities | - | - | - | - |
| - trade and other payables | 15,249 | 15,249 | 19,439 | 19,439 |

| | Fair value hierarchy as at 31 December 2017 | | | |
|---|---|---|---|---|
| | **Level 1** | **Level 2** | **Level 3** | **Total** |
| ***Financial assets*** | | | | |
| *Loans and receivables:* | | | | |
| - loans to customers | - | - | 19,110,863 | **19,110,863** |
| - trade and other receivables | - | - | 15,523 | **15,523** |
| *Held-to-maturity investments:* | | | | |
| - government treasury bills | - | 375,274 | - | **375,274** |
| ***Total*** | **-** | **375,274** | **19,126,386** | **19,501,660** |
| ***Financial liabilities*** | | | | |
| *Financial liabilities held at amortised cost:* | | | | |
| - loans from related parties | - | 2,278,494 | - | **2,278,494** |
| - trade and other payables | - | - | 15,249 | **15,249** |
| **Total** | | **2,278,494** | **15,249** | **2,293,743** |

(in thousands of Armenian Drams)

| | Fair value hierarchy as at 31 December 2016 | | | |
|---|---|---|---|---|
| | **Level 1** | **Level 2** | **Level 3** | **Total** |
| ***Financial assets*** | | | | |
| *Loans and receivables:* | | | | |
| - loans to customers | - | 16,771,611 | - | **16,771,611** |
| - trade and other receivables | - | - | 4,554 | **4,554** |
| *Held-to-maturity investments:* | | | | |
| - government treasury bills | - | 767,575 | - | **767,575** |
| ***Total*** | **-** | **17,539,185** | **4,554** | **17,543,739** |
| ***Financial liabilities*** | | | | |
| *Financial liabilities held at amortised cost:* | | | | |
| - repurchase agreements | - | 191,117 | - | **191,117** |
| - loans from related parties | - | 2,262,751 | | **2,262,751** |
| - loans from other entities | - | - | - | **-** |
| - trade and other payables | - | - | 19,439 | **19,439** |
| **Total** | **-** | **2,453,868** | **19,439** | **2,473,307** |

The fair values of the financial assets and liabilities included in the Level 2 and Level 3 categories above have been determined in accordance with generally accepted pricing models based on a discounted cash flow analysis, with the most significant inputs being the discount rate that reflects the credit risk of counterparties.

## 24. Related Party Transactions

Parties are generally considered to be related if the parties are under common control or one party has the ability to control the other party or can 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.

At 31 December 2017 and 2016, the outstanding balances with related parties were as follows:

| | **31 December 2017** | | **31 December 2016** | |
|---|---|---|---|---|
| | Related party balances | Total category as per the financial statements caption | Related party balances | Total category as per the financial statements caption |
| Loans to customers: | | | | |
| - Gross amount of loans to key management (contractual interest rate: 5%, maturity: 2026) | 92,371 | 17,507,719 | 99,417 | 16,437,355 |
| Allowance for impairment losses on loans to customers | (514) | (423,263) | (2,694) | (726,895) |
| Loans and borrowings: | | | | |
| - the shareholder | 2,150,776 | 2,150,776 | 2,189,032 | 2,189,032 |
| Dividends payable | | | | |
| - the shareholder | 200,282 | 200,282 | 137,767 | 137,767 |

Key management personnel include members of Executive Administration, Heads of Units and Controller.

Total remuneration for members of the Board of Directors included in Administrative and Other Operating Expenses and for key management personnel included in Staff Costs for the years ended 31 December 2017 and 2016 were as follows:

(in thousands of Armenian Drams)

| | 2017 | | 2016 | |
|---|---|---|---|---|
| | Related party transactions | Total category as per the financial statements caption | Related party transactions | Total category as per the financial statements caption |
| **Key management personnel compensation:** | | (955,415) | | (947,098) |
| *- short-term employee benefits* | (101,387) | | 109,090 | |
| *- other long-term benefits* | (10,077) | | 10,223 | |
| **Total** | **(111,464)** | **(955,415)** | **119,313** | **(947,098)** |

The income and expense items with related parties were as follows:

| | 2017 | | 2016 | |
|---|---|---|---|---|
| | Related party transactions | Total category as per the financial statements caption | Related party transactions | Total category as per the financial statements caption |
| Interest income | | 5,022,250 | | 4,382,598 |
| *- key management personnel* | 16,950 | | 18,536 | |
| Interest expense | | 302,007 | | 303,715 |
| *- the shareholder* | 301,478 | | 303,275 | |
| Operating expenses | | 647,578 | | 643,525 |
| *- Board related expenses* | 36,870 | | 39,300 | |

All related party transactions were made on an arm’s length, except for staff loans.