Financial Statements and Independent Auditor's Report

“ARMBUSINESSBANK” Closed Joint Stock Company

31 December 2018

Contents

Independent auditor's report

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Վաղարշյան 8/1

Հ. + 374 10 260 964
Ֆ.+ 374 10 260 961

Grant Thornton CJSC
8/1 Vagharshyan Str.
0012 Yerevan, Armenia

T + 374 10 260 964
F + 374 10 260 961

To the shareholders of "ARMBUSINESSBANK" Closed Joint Stock Company

Opinion

We have audited the financial statements of "ARMBUSINESSBANK" Closed Joint Stock Company (the "Bank"), which comprise the statement of financial position as of 31 December 2018, and the statement of profit or loss and other 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 give a true and fair view of the financial position of the Bank as of 31 December 2018 and of 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 Bank 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 the Republic of Armenia, and we have fulfilled our other ethical responsibilities in accordance with those ethical requirements. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Key Audit Matters

Key audit matters are those matters that, in our professional judgment, were of most significance in our audit of the financial statements of the current period. These matters were addressed in the context of our audit of the financial statements as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on these matters.

- *First time adoption of IFRS 9*

Refer to note **4.4** of the financial statements for a description of the accounting policies and to note **36.1** for an analysis of credit risk.

The International Accounting Standards Board (IASB) issued IFRS 9 – "Financial Instruments" which replaces "IAS 39 – Financial Instruments". The key changes arising from adoption of IFRS 9 are that the Bank's

impairment losses are now based on expected losses rather than an incurred loss model, and the change in the classification and measurement of the Bank's financial assets and liabilities, which are detailed in Note **4.4** to the financial statements. There were no significant changes arising from the adoption of the hedge accounting requirements of IFRS 9.

As described in the notes to the financial statements, the financial assets have been classified and the impairment losses have been determined in accordance with IFRS 9 Financial Instruments. This was considered a key audit matter as IFRS 9 is a new and complex accounting standard which requires significant judgment to classify the financial assets as well as to determine the impairment reserve.

Key areas of judgment included: the assessment of the business model within which the assets are held, the assessment of whether the contractual terms of the financial asset are solely payments of principal and interest on the principal amount outstanding, the interpretation of the requirements to determine impairment under application of IFRS 9, which is reflected in the Bank's expected credit loss model, the identification of exposures with a significant deterioration in credit quality, assumptions used in the expected credit loss model such as the financial condition of the counterparty, expected future cash flows and forward looking macroeconomic factors and the need to apply additional overlays to reflect current or future external factors that are not appropriately captured by the expected credit loss model.

With respect to classification and measurement of financial assets and financial liabilities, our audit procedures comprised the following;

- We read the Bank's IFRS 9 based classification and measurement of financial assets and financial liabilities policy and compared it with the requirements of IFRS 9;
- We obtained an understanding and checked the Bank's business model assessment and the test on the contractual cash flows, which give rise to cash flows that are 'solely payments of principal and interest' [SPPI test] performed by the Bank's consultant; and
- We checked the appropriateness of the opening balance adjustments.

With respect to impairment methodology, our audit procedures comprised the following;

- We read the Bank's IFRS 9 based impairment provisioning policy and compared it with the requirements of IFRS 9;
- We assessed the design and tested the operating effectiveness of relevant controls over the data used to determine the impairment reserve, including transactional data captured at loan origination, ongoing internal credit quality assessments, storage of date and interfaces to the expected credit loss model;
- We assessed the design and tested the operating effectiveness of relevant controls over the expected credit loss model, including model build and approval, ongoing monitoring/validation, model governance and mathematical accuracy;
- We checked the appropriateness of the Bank's determination of significant increase in credit risk and the resultant basis for classification of exposures into various stages;
- For a sample of exposures, we checked the appropriateness of the Bank's staging;
- We assessed and tested the material modeling assumptions as well as overlays with a focus on the key modeling assumptions adopted by the Bank and sensitivity of the provisions to changes in modeling assumptions;
- For forward looking assumptions used by the Bank's management in its ECL calculations, we held discussions with management and corroborated the assumptions using publicly available information;
- We examined a sample of exposures and performed procedures to evaluate the timely identification of exposures with a significant deterioration in credit quality and expected loss calculation for exposures assessed on an individual basis;
- We checked the completeness of loans and advances, off balance sheet items, investment securities,

placements and other financial assets included in the ECL calculations as of 31 December 2018; We understood the theoretical soundness and tested the mathematical integrity of the Models;

- For data from external sources, we understood the process of choosing such data, its relevance for the Bank, and the controls and governance over such data;
- We involved our IT specialists in areas that required specific expertise (i.e. data reliability and the expected credit loss model);
- We checked the appropriateness of the opening balance adjustments.

We assessed the accuracy of the disclosures in the financial statements.

Other information

Management is responsible for the other information. The other information comprises the information included in the annual report of the Bank for the year ended 31 December 2018, but does not include the financial statements and our auditor's report thereon. The annual report is expected to be made available to us after the date of this auditor's report.

Our opinion on the financial statements does not cover the other information and we will not express any form of assurance conclusion thereon.

In connection with our audit of the financial statements, our responsibility is to read the other information identified above when it becomes available and, in doing so, consider whether the other information is materially inconsistent with the financial statements or our knowledge obtained in the audit, or otherwise appears to be materially misstated.

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 Bank'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 Bank or to cease operations, or has no realistic alternative but to do so.

Those charged with governance are responsible for overseeing the Bank'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 skepticism 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 Bank'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 Bank'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 Bank 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.

We also provide those charged with governance with a statement that we have complied with relevant ethical requirements regarding independence, and to communicate with them all relationships and other matters that may reasonably be thought to bear on our independence, and where applicable, related safeguards.

From the matters communicated with those charged with governance, we determine those matters that were of most significance in the audit of the financial statements of the current period and are therefore the key audit matters. We describe these matters in our auditor's report unless law or regulation precludes public disclosure about the matter or when, in extremely rare circumstances, we determine that a matter should not be communicated in our report because the adverse consequences of doing so would reasonably be expected to outweigh the public interest benefits of such communication.

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

Gagik Gyulbudaghyan	Armen Hovhannisyan
Managing Partner	Engagement Partner

29 April 2019

Statement of profit or loss and other comprehensive income

In thousand Armenian drams

	Notes	2018	2017
Interest and similar income	7	41,563,495	35,262,768
Interest and similar expense	7	(32,975,738)	(28,374,816)
Net interest income		8,587,757	6,887,952
Fee and commission income	8	4,749,493	3,282,273
Fee and commission expense	8	(1,361,796)	(883,875)
Net fee and commission income		3,387,697	2,398,398
Net trading income	9	2,108,344	1,429,550
Gains less losses from foreign currency translation		113,608	(4,755)
Gains less losses on investments available for sale		-	16,987
Other income	10	3,321,707	2,525,494
Impairment losses	11	(7,453,083)	(3,105,599)
Personnel expenses	12	(3,950,625)	(3,626,877)
Depreciation of property and equipment	20	(679,115)	(819,859)
Amortization of intangible assets	21	(372,258)	(161,098)
Other expenses	13	(3,877,988)	(3,871,793)
Operating profit		1,186,044	1,668,400
Income tax expense	14	(333,524)	(388,206)
Profit for the year		852,520	1,280,194
Items that will be reclassified subsequently to profit or loss			
Movement in fair value reserve (debt instruments)			
Net change in fair value during the year		225,428	-
Income tax related to the above		(45,087)	-
Net gains on financial investments at fair value through other comprehensive income		180,341	-
Movement in fair value reserve (available –for-sale)			
Net unrealized gains from changes in fair value from available-for-sale financial assets		-	562,783
Net amounts realized to statement of profit or loss and other comprehensive income on disposal of available-for-sale instruments		-	69,375
Income tax related to the above		-	(126,432)
Net gains on available-for-sale financial assets		-	505,726
Total comprehensive income for the year		1,032,861	1,785,920

The statement of profit or loss and other comprehensive is to be read in conjunction with the notes to and forming part of the financial statements set out on pages 13 to 77.

Statement of financial position

In thousand Armenian drams	Notes	31 December 2018	31 December 2017
Assets			
Cash and cash equivalents	15	127,342,452	115,576,209
Amounts due from financial institutions	17	13,898,845	14,036,722
Loans to customers	18	435,625,901	382,547,013
Investment securities			
- Investments available for sale	19	-	1,649,612
- Investment securities at fair value through other comprehensive income	19	3,460,892	-
- Securities pledged under repurchase agreements	19	9,145,216	15,258,125
Property and equipment	20	12,316,130	9,138,396
Intangible assets	21	2,502,505	2,702,599
Deferred income tax assets	14	996,100	-
Repossessed assets	22	3,566,477	3,716,481
Other assets	23	2,969,505	2,905,216
Total assets		611,824,023	547,530,373
Liabilities and equity			
Liabilities			
Derivative financial liabilities	16	8,940	-
Amounts due to financial institutions	24	64,996,179	76,004,421
Financial liabilities held for trading	25	23,230,915	24,556,156
Amounts due to Government of the RA	26	637,591	692,952
Amounts due to customers	27	473,205,797	398,967,148
Debt securities issued	28	11,462,171	8,967,294
Current income tax liabilities		419,282	296,211
Deferred income tax liabilities	14	-	7,716
Other liabilities	29	1,895,505	1,201,476
Total liabilities		575,856,380	510,693,374

Statement of financial position (continued)

In thousand Armenian drams

	Notes	31 December 2018	31 December 2017
Equity			
Share capital	30	31,374,560	31,374,560
Statutory general reserve		755,177	691,167
Other reserves		2,672,235	2,480,668
Retained earnings		1,165,671	2,290,604
Total equity		35,967,643	36,836,999
Total liabilities and equity		611,824,023	547,530,373

The financial statements were approved on 29 April 2019 by:

Artavazd Sargsyan
Chairman of the Executive Board

Narine Sargsyan
Chief Accountant

The statement of financial position is to be read in conjunction with the notes to and forming part of the financial statements set out on pages 13 to 77.

Statement of changes in equity

In thousand Armenian drams

	Share capital	Statutory general reserve	Fair value reserve	Revaluation reserve of property and equipment	Retained earnings	Total
Balance as of 31 December 2017	31,374,560	691,167	2,009,246	471,422	2,290,604	36,836,999
Impact of adopting IFRS 9 (**note 6**)	-	-	11,226	-	(1,913,443)	(1,902,217)
Restated balance at 1 January 2018	31,374,560	691,167	2,020,472	471,422	377,161	34,934,782
Profit for the year	-	-	-	-	852,520	852,520
Other comprehensive income:						
Net change in fair value of equity instruments at FVOCI	-	-	225,428	-	-	225,428
Income tax relating to components of other comprehensive income	-	-	(45,087)	-	-	(45,087)
Total comprehensive income for the year	-	-	180,341	-	852,520	1,032,861
Distribution to reserve	-	64,010	-	-	(64,010)	-
Total transactions with owners	-	64,010	-	-	(64,010)	-
Balance as of 31 December 2018	31,374,560	755,177	2,200,813	471,422	1,165,671	35,967,643
Balance as of 1 January 2017	31,374,560	638,508	1,503,520	471,422	1,063,069	35,051,079
Profit for the year	-	-	-	-	1,280,194	1,280,194
Other comprehensive income:						
Net unrealized gains from changes in fair value	-	-	562,783	-	-	562,783
Net amounts realized to statement of profit or loss and other comprehensive income on disposal of available-for-sale instruments	-	-	69,375	-	-	69,375
Income tax relating to components of other comprehensive income	-	-	(126,432)	-	-	(126,432)
Total comprehensive income for the year	-	-	505,726	-	1,280,194	1,785,920
Distribution to reserve	-	52,659	-	-	(52,659)	-
Total transactions with owners	-	52,659	-	-	(52,659)	-
Balance as of 31 December 2017	31,374,560	691,167	2,009,246	471,422	2,290,604	36,836,999

The statement of changes in equity is to be read in conjunction with the notes to and forming part of the financial statements set out on pages 13 to 77.

Statement of cash flows

In thousand Armenian drams

	2018	2017
Cash flows from operating activities		
Profit before tax	1,186,044	1,668,400
Adjustments for		
Amortization and depreciation allowances	1,051,373	980,957
Gain from sale of property and equipment	(37)	(13,129)
Impairment charge of financial assets	7,453,083	3,105,599
Net (gain)/loss from changes in fair value of trading instruments	45,119	(19,880)
Interest receivable	(11,557,887)	(5,078,406)
Interest payable	1,277,722	996,153
Foreign currency translation net (gain)/loss	(113,608)	4,755
Cash flows from/(used in) operating activities before changes in operating assets and liabilities	(658,191)	1,644,449
(Increase)/decrease in operating assets		
Derivative financial assets	(45,119)	42,728
Amounts due from financial institutions	(604,214)	(5,204,585)
Loans to customers	(51,473,010)	(102,663,389)
Repossessed assets	150,004	805,866
Other assets	(418,898)	(521,036)
Increase/(decrease) in operating liabilities		
Derivative financial liabilities	8,940	(42,456)
Amounts due to financial institutions	(6,423,565)	(18,023,948)
Financial liabilities held for trading	(1,325,241)	3,067,084
Amounts due to RA Government	(53,920)	(467,713)
Amounts due to customers	76,269,316	135,379,207
Other liabilities	831,409	177,865
Net cash flow from operating activities before income tax	16,257,511	14,194,072
Income tax paid	(783,800)	(114,014)
Net cash from operating activities	15,473,711	14,080,058

Statement of cash flows (continued)

In thousand Armenian drams

	2018	2017
Cash flows from investing activities		
Proceeds from sale of investment securities	4,368,743	19,678,998
Purchase of property and equipment	(4,758,756)	(925,867)
Purchase of intangible assets	(172,164)	(440,770)
Proceeds from sale of property and equipment	901,944	237,737
Net cash from investing activities	339,767	18,550,098
Cash flow from financing activities		
Loans received/(repayment) from financial institutions	(3,801,812)	9,770,445
Debt securities issued	2,457,166	8,912,120
Net cash from/ (used in) financing activities	(1,344,646)	18,682,565
Net increase in cash and cash equivalents	14,468,832	51,312,721
Cash and cash equivalents at the beginning of the year	115,576,209	63,215,155
Effect of ECL	(6,085)	-
Exchange differences on cash and cash equivalents	(2,696,504)	1,048,333
Cash and cash equivalents at the end of the year (note 15)	127,342,452	115,576,209
Supplementary information:		
Interest received	30,005,608	30,184,362
Interest paid	(32,975,738)	(27,378,663)

The statement of cash flows is to be read in conjunction with the notes to and forming part of the financial statements set out on pages 13 to 77.

Notes to the financial statements

1 Principal activities

"ARMBUSINESSBANK" Closed Joint Stock Company (previous "Hayinvestbank" CJSC) (the "Bank") was incorporated in the Republic of Armenia in 1991. The Bank is regulated by the legislation of RA and conducts its business under license number 40, granted on 10 December 1991 by the Central Bank of Armenia (the "CBA").

The Bank is a member of Individuals deposit compensation guarantee state system of RA, as well as member of Union of Banks of Armenia, ArCa, MasterCard, Visa International payment systems.

The Bank accepts deposits from the public, extends credits, transfers payments in Armenia and abroad, exchanges currencies and provides other banking services to its commercial and retail customers.

The Bank's main office and its 27 branches are located in Yerevan, 23 branches are located in different regions of Armenia and 7 branches are located in the Republic of Nagorno Karabakh.

The registered office of the Bank is located at: 48 Nalbandyan Street, Yerevan.

2 Armenian business environment

Armenia continues to undergo political and economic changes. The stability and development of the Armenian economy largely depends on these changes, as well as developments in the Eurasian Economic Union with which the integration of the Armenian economy continues.

Management of the Bank believes that in the current conditions appropriate measures are implemented in order to ensure economic stability of the Bank.

3 Basis of preparation

3.1 Statement of compliance

The financial statements of the Bank have been prepared in accordance with International Financial Reporting Standards ("IFRS") as developed and published by the International Accounting Standards Board (IASB), and Interpretations issued by the International Financial Reporting Interpretations Committee ("IFRIC").

The Bank prepares statements for regulatory purposes in accordance with legislative requirements of the Republic of Armenia. These financial statements are based on the Bank's books and records as adjusted and reclassified in order to comply with IFRS.

3.2 Basis of measurement

The financial statements have been prepared on a fair value basis for financial instruments at fair value through profit or loss and at fair value through other comprehensive income (before 1 January 2018 available for sale assets). Other financial assets and liabilities are stated at amortized cost and non-financial assets and liabilities are stated at historical cost, with the exception of buildings, which are stated at revalued amount.

3.3 Functional and presentation currency

Functional currency of the Bank is the currency of the primary economic environment in which the Bank operates. The Bank's functional currency and the Bank's presentation currency is Armenian Dram ("AMD"), since this currency best reflects the economic substance of the underlying events and transactions of the Bank. The financial statements are presented in thousands of AMD, unless otherwise stated, which is not convertible outside Armenia.

3.4 Changes in accounting policies

The Bank applied for the first time certain standards and amendments, which are effective for annual periods beginning on or after 1 January 2018. The Bank has not early adopted any other standard, interpretation or amendment that has been issued but is not yet effective.

IFRS 9 Financial Instruments

IFRS 9 replaces IAS 39 for annual periods on or after 1 January 2018. The Bank has not restated comparative information for 2017 for financial instruments in the scope of IFRS 9. Therefore, the comparative information for 2017 is reported under IAS 39 and is not comparable to the information presented for 2018. Differences arising from the adoption of IFRS 9 have been recognised directly in retained earnings as of 1 January 2018 and are disclosed in **Note 6.**

Changes to classification and measurement

To determine their classification and measurement category, IFRS 9 requires all financial assets, except equity instruments and derivatives, to be assessed based on a combination of the entity's business model for managing the assets and the instruments' contractual cash flow characteristics.

The IAS 39 measurement categories of financial assets (fair value through profit or loss (FVPL), available for sale (AFS), held-to-maturity and amortised cost) have been replaced by:

- Debt instruments at amortised cost
- Debt instruments at fair value through other comprehensive income (FVOCI), with gains or losses recycled to profit or loss on derecognition
- Equity instruments at FVOCI, with no recycling of gains or losses to profit or loss on derecognition
- Financial assets FVPL

The accounting for financial liabilities remains largely the same as it was under IAS 39, except for the treatment of gains or losses arising from an entity's own credit risk relating to liabilities designated at FVPL. Such movements are presented in OCI with no subsequent reclassification to the income statement.

The Bank's classification of its financial assets and liabilities is explained in **Note 4.4.2.** The quantitative impact of applying IFRS 9 as at 1 January 2018 is disclosed in **Note 6**.

Changes to the impairment calculation

The adoption of IFRS 9 has fundamentally changed the Bank's accounting for loan loss impairments by replacing IAS 39's incurred loss approach with a forward-looking expected credit loss (ECL) approach. IFRS 9 requires the Bank to record an allowance for ECLs for all loans and other debt financial assets not held at FVPL, together with loan commitments and financial guarantee contracts. Under IFRS 9, no impairment loss is recognised on equity investments. The allowance is based on the ECLs associated with the probability of default in the next twelve months unless there has been a significant increase in credit risk since origination. If the financial asset meets the definition of purchased or originated credit impaired (POCI), the allowance is based on the change in the ECLs over the life of the asset.

Details of the Bank's impairment assessment are disclosed in Note **36.1.2**. The quantitative impact of applying IFRS 9 as at 1 January 2018 is disclosed in **Note 6**.

IFRS 7

To reflect the differences between IFRS 9 and IAS 39, IFRS 7 Financial Instruments: Disclosures was updated and the Bank has adopted it, together with IFRS 9, for the year beginning 1 January 2018. Changes include transition disclosures as shown in **Note 6**, detailed qualitative and quantitative information about the ECL calculations such as the assumptions and inputs used are set out in Note **36.1.2**.

Other new standards and amendments described below and applied for the first time in 2018, did not have a material impact on the annual financial statements of the Bank.

- *"Revenue from contracts with customers" (IFRS 15) and "Revenue from contracts with customer", Clarifications (Amendment to IFRS 15)*

- *"Share based payments" classification and measurement of share-based payment transactions (Amendment to IFRS 2)*
- *Annual Improvements to IFRSs 2014-2017 Cycle – Amendments to IFRS 1 and IAS 28*
- *Amendments to IAS 40 Investment Property: Transfers of Investment Property*
- *IFRIC 22 Foreign Currency Transactions and Advance Consideration.*

3.5 Standards and interpretations not yet applied by the Bank

At the date of authorization of these financial statements, certain new standards, amendments and interpretations to the existing Standards have been published but are not yet effective. The Bank has not early adopted any of these pronouncements.

Management anticipates that all of the pronouncements will be adopted in the Bank's accounting policy for the first period beginning after the effective date of the pronouncement.

Management does not anticipate a material impact on the Bank's financial statements from these Amendments, they are presented below.

IFRS 16 Leases

IFRS 16 will replace IAS 17 "Leases" and three related Interpretations. It completes the IASB's long running project to overhaul lease accounting. Leases will be recorded in the statement of financial position in the form of a right-of-use asset and a lease liability. There are two important reliefs provided by IFRS 16 for assets of low value and short-term leases of less than 12 months.

IFRS 16 is effective from periods beginning on or after 1 January 2019. Early adoption is permitted; however, the Bank have decided not to early adopt.

Management is in the process of assessing the full impact of the Standard. So far, the Bank:

- has decided to make use of the practical expedient not to perform a full review of existing leases and apply IFRS 16 only to new or modified contracts. As some leases will be modified or renewed in 2019, the Bank has reassessed these leases and concluded they will be recognised on the statement of financial position as a right-of-use asset
- believes that the most significant impact will be that the Bank will need to recognise a right of use asset and a lease liability for the office and production buildings currently treated as operating leases. At 31 December 2018 the future minimum lease payments amounted to AMD 44,715 thousand. This will mean that the nature of the expense of the above cost will change from being an operating lease expense to depreciation and interest expense.
- concludes that there will not be a significant impact to the finance leases currently held on the statement of financial position
- is implementing a new IT system that will facilitate to record lease contracts.

The Bank is planning to adopt IFRS 16 on 1 January 2019 using the Standard's modified retrospective approach. Under this approach the cumulative effect of initially applying IFRS 16 is recognised as an adjustment to equity at the date of initial application. Comparative information is not restated.

Choosing this transition approach results in further policy decisions the Bank need to make as there are several other transitional reliefs that can be applied. These relate to those leases previously held as operating leases and can be applied on a lease-by-lease basis. The Bank are currently assessing the impact of applying these other transitional reliefs.

IFRS 16 has not made any significant changes to the accounting for lessors, and therefore the Bank does not expect any changes for leases where they are acting as a lessor.

Other standards

- IFRIC 23 Uncertainty over Income Tax Treatments (effective from 1 January 2019),

- Amendment to IFRS 9 "Financial instruments"-Prepayment features with negative compensation (effective from 1 January 2019),
- Amendment to IAS 19 "Employee benefits" – Plan amendment, curtailment or settlement (effective from 1 January 2019),
- Annual Improvements to IFRSs 2015-2017 (effective from 1 January 2019).

4 Summary of significant accounting policies

The following significant accounting policies have been applied in the preparation of the financial statements. The accounting policies have been consistently applied.

4.1 Recognition of income and expenses

Revenue is recognized to the extent that it is probable that the economic benefits will flow to the Bank and the revenue can be reliably measured. Expense is recognized to the extent that it is probable that the economic benefits will flow from the Bank and the expense can be reliably measured. The following specific criteria must also be met before revenue is recognized:

The effective interest rate method

Under both IFRS 9 and IAS 39, interest income is recorded using the effective interest rate (EIR) method for all financial instruments measured at amortised cost, financial instruments designated at FVPL. Interest income on interest bearing financial assets measured at FVOCI under IFRS 9, similarly to interest bearing financial assets classified as available-for-sale or held to maturity under IAS 39 are also recorded by using the EIR method. The EIR is the rate that exactly discounts estimated future cash receipts through the expected life of the financial instrument or, when appropriate, a shorter period, to the net carrying amount of the financial asset.

The EIR (and therefore, the amortised cost of the asset) is calculated by taking into account any discount or premium on acquisition, fees and costs that are an integral part of the EIR. The Bank recognises interest income using a rate of return that represents the best estimate of a constant rate of return over the expected life of the loan. Hence, it recognises the effect of potentially different interest rates charged at various stages, and other characteristics of the product life cycle (including prepayments, penalty interest and charges).

If expectations regarding the cash flows on the financial asset are revised for reasons other than credit risk, the adjustment is booked as a positive or negative adjustment to the carrying amount of the asset in the balance sheet with an increase or reduction in interest income. The adjustment is subsequently amortised through Interest and similar income in the income statement.

Calculation of interest income and expense

In calculating interest income and expense, the effective interest rate is applied to the gross carrying amount of the asset (when the asset is not credit-impaired) or to the amortised cost of the liability.

However, for financial assets that have become credit-impaired subsequent to initial recognition, interest income is calculated by applying the effective interest rate to the net amortised cost of the financial asset. If the asset is no longer credit-impaired, then the calculation of interest income reverts to the gross basis.

For financial assets that were credit-impaired on initial recognition, interest income is calculated by applying the credit-adjusted effective interest rate to the amortised cost of the asset. The calculation of interest income does not revert to a gross basis, even if the credit risk of the asset improves.

For information on when financial assets are credit-impaired, see **Note 4.4.6.**

Fee and commission income

Loan origination fees for loans issued to customers are deferred (together with related direct costs) and recognised as an adjustment to the effective yield of the loans. Fees, commissions and other income and expense items are generally recorded on an accrual basis when the service has been provided. Portfolio and other management advisory and service fees are recorded based on the applicable service contracts. Asset management fees related to investment funds are recorded over the period the service is provided. The same

principle is applied for wealth management, financial planning and custody services that are continuously provided over an extended period of time.

Dividend income

Revenue is recognized when the Bank's right to receive the payment is established.

Net trading income

Net trading income comprises gains less losses related to trading assets and liabilities, and includes all realized and unrealized fair value changes, interest, dividends and foreign exchange differences related to trading assets and liabilities. Net trading income also includes gains less losses from trading in foreign currencies and is recognized in profit or loss when the corresponding service is provided.

4.2 Foreign currency

Transactions in foreign currencies are initially recorded in the functional currency rate ruling at the date of the transactions. Gains and losses resulting from the translation of trading assets are recognised in the statement of profit or loss and other comprehensive income in net trading income, while gains less losses resulting from translation of non-trading assets are recognized in the statement of income in other income or other expense. Monetary assets and liabilities denominated in foreign currencies are retranslated at the functional currency rate of exchange ruling at the balance sheet date.

Changes in the fair value of monetary securities denominated in foreign currency classified as investment securities at fair value through other comprehensive income (as available for sale before 01 January 2018) are analysed between translation differences resulting from changes in the amortised cost of the security and other changes in the carrying amount of the security. Translation differences related to changes in the amortised cost are recognised in profit or loss, and other changes in the carrying amount are recognised in the own equity.

Non-monetary items that are measured in terms of historical cost in a foreign currency are translated using the exchange rates as the dates of the initial transactions (applicable for the financial statements as of 31 December 2017). Non-monetary items measured at fair value in a foreign currency are translated using the exchange rates at the date when the fair value was determined. Translation differences on non-monetary items, such as equities held at fair value through profit or loss, are reported as part of the fair value gain or loss. Translation differences on non-monetary items, such as equities classified as equity investment in respect of which an election has been made to present subsequent changes in fair value in OCI (available-for-sale equity instruments before 1 January 2018) are included in the fair value reserve in equity.

Differences between the contractual exchange rate of a certain transaction and the prevailing average exchange rate on the date of the transaction are included in gains less losses from trading in foreign currencies in net trading income.

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

	31 December 2018	31 December 2017
AMD/1 US Dollar	483.75	484.10
AMD/1 EUR	553.65	580.10

4.3 Taxation

Income tax on the profit for the year comprises current and deferred tax. Income tax is recognized in the statement of profit or loss and other comprehensive income except to the extent that it relates to items recognized directly in equity, in which case it is recognized in equity.

Current tax is the expected tax payable on the taxable income for the year, using tax rates enacted or substantially enacted at the balance sheet date, and any adjustment to tax payable in respect of previous years. In the case when financial statements are authorized for issue before appropriate tax returns are submitted, taxable profits or losses are based on estimates. Tax authorities might have more stringent position in interpreting tax legislation and in reviewing tax calculations. As a result tax authorities might claim additional taxes for those transactions, for which they did not claim previously. As a result significant additional taxes,

fines and penalties could arise. Tax review can include 3 calendar years immediately preceding the year of a review. In certain circumstances tax review can include even more periods.

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

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

Deferred income tax is provided on temporary differences arising on investments in subsidiaries, associates and joint ventures, except where the timing of the reversal of the temporary difference can be controlled and it is probable that the temporary difference will not reverse in the foreseeable future.

The Republic of Armenia also has various operating taxes, which are assessed on the Bank's activities. These taxes are included as a component of other expenses in the statement of profit or loss and other comprehensive income.

4.4 Financial instruments

4.4.1 Recognition and initial measurement

The Bank initially recognises loans and advances, deposits, debt securities issued and subordinated liabilities on the date on which they are originated. All other financial instruments (including regular-way purchases and sales of financial assets) are recognised on the trade date, which is the date on which The Bank becomes a party to the contractual provisions of the instrument.

A financial asset or financial liability is measured initially at fair value plus, for an item not at FVTPL, transaction costs that are directly attributable to its acquisition or issue.

4.4.2 Classification

Financial assets – Policy applicable from 1 January 2018

On initial recognition, a financial asset is classified as measured at: amortised cost, FVOCI or FVTPL.

A financial asset is measured at amortised cost if it meets both of the following conditions and is not designated as at FVTPL:

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

A debt instrument is measured at FVOCI only if it meets both of the following conditions and is not designated as at FVTPL:

- the asset is held within a business model whose objective is achieved by both collecting contractual cash flows and selling financial assets; and
- the contractual terms of the financial asset give rise on specified dates to cash flows that are solely payments of principal and interest on the principal amount outstanding.

On initial recognition of an equity investment that is not held for trading, the Bank may irrevocably elect to present subsequent changes in fair value in OCI. This election is made on an investment-by-investment basis.

All other financial assets are classified as measured at FVTPL.

In addition, on initial recognition, the Bank may irrevocably designate a financial asset that otherwise meets the requirements to be measured at amortised cost or at FVOCI as at FVTPL if doing so eliminates or significantly reduces an accounting mismatch that would otherwise arise.

Business model assessment

The Bank makes an assessment of the objective of a business model in which an asset is held at a portfolio level because this best reflects the way the business is managed and information is provided to management. The information considered includes:

- the stated policies and objectives for the portfolio and the operation of those policies in practice. In particular, whether management's strategy focuses on earning contractual interest revenue, maintaining a particular interest rate profile, matching the duration of the financial assets to the duration of the liabilities that are funding those assets or realising cash flows through the sale of the assets;
- how the performance of the portfolio is evaluated and reported to the Bank's management;
- the risks that affect the performance of the business model (and the financial assets held within that business model) and how those risks are managed;
- how managers of the business are compensated – e.g. whether compensation is based on the fair value of the assets managed or the contractual cash flows collected; and
- the frequency, volume and timing of sales in prior periods, the reasons for such sales and its expectations about future sales activity. However, information about sales activity is not considered in isolation, but as part of an overall assessment of how the Bank's stated objective for managing the financial assets is achieved and how cash flows are realised.

Assessment whether contractual cash flows are solely payments of principal and interest (The SPPI test)

For the purposes of this assessment, 'principal' is defined as the fair value of the financial asset on initial recognition. 'Interest' is defined as consideration for the time value of money and for the credit risk associated with the principal amount outstanding during a particular period of time and for other basic lending risks and costs (e.g. liquidity risk and administrative costs), as well as profit margin. In assessing whether the contractual cash flows are solely payments of principal and interest, the Bank considers the contractual terms of the instrument. This includes assessing whether the financial asset contains a contractual term that could change the timing or amount of contractual cash flows such that it would not meet this condition. In making the assessment, the Bank considers:

- contingent events that would change the amount and timing of cash flows;
- leverage features;
- prepayment and extension terms;
- terms that limit the Bank's claim to cash flows from specified assets (e.g. non-recourse asset arrangements); and
- features that modify consideration of the time value of money – e.g. periodical reset of interest rates.

Reclassifications

Financial assets are not reclassified subsequent to their initial recognition, except in the period after the Bank changes its business model for managing financial assets. Financial liabilities are never reclassified.

Financial assets – Policy applicable before 1 January 2018

The Bank classified its financial assets into one of the following categories:

- loans and receivables;
- held to maturity;
- available-for-sale; and
- at FVTPL, and within this category as:

- held for trading; or
- designated as at FVTPL.

Financial liabilities

The Bank classifies its financial liabilities as measured at amortised cost or FVTPL.

4.4.3 Derecognition

Financial assets

The Bank derecognises a financial asset when the contractual rights to the cash flows from the financial asset expire (see also **Note 4.4.4**), or it transfers the rights to receive the contractual cash flows in a transaction in which substantially all of the risks and rewards of ownership of the financial asset are transferred or in which the Bank neither transfers nor retains substantially all of the risks and rewards of ownership and it does not retain control of the financial asset.

On derecognition of a financial asset, the difference between the carrying amount of the asset (or the carrying amount allocated to the portion of the asset derecognised) and the sum of (i) the consideration received (including any new asset obtained less any new liability assumed) and (ii) any cumulative gain or loss that had been recognised in OCI is recognised in profit or loss.

From 1 January 2018 any cumulative gain/loss recognised in OCI in respect of equity investment securities designated as at FVOCI is not recognised in profit or loss on derecognition of such securities. Any interest in transferred financial assets that qualify for derecognition that is created or retained by the Bank is recognised as a separate asset or liability.

The Bank enters into transactions whereby it transfers assets recognised on its statement of financial position, but retains either all or substantially all of the risks and rewards of the transferred assets or a portion of them. In such cases, the transferred assets are not derecognised. Examples of such transactions are securities lending and sale-and-repurchase transactions.

When assets are sold to a third party with a concurrent total rate of return swap on the transferred assets, the transaction is accounted for as a secured financing transaction similar to sale and repurchase transactions, because the Bank retains all or substantially all of the risks and rewards of ownership of such assets.

In transactions in which the Bank neither retains nor transfers substantially all of the risks and rewards of ownership of a financial asset and it retains control over the asset, the Bank continues to recognise the asset to the extent of its continuing involvement, determined by the extent to which it is exposed to changes in the value of the transferred asset.

In certain transactions, the Bank retains the obligation to service the transferred financial asset for a fee. The transferred asset is derecognised if it meets the derecognition criteria. An asset or liability is recognised for the servicing contract if the servicing fee is more than adequate (asset) or is less than adequate (liability) for performing the servicing.

Financial liabilities

The Bank derecognises a financial liability when its contractual obligations are discharged or cancelled, or expire.

4.4.4 Modifications of financial assets and financial liabilities

Financial assets

If the terms of a financial asset are modified, the Bank evaluates whether the cash flows of the modified asset are substantially different. If the cash flows are substantially different, then the contractual rights to cash flows from the original financial asset are deemed to have expired. In this case, the original financial asset is derecognised (see Note **4.4.3**) and a new financial asset is recognised at fair value.

Policy applicable from 1 January 2018

If the cash flows of the modified asset carried at amortised cost are not substantially different, then the modification does not result in derecognition of the financial asset. In this case, The Bank recalculates the gross carrying amount of the financial asset and recognises the amount arising from adjusting the gross carrying amount as a modification gain or loss in profit or loss. If such a modification is carried out because of financial difficulties of the borrower (see Note **4.4.6**), then the gain or loss is presented together with impairment losses. In other cases, it is presented as interest income.

Policy applicable before 1 January 2018

If the terms of a financial asset were modified because of financial difficulties of the borrower and the asset was not derecognised, then impairment of the asset was measured using the pre-modification interest rate.

Financial liabilities

The Bank derecognises a financial liability when its terms are modified and the cash flows of the modified liability are substantially different. In this case, a new financial liability based on the modified terms is recognised at fair value. The difference between the carrying amount of the financial liability extinguished and the new financial liability with modified terms is recognised in profit or loss.

4.4.5 Offsetting

Financial assets and liabilities, and income and expenses, are offset and the net amount reported in the financial statements when there is a legally enforceable right to set off the recognised amounts and there is an intention to settle on a net basis, or realise the asset and settle the liability simultaneously.

Income and expenses are presented on a net basis only when permitted under IFRS, or for gains and losses arising from a group of similar transactions such as in the Bank's trading activity.

4.4.6 Impairment

Policy applicable from 1 January 2018

The Bank assesses on a forward-looking basis the expected credit losses ('ECL') on the following financial instruments that are not measured at FVTPL:

- financial assets measured at amortised cost
- financial assets measured at fair value through other comprehensive income
- lease receivables
- loan commitments to provide a loan
- financial guarantee contracts

No impairment loss is recognised on equity investments.

The Bank measures loss allowances at an amount equal to lifetime ECL, except for the following, for which they are measured as 12-month ECL:

- debt investment securities that are determined to have low credit risk at the reporting date; and
- other financial instruments on which credit risk has not increased significantly since their initial recognition.

The Bank considers a debt security to have low credit risk when their credit risk rating is equivalent to the globally understood definition of 'investment grade.

12-month ECL (12mECLs) are the portion of ECL that result from default events on a financial instrument that are possible within the 12 months after the reporting date.

Lifetime expected credit losses (LTECLs) are the expected credit losses that result from all possible default events over the expected life of a financial instrument.

Measurement of ECL

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

The Bank has established a policy to perform an assessment, at the end of each reporting period, of whether a financial instrument's credit risk has increased significantly since initial recognition, by considering the change in the risk of default occurring over the remaining life of the financial instrument. This is further explained in Note **36.1.2**.

Based on the above process, The Bank groups its financial instruments into Stage 1, Stage 2, Stage 3 and POCI, as described below:

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

Expected credit losses are the discounted product of the Probability of Default (PD), Exposure at Default (EAD), and Loss Given Default (LGD), defined as follows:

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

The PD, the EAD and the LGD are further explained in Note **36.1.2**.

Restructured financial assets

If the terms of a financial asset are renegotiated or modified or an existing financial asset is replaced with a new one due to financial difficulties of the borrower, then an assessment is made of whether the financial asset should be derecognised (see Note **4.4.4**) and ECL are measured as follows.

- If the expected restructuring will not result in derecognition of the existing asset, then the expected cash flows arising from the modified financial asset are included in calculating the cash shortfalls from the existing asset.
- If the expected restructuring will result in derecognition of the existing asset, then the expected fair value of the new asset is treated as the final cash flow from the existing financial asset at the time of its derecognition. This amount is included in calculating the cash shortfalls from the existing financial asset that are discounted from the expected date of derecognition to the reporting date using the original effective interest rate of the existing financial asset.

Credit-impaired financial assets

At each reporting date, The Bank assesses whether financial assets carried at amortised cost and debt financial assets carried at FVOCI are credit-impaired. A financial asset is 'credit-impaired' when one or more events that have a detrimental impact on the estimated future cash flows of the financial asset have occurred. Evidence that a financial asset is credit-impaired includes the following observable data:

- significant financial difficulty of the borrower or issuer;
- a breach of contract such as a default or past due event;
- the restructuring of a loan or advance by The Bank on terms that The Bank would not consider otherwise;
- it is becoming probable that the borrower will enter bankruptcy or other financial reorganisation; or
- the disappearance of an active market for a security because of financial difficulties.

A loan that has been renegotiated due to a deterioration in the borrower's condition is usually considered to be credit-impaired unless there is evidence that the risk of not receiving contractual cash flows has reduced significantly and there are no other indicators of impairment.

In making an assessment of whether an investment in sovereign debt is credit-impaired, The Bank considers the following factors.

- The market's assessment of creditworthiness as reflected in the bond yields.
- The rating agencies' assessments of creditworthiness.
- The country's ability to access the capital markets for new debt issuance.

Presentation of allowances for ECL in the statement of financial position

Allowances for ECL are presented in the statement of financial position as follows:

- financial assets measured at amortised cost: as a deduction from the gross carrying amount of the assets;
- debt instruments measured at FVOCI: no loss allowance is recognised in the statement of financial position because the carrying amount of these assets is their fair value. However, the loss allowance is disclosed and is recognised in the fair value reserve.
- loan commitments and financial guarantee contracts: generally, as a provision;
    - When estimating LTECLs for undrawn loan commitments, The Bank estimates the expected portion of the loan commitment that will be drawn down over its expected life. The expected cash shortfalls are discounted at an approximation to the expected EIR on the loan.
    - where a financial instrument includes both a drawn and an undrawn component, and The Bank cannot identify the ECL on the loan commitment component separately from those on the drawn component: The Group presents a combined loss allowance for both components. The combined amount is presented as a deduction from the gross carrying amount of the drawn component. Any excess of the loss allowance over the gross amount of the drawn component is presented as a provision;
    - The Bank's liability under each guarantee is measured at the higher of the amount initially recognised less cumulative amortisation recognised in the income statement, and the ECL provision. For this purpose, The Bank estimates ECLs based on the present value of the expected payments to reimburse the holder for a credit loss that it incurs The shortfalls are discounted by the risk-adjusted interest rate relevant to the exposure. The ECLs related to financial guarantee contracts are recognised within Provisions.

Write-offs

Loans and debt securities are written off (either partially or in full) when there is no realistic prospect of recovery. This is generally the case when The Bank determines that the borrower does not have assets or sources of income that could generate sufficient cash flows to repay the amounts subject to the write-off. However, financial assets that are written off could still be subject to enforcement activities in order to comply with the Bank's procedures for recovery of amounts due.

Policy applicable before 1 January 2018

Assets carried at amortized cost

A financial asset or a group of financial assets is impaired and impairment losses are incurred only if there is objective evidence of impairment as a result of one or more events that occurred after the initial recognition of

the asset ("loss event") and that loss event (or events) has an impact on the estimated future cash flows of the financial asset or group of financial assets that can be reliably estimated.

Criteria used to determine that there is objective evidence of an impairment loss may include indications that the borrower or a group of borrowers is experiencing significant financial difficulty (for example, equity ratio, net income percentage of sales), default or delinquency in interest or principal payments, breach of loan covenants or conditions, deterioration in the value of collateral, the probability that they will enter bankruptcy or other financial reorganization and where observable data indicate that there is a measurable decrease in the estimated future cash flows, such as changes in arrears or economic conditions that correlate with defaults.

The Bank first assesses whether objective evidence of impairment exists individually for financial assets that are individually significant, and individually or collectively for financial assets that are not individually significant. If it is determined that no objective evidence of impairment exists for an individually assessed financial asset, whether significant or not, the asset is included in a group of financial assets with similar credit risk characteristics and that group of financial assets is collectively assessed for impairment. Assets 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.

If there is objective evidence that an impairment loss on financial assets carried at amortised cost has been incurred, the amount of the loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows (excluding future credit losses that have not been incurred) discounted at the financial asset's original effective interest rate (i.e. the effective interest rate computed at initial recognition). The carrying amount of the asset shall be reduced through use of an allowance account. The amount of the loss shall be recognised in the statement of profit or loss and other comprehensive income. If a loan or held-to-maturity investment has a variable interest rate, the discount rate for measuring any impairment loss is the current effective interest rate determined under the contract. The Bank may measure impairment on the basis of an instrument's fair value using an observable market price.

The calculation of the present value of the estimated future cash flows of a collateralised financial asset reflects the cash flows that may result from foreclosure less costs for obtaining and selling the collateral, whether or not the foreclosure is probable.

For the purpose of a collective evaluation of impairment, financial assets are grouped on the basis of the Bank's internal credit grading system that considers credit risk characteristics such as asset type, industry, geographical location, collateral type, past-due status and other relevant factors.

Future cash flows in a group of financial assets that are collectively evaluated for impairment are estimated on the basis of the contractual cash flows of the assets in The Bank and historical loss experience for assets with credit risk characteristics similar to those in the group. Historical loss experience is adjusted on the basis of current observable data to reflect the effects of current conditions that did not affect the period on which the historical loss experience is based and to remove the effects of conditions in the historical period that do not currently exist.

Estimates of changes in future cash flows for groups of assets should reflect and be directionally consistent with changes in related observable data from period to period (for example, changes in unemployment rates, property prices, payment status, or other factors indicative of changes in the probability of losses in The Bank and their magnitude). The methodology and assumptions used for estimating future cash flows are reviewed regularly by the Bank to reduce any differences between loss estimates and actual loss experience.

Loans together with the associated allowance are written off when there is no realistic prospect of future recovery and all collateral has been realized or has been transferred to the Bank. If, in a subsequent year, the amount of the estimated impairment loss increases or decreases because of an event occurring after the impairment was recognized, the previously recognized impairment loss is increased or reduced by adjusting the allowance account. If future write-off is later recovered, the recovery is credited to the allowance account.

Impairment allowances of financial assets have been identified in the financial statements on the basis of existing economic conditions. Bank is not able to predict how conditions may change in Armenia, and what impact these changes may have on the adequacy of the impairment allowance of financial assets in future periods.

Renegotiated loans

Where possible, the Bank seeks to restructure loans rather than to take possession of collateral. This may involve extending the payment arrangements and the agreement of new loan conditions. Once the terms have been renegotiated, the loan is no longer considered past due. Management continuously reviews renegotiated loans to ensure that all criteria are met and that future payments are likely to occur. The loans continue to be subject to an individual or collective impairment assessment, calculated using the loan's original effective interest rate.

Available-for-sale financial assets

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

4.5 Cash and cash equivalents

Cash and cash equivalents comprise cash on hand, balances on correspondent accounts with the Central Bank of Armenia (excluding those funds deposited for the settlement of ArCa payment cards), and amounts due from other banks, which can be converted into cash at short notice, including highly liquid investments maturing within 90 days from the date of acquisition that are readily convertible into known amounts of cash and which are subject to an insignificant risk of changes in value.

Cash and cash equivalents are carried at amortised cost.

4.6 Amounts due from financial institutions

In the normal course of business, the Bank maintains advances or deposits for various periods of time with other banks. Loans and advances to banks with a fixed maturity term are subsequently measured at amortized cost using the effective interest method. Those that do not have fixed maturities are carried at amortized cost based on maturities estimated by management. Amounts due from financial institutions are carried net of any allowance for impairment losses.

4.7 Trading assets and liabilities

"Trading assets and liabilities" are those assets and liabilities that the Bank acquires or incurs principally for the purpose of selling or repurchasing in the near term, or holds as part of a portfolio that is managed together for short-term profit or position taking. Trading assets and liabilities are initially recognised and subsequently measured at fair value in the statement of financial position, with transaction costs recognised in profit or loss. All changes in fair value are recognised as part of net trading income in profit or loss.

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

4.8 Loans

Loans are financial assets with fixed or determinable payments, which arise when the Bank provides money directly to a debtor with no intention of trading the receivable.

Loans granted by the Bank with fixed maturities are initially recognized at fair value plus related transaction costs. Where the fair value of consideration given does not equal the fair value of the loan, for example where

the loan is issued at lower than market rates, the difference between the fair value of consideration given and the fair value of the loan is recognized as a loss on initial recognition of the loan and included in the statement of profit or loss and other comprehensive income as losses on origination of assets. Subsequently, the loan carrying value is measured using the effective interest method. Loans to customers that do not have fixed maturities are accounted for under the effective interest method based on expected maturity. Loans to customers are carried net of any allowance for impairment losses.

4.9 Investment securities

Policy applicable from 1 January 2018

The 'investment securities' caption in the statement of financial position includes:

- debt investment securities measured at amortised cost; these are initially measured at fair value plus incremental direct transaction costs, and subsequently at their amortised cost using the effective interest method;
- debt and equity investment securities mandatorily measured at FVTPL or designated as at FVTPL; these are at fair value with changes recognised immediately in profit or loss;
- debt securities measured at FVOCI; and
- equity investment securities designated as at FVOCI.

For debt securities measured at FVOCI, gains and losses are recognised in OCI, except for the following, which are recognised in profit or loss in the same manner as for financial assets measured at amortised cost:

- interest revenue using the effective interest method;
- ECL and reversals; and
- foreign exchange gains and losses.

When debt security measured at FVOCI is derecognised, the cumulative gain or loss previously recognised in OCI is reclassified from equity to profit or loss.

The Bank elects to present in OCI changes in the fair value of certain investments in equity instruments that are not held for trading. The election is made on an instrument-by-instrument basis on initial recognition and is irrevocable.

Gains and losses on such equity instruments are never reclassified to profit or loss and no impairment is recognised in profit or loss. Dividends are recognised in profit or loss unless they clearly represent a recovery of part of the cost of the investment, in which case they are recognised in OCI. Cumulative gains and losses recognised in OCI are transferred to retained earnings on disposal of an investment.

Policy applicable before 1 January 2018

Investment securities were initially measured at fair value plus, incremental direct transaction costs, and subsequently accounted as available-for-sale.

Available-for-sale financial assets

Assets available for sale represent debt and equity assets that are intended to be held for an indefinite period of time, which may be sold in response to needs for liquidity or changes in interest rates, exchange rates or equity prices. After initial recognition available-for sale financial assets are measured at fair value with gains or losses being recognised as a separate component of other comprehensive income until the investment is derecognised or until the investment is determined to be impaired at which time the cumulative gain or loss previously reported in equity is included in the statement of profit or loss and other comprehensive income. However, interest calculated using the effective interest method is recognised in the statement of profit or loss and other comprehensive income. Dividends on available-for-sale equity instruments are recognised in profit or loss when the Bank's right to receive payment is established.

The fair value of investments that are actively traded in organised financial markets is determined by reference to quoted market bid prices at the close of business on the balance sheet date. For investments where there is no active market, fair value is determined using valuation techniques. Such techniques include using recent

arm's length market transactions, reference to the current market value of another instrument, which is substantially the same and discounted cash flow analysis. Otherwise the investments are stated at cost less any allowance for impairment.

4.10 Repurchase and reverse repurchase agreements

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

Securities purchased under agreements to resell ("reverse repo") are recorded as amounts due from financial institutions or loans and advances to customers as appropriate and are not recognized in the statement of financial position. The difference between sale and repurchase price is treated as interest and accrued over the life of repo agreements using the effective yield method.

If assets purchased under an agreement to resell are sold to third parties, the obligation to return the securities is recorded as a trading liability and measured at fair value.

4.11 Securities lending and borrowing

Securities lending and borrowing transactions are usually collateralised by securities or cash. The transfer of the securities to counterparties is only reflected in the statement of financial position if the risks and rewards of ownership are also transferred. Cash advanced or received as collateral is recorded as an asset or liability.

Securities borrowed are not recognized in the statement of financial position, unless they are sold to third parties, in which case the obligation to return the securities is recorded as a trading liability and measured at fair value with any gains or losses included in "Net trading income".

4.12 Leases

Operating - Bank as lessee

Leases of assets under which the risks and rewards of ownership are effectively retained by the lessor are classified as operating leases. Lease payments under an operating lease are recognised as expenses on a straight-line basis over the lease term and included in other operating expenses.

4.13 Precious metals

Gold and other precious metals are recorded at CBA prices which approximate fair values and are quoted according to London Bullion Market rates. Precious metals are included in other assets in the statement of financial position.

Changes in the bid prices are recorded in net gain/loss on operations with precious metals in other income/expense.

4.14 Property and equipment

Property and equipment are recorded at historical cost less accumulated depreciation. The Bank's buildings are stated at fair value less accumulated depreciation. If the recoverable value of property and equipment is lower than its carrying amount, due to circumstances not considered to be temporary, the respective asset is written down to its recoverable value. Land is carried at historical cost. It has unlimited useful life and thus is not depreciated.

Depreciation is calculated using the straight-line method based on the estimated useful life of the asset. The following depreciation rates have been applied:

	Useful life (years)	Rate (%)
Buildings	30	3.3
Computers	3	33.3
ATMs	10	10
Vehicles	5	20
Office equipment	5	20
Other fixed assets	5	20

Leasehold improvements are capitalized and depreciated over the shorter of the lease term and their useful lives on a straight-line basis. Assets under the course of construction are accounted based on actual expenditures less any impairment losses. Upon completion of construction assets are transferred to property plant and equipment and accounted at their carrying amounts. Assets under the course of construction are not depreciated until they are ready for usage.

Repairs and maintenance are charged to the statement of profit or loss and other comprehensive income during the period in which they are incurred. The cost of major renovations is included in the carrying amount of the asset when it is incurred and when it satisfies the criteria for asset recognition. Major renovations are depreciated over the remaining useful life of the related asset.

Gains and losses on disposals are determined by comparing proceeds with carrying amount and are included in operating profit.

Buildings are revalued on a regular basis. The frequency of revaluation depends on changes in fair value of assets. In case of significant divergences between fair value of revalued assets and their carrying amounts further revaluation is conducted. Revaluation is conducted for the whole class of property, plant and equipment.

Any revaluation surplus is credited to the revaluation reserve for property and equipment included in the revaluation reserve for property and equipment in equity section of the balance sheet, except to the extent that it reverses a revaluation decrease of the same asset previously recognised in the statement of income, in which case the increase is recognised in the statement of income. A revaluation deficit is recognised in the statement of income, except that a deficit directly offsetting a previous surplus on the same asset is directly offset against the surplus in the revaluation reserve for property and equipment.

In case of sale or write-off of fixed assets the balance relating to revaluation reserve of that fixed assets is totally transferred to retained earnings.

4.15 Intangible assets

Intangible assets include computer software, licences and other.

Intangible assets acquired separately are measured on initial recognition at cost. Following initial recognition, intangible assets are carried at cost less any accumulated amortisation and any accumulated impairment losses. The useful lives of intangible assets are assessed to be either finite or indefinite. Intangible assets with finite lives are amortised on a straight-line basis over the useful economic lives and are assessed for impairment whenever there is an indication that the intangible asset may be impaired. Amortisation periods and methods for intangible assets with finite useful lives are reviewed at least at each financial year-end.

Intangible assets with indefinite useful lives are not amortised, but tested for impairment annually either individually or at the cash-generating unit level. The useful life of an intangible asset with an indefinite life is reviewed annually to determine whether indefinite life assessment continues to be supportable.

Costs associated with maintaining computer software programmes are recorded as an expense as incurred.

4.16 Repossessed assets

The Bank's policy is to determine whether a repossessed asset can be best used for its internal operations or should be sold. Assets determined to be useful for the internal operations are transferred to their relevant asset

category at the lower of their repossessed value or the carrying value of the original secured asset. Assets for which selling is determined to be a better option are transferred to assets held for sale at their fair value (if financial assets) and fair value less cost to sell for non-financial assets at the repossession date, in line with the Bank's policy.

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

4.17 Grants

Grants relating to the assets are included in other liabilities and are credited to the statement of profit or loss and other comprehensive income on a straight line basis over the expected lives of the related assets.

4.18 Borrowings

Borrowings, which include amounts due to the RA Central Bank and Government, amounts due to RA financial institutions and international financial institutions, debt securities issued, amounts due to customers are initially recognised at the fair value of the consideration received less directly attributable transaction costs. After initial recognition, borrowings are subsequently measured at amortised cost using the effective interest method. Gains and losses are recognised in the statement of profit or loss and other comprehensive income when the liabilities are derecognised as well as through the amortisation process.

If the Bank purchases its own debt, it is removed from the balance sheet and the difference between the carrying amount of the liability and the consideration paid is recognised in the statement of income.

4.19 Financial guarantees and loan commitments

"Financial guarantees" are contracts that require The Bank to make specified payments to reimburse the holder for a loss that it incurs because a specified debtor fails to make payment when it is due in accordance with the terms of a debt instrument. "Loan commitments" are firm commitments to provide credit under pre-specified terms and conditions.

Financial guarantees issued or commitments to provide a loan at a below-market interest rate are initially measured at fair value and the initial fair value is amortised over the life of the guarantee or the commitment. Subsequently, they are measured as follows:

- from 1 January 2018: at the higher of this amortised amount and the amount of loss allowance; and
- before 1 January 2018: at the higher of this amortised amount and the present value of any expected payment to settle the liability when a payment under the contract has become probable.

Liabilities arising from financial guarantees are included in provisions in "Other liabilities". Losses arising on loan commitments are included within provisions of "Loans to customers" in note 18.

4.20 Provisions

Provisions are recognised when the Bank has a present legal or constructive obligation as a result of past events, and it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation and a reliable estimate of the amount of obligation can be made. Provisions also include liabilities arising from financial guarantees and loan commitments as provided in Note **4.19**.

4.21 Equity

Share capital

Ordinary shares and non-redeemable preference shares with discretionary dividends are both classified as equity. External costs directly attributable to the issue of new shares, other than on a business combination, are shown as a deduction from the proceeds in equity. Any excess of the fair value of consideration received over the par value of shares issued is recognised as additional paid-in capital.

Retained earnings

Include accumulated earnings of current and previous periods.

Dividends

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

Property revaluation surplus

The property revaluation surplus is used to record increases in the fair value of buildings and decreases to the extent that such decrease relates to an increase on the same asset previously recognised in equity.

Fair value reserve for investments securities at FVOCI

This reserve records fair value changes in investment securities at fair value through other comprehensive income.

5 Critical accounting estimates and judgements

The preparation of financial statements in conformity with IFRS requires management to make judgments, estimates and assumptions that affect the application of policies and the reported amounts of assets and liabilities, income and expense. The estimates and associated assumptions are based on historical experience and various other factors that are believed to be reasonable under the circumstances, the results of which form the basis of making the judgements about carrying values of assets and liabilities that are not readily apparent from other sources. Although these estimates are based on management's best knowledge of current events and actions, actual results ultimately may differ from these estimates.

The most significant areas of judgements and estimates with regards to these financial statements are presented below:

Business models and SPPI

The Bank assesse of the business model within which the assets are held and assesse of whether the contractual terms of the financial asset are solely payments of principal and interest on the principal amount outstanding (see Note **4.4.2**).

Measurement of fair values

Management uses valuation techniques to determine the fair value of financial instruments (where active market quotes are not available) and non-financial assets. This involves developing estimates and assumptions consistent with how market participants would price the instrument. Management bases its assumptions on observable data as far as possible but this is not always available. In that case management uses the best information available. Estimated fair values may vary from the actual prices that would be achieved in an arm's length transaction at the reporting date (see Note 33).

Useful Life of property and equipment

Useful life evaluation of property and equipment is the result of judgement, based on the experience with similar assets. Future economic benefits are embodied in assets and mainly consumed along with usage. However, such factors as operational, technical or commercial depreciation often lead to decrease of asset's economic benefit. Management evaluates the remaining useful life according to the asset's current technical condition and estimated period, during which the Bank expects to receive benefits. For the evaluation of remaining useful life are considered the following main factors: expectable usage of assets, depending on the operational factors and maintenance program, that is depreciation and technical and commercial depreciation arising from the changes in the market conditions.

Related party transactions

In the normal course of business, the Bank enters into transactions with its related parties. These transactions are priced predominantly at market rates. Judgement is applied in determining if transactions are priced at market or non-market interest rates, where there is no active market for such transactions. The basis for

judgement is pricing for similar types of transactions with unrelated parties and effective interest rate analysis (see Note 32).

Impairment of financial instruments

The Bank assess of whether credit risk on the financial asset has increased significantly since initial recognition and incorporation of forward-looking information in the measurement of ECL (see Note **36.1.2**), as well as the key assumptions used in estimating recoverable cash flows (see Note **4.4.6**).

Tax legislation

Armenian tax legislation is subject to varying interpretations. See Note 31.

6 Transition disclosure

The following set out the impact of adopting IFRS 9 on the statement of financial position, and retained earnings including the effect of replacing IAS 39's incurred credit loss calculations with IFRS 9's ECLs.

The following table shows the original measurement categories in accordance with IAS 39 and the new measurement categories under IFRS 9 for the Bank's financial assets and financial liabilities as at 1 January 2018.

In thousand Armenian drams	Original classification under IAS 39	New classification under IFRS 9	Original carrying amount under IAS 39	New carrying amount under IFRS 9
Financial assets				
Cash and cash equivalents	Loans and receivables	Amortised cost	115,576,209	115,566,795
Amounts due from financial institutions	Loans and receivables	Amortised cost	14,036,722	13,957,218
Loans and advances to customers	Loans and receivables	Amortised cost	382,547,013	381,309,320
Investment securities – debt	Available for sale	FVOCI	16,883,709	16,883,709
Investment securities - equity	Available for sale	FVOCI	24,028	24,028
Other financial assets	Loans and receivables	Amortised cost	1,031,725	941,971
Total financial assets			530,099,406	528,683,041
Financial liabilities				
Amounts due to financial institutions	Amortised cost	Amortised cost	76,004,421	76,004,421
Financial liabilities held for trading	FVTPL	FVTPL	24,556,156	24,556,156
Amounts due to RA Government	Amortised cost	Amortised cost	692,952	692,952
Amounts due to customers	Amortised cost	Amortised cost	398,967,148	398,967,148
Debt securities issued	Amortised cost	Amortised cost	8,967,294	8,967,294
Other financial liabilities	Amortised cost	Amortised cost	740,658	740,658
Total financial liabilities			509,928,629	509,928,629

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

In thousand Armenian drams	IAS 39 carrying amount 31 December 2017	Reclassifi-cation	Remeasure-ment /ECL/	IFRS 9 carrying amount 1 January 2018
Financial assets				
Amortised cost				
Cash and cash equivalents				
Opening balance	115,576,209			
Remeasurement		-	(9,414)	
Closing balance				115,566,795
Amounts due from financial institutions				
Opening balance	14,036,722			
Remeasurement		-	(79,504)	
Closing balance				13,957,218
Loans and advances to customers				
Opening balance	382,547,013			
Remeasurement		-	(1,237,693)	
Closing balance				381,309,320
Other financial assets				
Opening balance	1,031,725			
Remeasurement		-	(89,754)	
Closing balance				941,971
Total amortised cost	513,191,669	-	(1,416,365)	511,775,304
Available-for-sale				
Investment securities				
Opening balance	16,907,737			
To FVOCI – Equity		(24,028)	-	
To FVOCI – Debt		(16,883,709)	-	
Closing balance				-
Investment securities measured at FVOCI – debt				
Opening balance	-			
From available for sale securities		16,883,709	-	
Closing balance				16,883,709
Investment securities measured at FVOCI – equity				
Investment securities				
Opening balance	-			
From available-for-sale		24,028	-	
Closing balance				24,028
Total FVTPL	-	16,907,737	-	16,907,737

In thousand Armenian drams	IAS 39 carrying amount 31 December 2017	Reclassifi-cation	Remeasure-ment /ECL/	IFRS 9 carrying amount 1 January 2018
Financial liabilities				
Amortised cost				
Amounts due to financial institutions	76,004,421	-	-	76,004,421
Amounts due to RA Government	692,952	-	-	692,952
Amounts due to customers	398,967,148	-	-	398,967,148
Debt securities issued	8,967,294	-	-	8,967,294
Other financial liabilities	740,658	-	-	740,658
Total amortised cost	485,372,473	-	-	485,372,473
FVTPL				
Financial liabilities held for trading	24,556,156	-	-	24,556,156
Total FVTPL	24,556,156	-	-	24,556,156

The impact of transition to IFRS 9 on reserves and retained earnings is, as follows.

In thousand Armenian drams	Reserves and retained earnings
Fair value reserve	
Closing balance under IAS 39 (31 December 2017)	2,009,246
Recognition of expected credit losses under IFRS 9 for debt financial assets at FVOCI	11,226
Opening balance under IFRS 9 (1 January 2018)	2,020,472
Retained earnings	
Closing balance under IAS 39 (31 December 2017)	2,290,604
Recognition of IFRS 9 ECLs including those measured at FVOCI (see below)	(2,388,999)
Deferred tax in relation to the above	475,556
Opening balance under IFRS 9 (1 January 2018)	377,161
Total change in equity due to adopting IFRS 9	(1,902,217)

The following table reconciles:

- the closing impairment allowance for financial assets in accordance with IAS 39 as at 31 December 2017;
- the opening ECL allowance determined in accordance with IFRS 9 as at 1 January 2018.

In thousand Armenian drams	Loan loss provision under IAS 39 at 31 December 2017	Remeasurement	ECLs under IFRS 9 at 1 January 2018
Impairment allowance for			
Loans and receivables per IAS 39/financial assets at amortised cost under IFRS 9	(10,029,568)	(1,416,365)	(11,445,933)
Available-for-sale debt investment securities per IAS 39/debt financial assets at FVOCI under IFRS 9	-	(11,226)	(11,226)
	(10,029,568)	(1,427,591)	(11,457,159)
Financial guarantee contracts issued	-	(961,408)	(961,408)
	-	(961,408)	(961,408)
Total impairment allowance	(10,029,568)	(2,388,999)	(12,418,567)

7 Interest and similar income and expense

In thousand Armenian drams	2018	2017
Loans to customers	37,998,732	31,533,456
Investment securities at FVOCI (2017 available-for-sale)	1,376,707	1,666,094
Amounts due from financial institutions	735,382	576,362
Reverse repurchase transactions	1,452,674	1,445,773
Interest accrued on individually impaired financial assets	-	40,219
Other interest income	-	864
Total interest and similar income	41,563,495	35,262,768
Amounts due to financial institutions	4,435,186	4,534,419
Repurchase transactions	1,045,022	173,078
Amounts due to RA Government	17,502	32,602
Amounts due to customers	26,617,926	23,537,124
Debt securities issued	860,102	97,593
Total interest and similar expense	32,975,738	28,374,816

8 Fee and commission income and expense

In thousand Armenian drams	2018	2017
Cash operations	996,392	295,641
Utility payments	20,747	28,975
Payment transactions/money transfers	1,487,794	904,142
Loan servicing	790,553	901,042
Plastic cards operations	1,073,462	867,359
Guarantees	356,346	268,675
Operations with securities	20,670	16,439
Other fees and commissions	3,529	-
Total fee and commission income	4,749,493	3,282,273
Payment transactions/money transfers	316,851	282,840
Cash operations	156,122	3,284
Plastic cards operations	825,747	565,024
Operations with securities	-	7,981
Operations with letters of credit	34,807	18,260
Other expenses	28,269	6,486
Total fee and commission expense	1,361,796	883,875

9 Net trading income

In thousand Armenian drams	2018	2017
Net income from foreign currency operations	2,050,726	1,450,704
Net gains/(losses) from foreign currency swap	57,618	(21,154)
Total net trading income	2,108,344	1,429,550

10 Other income

In thousand Armenian drams	2018	2017
Fines and penalties received	2,744,679	2,171,120
Insurance compensations	-	50
Income from grants	1,709	82
Income from sale of fixed assets	37	13,129
Income from sale of repossessed property	74,863	14,762
Income from closing of accounts	8,610	7,618
Income from extension of certificates	8,467	8,115
Income from loan and guarantee applications examination	14,405	34,145
Income from money transfers	85,226	68,992
Income from internet banking services	160,611	78,782
Income from vehicle technical screening coupons	51,544	50,154
Income from operations with precious metals	30,946	35,989
Other income	140,610	42,556
Total other income	3,321,707	2,525,494

11 Impairment losses/(reversal)

2018 In thousand Armenian drams	Note	12-month ECL	Lifetime ECL not credit-impaired	Lifetime ECL credit-impaired	Total 2018	Total 2017
Cash and cash equivalents	15	(3,329)	-	-	(3,329)	-
Amounts due from financial institutions	17	(21,226)	-	-	(21,226)	-
Loans to customers	18	215,353	232,840	7,234,624	7,682,817	3,105,599
Investment securities measured at FVOCI	19	(9)	-	-	(9)	-
Other assets	23	(97,749)	-	-	(97,749)	-
Financial guarantees and loan commitment	31	(107,421)	-	-	(107,421)	-
Total impairment losses/(reversal)		(14,381)	232,840	7,234,624	7,453,083	3,105,599

12 Personnel expenses

In thousand Armenian drams	2018	2017
Salary and other compensations of employees	3,949,275	3,619,093
Other expenses	1,350	7,784
Total staff costs	3,950,625	3,626,877

13 Other expenses

In thousand Armenian drams	2018	2017
Consulting and other services	17,390	111,355
Operating lease	271,711	184,310
Taxes, other than income tax, duties	369,929	310,128
Advertising costs	248,580	198,421
Insurance expenses	33,693	65,336
Representative expenses	52,578	46,760
Expenses on acquisition and issuance of plastic cards	58,703	51,045
Legal service expenses	30,292	-
Cash collection expenses	70,591	63,615
Administrative expenses	697,300	456,506
Loss from disposal of repossessed property	28,941	197,685
Repair and maintenance of tangible assets	360,691	383,108
Use and servicing expenses of computer programs	192,889	171,640
Communications	114,723	110,025
Security	196,288	179,943
Deposit guarantee fund expenses	748,918	997,683
Office supplies	93,739	91,996
Business trip expenses	161,246	130,185
Loan extension and repayment expenses	44,999	70,098
Payments to Financial system mediator	57,534	40,441
Penalties paid	13,116	677
Other expenses	14,137	10,836
Total other expense	3,877,988	3,871,793

14 Income tax expense

In thousand Armenian drams	2018	2017
Current tax expense	906,871	573,866
Deferred tax	(573,347)	(185,660)
Total income tax expense	333,524	388,206

The corporate income tax within the Republic of Armenia is levied at the rate of 20% (2017: 20%). Differences between IFRS and RA statutory tax regulations give rise to certain temporary differences between the carrying value of certain assets and liabilities for financial reporting purposes and for profit tax purposes. Deferred income tax is calculated using the principal tax rate of 20%.

Numerical reconciliation between the tax expenses and accounting profit is provided below:

In thousand Armenian drams	2018	Effective rate (%)	2017	Effective rate (%)
Profit before tax	1,186,044		1,668,400	
Income tax at the rate of 20%	237,209	20	333,680	20
Non-taxable income	(94,921)	(8)	(5,737)	-
Non-deductible expenses	210,133	18	90,303	5
Foreign exchange gains	(12,867)	(1)	(7,091)	-
Taxable income	68,376	6	(2,427)	-
Taxable expenses	-	-	(5,164)	-
Deductions arisen from payments to disabled workers	(74,406)	(6)	(15,358)	(1)
Income tax expense	333,524	29	388,206	24

Deferred tax calculation in respect of temporary differences:

In thousand Armenian drams	2017			Recognized in other comprehensive income	2018		
	Net	Impact of adopting IFRS 9	Recognized in profit or loss		Net	Deferred tax asset	Deferred tax liability
Cash and cash equivalents	-	1,883	(666)	-	1,217	1,217	-
Amounts due from financial institutions	-	15,901	(4,245)	-	11,656	11,656	-
Loans to customers	650,199	247,539	875,748	-	1,773,486	1,773,486	-
Investments in securities	(502,313)	-	-	(45,087)	(547,400)	-	(547,400)
Property and equipment	(200,726)	-	(87,327)	-	(288,053)	-	(288,053)
Other assets	(25,354)	17,951	(11,786)	-	(19,189)	-	(19,189)
Other liabilities	70,478	192,282	(198,377)	-	64,383	64,383	-
Deferred tax asset/(liability)	(7,716)	475,556	573,347	(45,087)	996,100	1,850,742	(854,642)

In thousand Armenian drams	2016	Recognized in profit or loss	Recognized in other comprehensive income	2017
Other liabilities	79,697	(9,219)	-	70,478
Loans to customers	431,214	218,985	-	650,199
Gross deferred tax asset	510,911	209,766	-	720,677
Other assets	(19,267)	(6,087)	-	(25,354)
Available for sale investments	(375,881)	-	(126,432)	(502,313)
Amortization of PPE	(82,530)	(340)	-	(82,870)
Revaluation of PPE	(100,177)	(17,679)	-	(117,856)
Total deferred tax liability	(577,855)	(24,106)	(126,432)	(728,393)
Net deferred tax liability	(66,944)	185,660	(126,432)	(7,716)

15 Cash and cash equivalents

In thousand Armenian drams	31 December 2018	31 December 2017
Cash on hand	7,076,916	7,036,940
Correspondent account with the CBA	109,194,765	54,978,114
Correspondent accounts with other banks	11,076,856	3,544,517
Deposits for less than 90 days	-	50,016,638
	127,348,537	115,576,209
Less loss allowance	(6,085)	-
Total cash and cash equivalents	127,342,452	115,576,209

As of 31 December 2018 correspondent account with Central Bank of Armenia represents the obligatory minimum reserve deposits with the CBA, which as of 31 December is computed at 2% (2017: 4%) of certain obligations of the Bank denominated in Armenian drams and 18% of certain obligations of the Bank, denominated in foreign currency and amounts to AMD 57,405,804 thousand (2017: 12%, AMD 49,315,192 thousand). There are no restrictions on the withdrawal of funds from the CBA, however, if minimum average requirement is not met, the Bank could be subject to penalties. Cash on hand, other money market placements, correspondent account and mandatory reserve deposits in the CBA are non-interest bearing.

As of 31 December 2018 the amounts of correspondent accounts with financial institutions in amounts of AMD 8,380,723 thousand (76%) (2017: AMD 3,048,341 thousand (86%)) were due from two commercial banks, which represent significant concentration.

An analysis of changes in the ECLs on cash and cash equivalents as follows:

In thousand Armenian drams	31 December 2018	31 December 2017
	12-month ECL	Total
Cash and cash equivalents		
ECL allowance as at 1 January 2018	9,414	-
Net remeasurement of loss allowance	(3,329)	-
Balance at 31 December	6,085	-

Non-cash transactions performed by the Bank during 2018 are represented by:

- repayment of AMD 651,231 thousand loan by obtaining ownership on repossessed collateral (2017: AMD 730,475 thousand)

16 Derivative financial instruments

Currency and interest rate swaps are commitments to exchange one set of cash flows for another. Swaps result in an economic exchange of currencies. The Bank's credit risk represents the potential cost to replace the swap contracts if counterparties fail to fulfil their obligation.

The aggregate contractual or notional amount of derivative financial instruments on hand, the extent to which instruments are favourable or unfavourable, and thus the aggregate fair values of derivative financial assets and liabilities, can fluctuate significantly from time to time.

The fair values of derivative instruments held are set out below.

In thousand Armenian drams	31 December 2018		
	Notional amount	Fair value of assets	Fair value of liabilities
Foreign exchange contracts			
Foreign exchange swap contracts	1,660,950	-	8,940
Total derivative financial instruments	1,660,950	-	8,940

17 Amounts due from financial institutions

In thousand Armenian drams	31 December 2018	31 December 2017
Deposited funds with CBA	210,000	120,000
Loans to financial institutions	10,388,946	6,357,818
Reverse sale-and-repurchase agreements	910,329	4,124,618
Deposited funds with other non-resident financial institutions	1,892,712	2,356,848
Other accounts	555,136	1,077,438
	13,957,123	14,036,722
Less loss allowance	(58,278)	-
Total amounts due from financial institutions	13,898,845	14,036,722

Deposited funds with the CBA include a guaranteed deposit for settlements via ArCa payment system.

Loans are not impaired or overdue.

As at 31 December 2018 the “Loans to financial institutions” in amounts of AMD 5,635,924 thousand (54%) were concentrated in two financial institution (2017: AMD 3,670,154 thousand (58%) were concentrated in one financial institutions).

As at 31 December 2018 the “Deposited funds in other non-resident financial institutions” clause include guarantee amounts provided by the Bank for its operations through Master Card payment system in the amount of AMD 317,093 thousand (2017: AMD 387,066 thousand), as well as frozen deposit placed by the Bank for membership to Visa payment system in the amount of AMD 226,235 thousand (2017: AMD 218,140 thousand), frozen amount for the received guarantee in amount of AMD 1,271,794 thousand (2017: AMD 1,669,330 thousand).

An analysis of changes in the ECLs on amount due from financial institutions as follows:

In thousand Armenian drams	31 December 2018	31 December 2017
	12-month ECL	Total
Amount due from financial institutions		
ECL allowance as at 1 January 2018	79,504	-
Net remeasurement of loss allowance	(21,226)	-
Balance at 31 December	58,278	-

18 Loans to customers

In thousand Armenian drams	31 December 2018			31 December 2017		
	Gross carrying amount	ECL allowance	Carrying amount	Gross carrying amount	Impairment allowance	Carrying amount
Mortgage and consumer lending						
Mortgage	11,768,956	(369,872)	11,399,084	12,823,767	(208,379)	12,615,388
Consumer lending	58,741,737	(4,936,274)	53,805,463	48,252,183	(3,489,053)	44,763,130
Commercial lending						
Reverse sale-and-repurchase agreements	22,646,535	(49,988)	22,596,547	20,847,485	-	20,847,485
Industry	53,554,417	(2,847,470)	50,706,947	36,553,879	(365,539)	36,188,340
Construction	46,958,509	(1,382,548)	45,575,961	47,574,623	(1,971,627)	45,602,996
Trading	118,802,871	(4,551,308)	114,251,563	107,048,226	(2,447,372)	104,600,854
Other	140,844,232	(3,553,896)	137,290,336	119,476,418	(1,547,598)	117,928,820
Total	453,317,257	(17,691,356)	435,625,901	392,576,581	(10,029,568)	382,547,013

The ECL allowance in these tables includes ECL on loan commitments for products such as credit cards and overdrafts, because the Bank cannot separately identify the ECL on the loan commitment component from those on the financial instrument component.

During the year ended 31 December 2018 the Bank obtained assets by taking possession of collateral for loans to customers. As of 31 December 2018 the carrying amount of such assets was AMD 3,566,477 thousand (2017: AMD 3,716,481 thousand) (see Note 22). The Bank is intended to sell these assets in a short period.

As of 31 December 2018 the weighted average effective interest rate on loans and advances to customers is 12.04% for loans in AMD (2017: 12.74%) and 10.41% for loans in USD and EUR (2017: 7.25%).

As of 31 December 2018, the Bank had a concentration of loans represented by AMD 148,789,266 thousand due from the ten largest third party entities and parties related with them (33% of gross loan portfolio) (2017: AMD 61,617,444 thousand or 16%). An allowance of AMD 2,858,161 thousand (2017: AMD 1,717,236 thousand).

An analysis of changes in ECL allowances in relation to mortgage and consumer lending and commercial lending are as follows.

In thousand Armenian drams				2018
	12-month ECL	Lifetime ECL not credit-impaired	Lifetime ECL credit-impaired	Total
Mortgage and consumer lending				
ECL allowance as at 1 January 2018	1,293,321	423,277	1,316,656	3,033,254
Changes due to financial assets recognised in opening balance that have:				
Transfer to 12-month ECL	15,691	(15,691)	-	-
Transfer to Lifetime ECL not credit-impaired	(8,505)	23,815	(15,310)	-
Transfer to Lifetime ECL credit-impaired	(45,506)	(146,527)	192,033	-
Net remeasurement of loss allowance	194,328	264,134	2,674,625	3,133,087
Recoveries	-	-	878,619	878,619
Amounts written off during the year	-	-	(1,738,814)	(1,738,814)
Balance at 31 December	1,449,329	549,008	3,307,809	5,306,146

In thousand Armenian drams				2018
	12-month ECL	Lifetime ECL not credit-impaired	Lifetime ECL credit-impaired	Total
Commercial lending				
ECL allowance as at 1 January 2018	3,096,902	731,345	4,405,760	8,234,007
Changes due to financial assets recognised in opening balance that have:				
Transfer to 12-month ECL	20,012	(20,012)	-	-
Transfer to Lifetime ECL not credit-impaired	(976)	976	-	-
Transfer to Lifetime ECL credit-impaired	(8,161)	(9,327)	17,488	-
Net remeasurement of loss allowance	21,025	(31,294)	4,559,999	4,549,730
Recoveries	-	-	101,711	101,711
Amounts written off during the year	-	-	(500,238)	(500,238)
Balance at 31 December	3,128,802	671,688	8,584,720	12,385,210

The increase in ECLs of the portfolio was driven by an increase in the gross size of the portfolio and movements between stages as a result of increases in credit risk and a deterioration in economic conditions. Further analysis of economic factors is outlined in Note **36.1.2.**

An analysis of the allowance for impairment losses under IAS 39 for loans and advances, by class, for the year to 31 December 2017 is, as follows:

In thousand Armenian drams			2017
	Mortgage and consumer lending	Commercial lending	Total
At 1 January 2017	1,293,063	6,234,766	7,527,829
Amounts written off	1,132,795	1,972,804	3,105,599
Charge for the year	153,775	1,076,607	1,230,382
Recoveries	(132,261)	(1,701,981)	(1,834,242)
At 31 December 2017	2,447,372	7,582,196	10,029,568
Individual impairment	216,655	147,787	364,442
Collective impairment	2,230,717	7,434,409	9,665,126
	2,447,372	7,582,196	10,029,568
Gross amount of loans individually determined to be impaired, before deducting any individually assessed impairment allowance	342,745	216,655	559,400

At 31 December 2018 and 2017 the estimated fair value of loans to customers approximates it carrying value. See Note 33.

Maturity analysis of loans to customers are disclosed in Note 35.

Credit, currency and interest rate analyses of loans to customers are disclosed in Note 36. The information on related party balances is disclosed in Note 32.

19 Investment securities

In thousand Armenian drams	31 December 2018	31 December 2017
Investment securities measured at FVOCI		
Investment securities measured at FVOCI – debt instruments	3,411,231	-
Investment securities designated as at FVOCI – equity investments	49,661	-
Available-for-sale investment securities	-	1,649,612
Total investment securities measured at FVOCI (2017 Available-for-sale)	3,460,892	1,649,612
Debt investment securities measured at FVOCI (2017 available-for-sale) pledged under repurchase agreements	9,145,216	15,258,125

An analysis of changes in the ECLs on debt investment securities measured at FVOCI, including pledged under repurchase agreements as follow:

In thousand Armenian drams	2018	2017
	12-month ECL	Total
ECL allowance as at 1 January 2018	11,226	-
Net remeasurement of loss allowance	(9)	-
Balance at 31 December	11,217	-

The above loss allowance is not recognised in the statement of financial position because the carrying amount of debt investment securities at FVOCI (2017: available-for-sale) is their fair value.

All debt securities have fixed coupons.

Investment securities measured at FVOCI (2017: available-for-sale) by effective interest rates and maturity date comprise:

In thousand Armenian drams	31 December 2018		31 December 2017	
	%	Maturity	%	Maturity
Government bonds	8.25-16.90	2019-2032	-	-
Corporate bonds	-	-	7.5-10.59	2018-2022

20 Property and equipment

In thousand Armenian drams	Land and buildings	Office equipment	Vehicles	Computers	Other fixed assets	Capital investments in leased assets	Total
Cost							
At 1 January 2017	8,357,430	570,005	231,570	3,482,535	1,264,857	204,175	14,110,572
Additions	31,783	42,783	73,398	361,485	319,557	96,861	925,867
Disposals	(221,941)	(130)	(87,949)	-	(632)	-	(310,652)
At 31 December 2017	8,167,272	612,658	217,019	3,844,020	1,583,782	301,036	14,725,787
Additions	4,100,700	29,984	73,791	299,172	224,202	30,907	4,758,756
Disposals	(859,078)	(11,483)	(47,224)	(118,922)	(36,509)	-	(1,073,216)
At 31 December 2018	11,408,894	631,159	243,586	4,024,270	1,771,475	331,943	18,411,327
Accumulated depreciation							
At 1 January 2017	872,427	472,148	186,344	2,417,005	876,590	29,062	4,853,576
Expenses for the year	301,400	30,751	22,608	322,137	136,185	6,778	819,859
Disposals	(3,402)	(111)	(82,531)	-	-	-	(86,044)
Adjustment	-	-	-	422	(422)	-	-
At 31 December 2017	1,170,425	502,788	126,421	2,739,564	1,012,353	35,840	5,587,391
Expenses for the year	313,681	24,405	20,909	238,775	71,816	9,529	679,115
Disposals	-	(11,039)	(23,792)	(103,240)	(33,238)	-	(171,309)
Reclassification	-	-	-	309	(309)	-	-
At 31 December 2018	1,484,106	516,154	123,538	2,875,408	1,050,622	45,369	6,095,197
Carrying amount							
At 31 December 2017	6,996,847	109,870	90,598	1,104,456	571,429	265,196	9,138,396
At 31 December 2018	9,924,788	115,005	120,048	1,148,862	720,853	286,574	12,316,130

Revaluation of assets

The buildings owned by the Bank were evaluated by an independent appraiser at 31 December 2013 using a combination of market, income and cost methods resulting in a revaluation of AMD 589,278 thousand. Management has based its estimate of the fair value of the buildings on the results of the independent appraisal.

For the fair value hierarchy of property and equipmentsee Note 33.3

The management believes that at 31 December 2018 the fair value of the buildings does not differ significantly from their revalued amounts.

If the net book value of buildings that would have been recognised under the historic cost, the revalued amounts will be presented as follows:

In thousand Armenian drams	31 December 2018	31 December 2017
Historic cost	7,194,583	7,194,583
Accumulated amortization	(1,357,501)	(1,081,817)
Revalued amount	5,837,082	6,112,766

Fully depreciated items

As at 31 December 2018 fixed assets included fully depreciated assets at cost in the amount of AMD 246,362 thousand (2017: AMD 128,232 thousand).

Fixed assets in the phase of installation

As at 31 December 2018 fixed assets included assets in the phase of installation in the amount of AMD 742,996 thousand (2017: AMD 751,911 thousand).

Restrictions on title of fixed assets

As at 31 December 2018 the Bank does not possess any fixed assets pledged as security for liabilities or whose title is otherwise restricted.

Contractual commitments

As at 31 December 2018 the Bank has not any contractual commitment in respect of acquisition of new property (2017: AMD 2,600,583 thousand in respect of purchased new head office of the Bank).

21 Intangible assets

In thousand Armenian drams	Licenses	Computer software	Capital investments	Other	Total
Cost					
At 1 January 2017	2,338,577	264,024	4,847	135,806	2,743,254
Additions	435,770	5,000	-	-	440,770
Disposals	(4,174)	-	-	-	(4,174)
At 31 December 2017	2,770,173	269,024	4,847	135,806	3,179,850
Additions	172,164	-	-	-	172,164
Disposals	(95,444)	-	-	-	(95,444)
At 31 December 2018	2,846,893	269,024	4,847	135,806	3,256,570
Accumulated amortisation					
At 1 January 2017	288,898	27,935	-	3,494	320,327
Amortisation charge	141,565	13,897	-	5,636	161,098
Disposals	(4,174)	-	-	-	(4,174)
At 31 December 2017	426,289	41,832	-	9,130	477,251
Amortisation charge	298,492	57,189	-	16,577	372,258
Disposals	(95,444)	-	-	-	(95,444)
At 31 December 2018	629,337	99,021	-	25,707	754,065
Carrying amount					
At 31 December 2017	2,343,884	227,192	4,847	126,676	2,702,599
At 31 December 2018	2,217,556	170,003	4,847	110,099	2,502,505

Contractual commitments

As of 31 December 2018 the Bank had a contractual commitment in respect of purchasing licenses in AMD 206,199 thousand (2017: AMD 309,299 thousand).

22 Repossessed assets

Details of non-financial assets obtained by the Bank during the year by taking possession of collateral held as security against loans and advances as at December 31 are shown below:

In thousand Armenian drams	31 December 2018	31 December 2017
Property	3,563,062	3,594,959
Other assets	3,415	121,522
Total repossessed assets	3,566,477	3,716,481

As of the date of repossession the collateral, it is measured at the lower of the carrying amount of outstanding loan commitment and fair value of realizable collateral.

The Bank's policy is to pursue timely realisation of the collateral in an orderly manner. The Bank generally does not use the non-cash collateral for its own operations. The assets are measured at the lower of their carrying amount and fair value less costs to sell.

23 Other assets

In thousand Armenian drams	31 December 2018	31 December 2017
Debtors and other receivables	1,440,094	1,031,725
Less loss allowance	(139,001)	-
Total other financial assets	1,301,093	1,031,725
Prepayments	1,024,660	1,209,767
Settlements with employees	-	30
Paintings	47,050	47,050
Future period expenses	17,583	22,648
Precious metals	154,475	115,135
Materials	318,529	389,360
Other	106,115	89,501
Total non-financial assets	1,668,412	1,873,491
Total other assets	2,969,505	2,905,216

An analysis of changes in the ECLs on other financial as follow:

In thousand Armenian drams	2018	2017
	ECL	Total
Other financial assets		
ECL allowance as at 1 January	89,754	-
Net remeasurement of loss allowance	(97,749)	-
Net recovery	146,996	-
Balance at 31 December	139,001	-

24 Amounts due to financial institutions

In thousand Armenian drams	31 December 2018	31 December 2017
Loans from financial institutions	34,783,231	38,585,043
Deposits from financial institutions	17,116,894	21,924,589
Current accounts of financial institutions	3,728,161	938,152
Correspondent accounts of other banks	1,577,823	708,760
Loans under repurchase agreements	7,790,070	13,847,877
Total amounts due to financial institutions	64,996,179	76,004,421

Loans and deposits from financial institutions have fixed interest rates.

As at 31 December 2018 loans from financial institutions in amount of AMD 19,078,298 thousand (55%) were due from 1 financial institution (2017: AMD 21,620,085 thousand (56%) were due from 1 financial institution).

As at 31 December 2018 the effective interest rates on amounts due to financial institutions was 8.63% for borrowings in AMD (2017: 8.82%) and 6.35% for borrowings in USD (2017: 3.03%).

25 Financial liabilities held for trading

In thousand Armenian drams	31 December 2018	31 December 2017
Repledged securities by repurchase agreements	23,230,915	24,556,156
Total financial liabilities held for trading	23,230,915	24,556,156

26 Amounts due to Government of the RA

In thousand Armenian drams	31 December 2018	31 December 2017
Current/Settlement accounts	208,880	89,421
Received loans	428,711	603,531
Total amounts due to Government of the RA	637,591	692,952

At 31 December 2018 loans received from the RA Government include loans received from “Rural finance facility-Project Implementation Unit State Institution” in the amount of AMD 352,643 thousand (2017: AMD 462,856 thousand) and “Millennium Challenge Account - Armenia” in the amount of AMD 10,614 thousand (2017: AMD 21,184 thousand), and within the scope of “Small and medium business loan project” of German-Armenian Fund in the amount of AMD 11,617 thousand (2017: AMD 69,241 thousand).

27 Amounts due to customers

In thousand Armenian drams	31 December 2018	31 December 2017
Corporate customers		
Current/Settlement accounts	131,905,739	66,460,012
Time deposits	33,434,612	50,957,236
	165,340,351	117,417,248
Retail customers		
Current/Demand accounts	38,577,398	22,614,470
Time deposits	269,288,048	258,935,430
	307,865,446	281,549,900
Total amounts due to customers	473,205,797	398,967,148

As at 31 December 2018 included in current accounts of corporate and individual customers are deposits amounting to AMD 29,974,151 thousand (2017: AMD 22,671,881 thousand) held as security against letters of credit issued and guarantees issued. The fair value of those deposits approximates the carrying amount.

At 31 December 2018 the aggregate balance of top ten customers of the Bank (including relating parties, see Note 32) amounts to AMD 110,292,567 thousand (2017: AMD 118,316,969 thousand) or 23.3% of total customer accounts (2017: 29.7%).

As of 31 December 2018 the effective interest rates on amounts due to customers ranged from 3.00-14.70% for amounts attracted in AMD (2017: from 0.08-16.04%) and from 0.10-10.00% for amounts attracted in USD and EUR (2017: from 0.08-15.47%).

The Bank has not had any defaults of principal, interest or other breaches with respect to its liabilities during the period (2017: either).

28 Debt securities issued

In thousand Armenian drams	31 December 2018	31 December 2017
Bonds	11,462,171	8,967,294
Total debt securities issued	11,462,171	8,967,294

As of 31 December 2018, the Bank had issued interest-bearing bonds with following terms:

Date of issue	Currency	Per value	Quantity	%	Maturity of bonds	Total nominal value
23.01.2017	AMD	10,000	10,000	14.0	23.01.2019	100,000,000
23.01.2017	USD	100	10,000	8.5	23.01.2019	1,000,000
05.12.2017	USD	100	172,000	7.5	07.12.2020	17,200,000
06.02.2018	USD	100	51,000	8.0	07.12.2022	5,100,000

The bonds of the Bank are listed in the NASDAQ OMX Armenia stock exchange.

The Bank has not repurchased any of its own debt during the year (2017: nil).

The Bank has not had any defaults of principal, interest or other breaches with respect to its liabilities during the period (2017: nil).

29 Other liabilities

In thousand Armenian drams	31 December 2018	31 December 2017
Accounts payables	317,667	456,041
Due to personnel	339,932	284,617
Total other financial liabilities	657,599	740,658
Tax payable, other than income tax	383,069	328,598
Revenues of future periods	848	587
Grants related to assets	-	1,709
Other operational liabilities	-	43
Provisions*	853,987	-
Other	2	129,881
Total other non-financial liabilities	1,237,906	460,818
Total other liabilities	1,895,505	1,201,476

Grants related to assets

In thousand Armenian drams	2018	2017
At 1 January	1,709	1,791
Recognition of income	(1,709)	(82)
At 31 December	-	1,709

*Provisions have been made in respect of costs arising from financial guarantees. An analysis of changes in the ECLs on loan commitments and financial guarantees see Note 31.

30 Equity

As of 31 December 2018 the Bank's registered and paid-in share capital was AMD 31,374,560 thousand (2017: AMD 31,374,560 thousand).

In accordance with the Bank's statues, the share capital consists of 41,120 ordinary shares, all of which have a par value of AMD 763 thousand each.

The respective shareholders as of 31 December 2018 may be specified as follows:

In thousand Armenian drams	31 December 2018		31 December 2017	
	Paid-in share capital	% of total paid-in capital	Paid-in share capital	% of total paid-in capital
Vitaly Grigoryants	29,805,832	95	31,374,560	100
Arsen Mikayelyan	1,568,728	5	-	-
	31,374,560	100	31,374,560	100

As of 31 December 2018, the Bank did not possess any of its own shares.

The holders of ordinary shares are entitled to receive dividends as declared and are entitled to one vote per share at annual and general meetings of the Bank.

During 2018 and 2017 the Bank had not increased its share capital.

Distributable among shareholders reserves equal the amount of retained earnings, determined according to the Armenian legislation. Non-distributable reserves are represented by a reserve fund, which is created as required by the statutory regulations, in respect of general banking risks, including future losses and other unforeseen risks or contingencies. The reserve has been created in accordance with the Bank's statutes that provide for the creation of a reserve for these purposes of not less than 15% of the Bank's share capital reported in statutory books.

31 Contingent liabilities and commitments

Tax and legal matters

The taxation system in Armenia 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. In the event of a breach of tax legislation, no liabilities for additional taxes, fines or penalties may be imposed by tax authorities once three years have elapsed from the date of the breach.

These circumstances may create tax risks in Armenia 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.

Management believes that the Bank has complied with all regulations and has completely settled all its tax liabilities.

Management also believes that the ultimate liability, if any, arising from legal actions and complaints taken against the Bank, will not have a material adverse impact on the financial condition or results of future operations of the Bank.

Loan commitment and financial guarantee

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

As of 31 December the nominal or contract amounts were:

In thousand Armenian drams	31 December 2018	31 December 2017
Undrawn loan commitments	31,687,504	20,719,108
Letters of credit	-	1,279,062
Guarantees	54,825,209	35,968,014
Undrawn overdrafts	495,672	330,148
Total commitments and contingent liabilities	87,008,385	58,296,332

An analysis of changes in the ECLs on financial guarantee is presented below. An analysis of changes in the ECLs on loan commitment is included in allowances of loans and advances to customers (Note 18).

In thousand Armenian drams	31 December 2018	31 December 2017
	12-month ECL	Total
Financial guarantees		
ECL allowance as at 1 January	961,408	-
Net remeasurement of loss allowance	(107,421)	-
Balance at 31 December	853,987	-

Operating lease commitments – Bank as a lessee

In the normal course of business, the Bank enters into commercial lease agreements for office equipment, head office and branch facilities.

The future aggregate minimum lease payments under non-cancellable operating leases are as follows:

In thousand Armenian drams	31 December 2018	31 December 2017
Not later than 1 year	44,715	41,412
Total operating lease commitments	44,715	41,412

Information on the Bank's capital commitments is disclosed in notes 20 and 21.

Insurance

The insurance industry in Armenia is in a developing state and many forms of insurance protection common in other parts of the world are not yet generally available.

As at 31 December 2018, the Bank has insured the truthfulness of employees, Bank's buildings and constructions, transit, forged checks, securities and money, Bank's branches and their contents, computer fraud, responsibility of directors and management, as well as professional liability.

Until the Bank obtains adequate insurance coverage, there is a risk that the loss or destruction of certain assets could have a material adverse effect on the Bank's operations and financial position

32 Transactions with related parties

In accordance with IAS 24 *Related Party Disclosures*, parties are considered to be related if one party has ability to control the other party or exercise significant influence over the other party in making financial or operational decisions. For the purpose of the present financial statements, related parties include shareholders, members of Bank's Management as well as other persons and enterprises related with and controlled by them respectively.

The ultimate controlling party of the Bank is the resident of the Russian Federation Vitally Grigoriyants.

A number of banking transactions are entered into with related parties in the normal course of business. These include loans, deposits and other transactions. These transactions were carried out on commercial terms and at market rates.

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

In thousand Armenian drams	2018		2017	
	Shareholders and parties related with them	**Associates and parties related with them**	**Shareholders and parties related with them**	**Associates and parties related with them**
Statement of financial position				
Amounts due from financial institutions				
At 1 January	-	3,876,021	-	2,936,745
Increase	909,459	-	-	12,555,692
Decrease	-	(3,876,021)	-	(11,616,416)
At 31 December, gross	909,459	-	-	3,876,021
Less: allowance for loan impairment	(2,407)	-	-	-
At 31 December	907,052	-	-	3,876,021
Loans to customers				
Loans outstanding at 1 January gross	755,630	3,871,486	-	456,661
Loans issued during the year	14,264,377	660,456	2,099,780	8,357,320
Loan repayments during the year	(7,476,325)	(4,203,174)	(1,344,150)	(4,942,495)
Loans outstanding at 31 December gross	7,543,682	328,768	755,630	3,871,486
Less: allowance for loan impairment	(294,204)	(12,822)	(12,090)	(61,944)
Loans outstanding at 31 December	7,249,478	315,946	743,540	3,809,542
Amounts due to financial institutions				
At 1 January	-	-	-	-
Increase	20,998,054	-	-	-
Decrease	(15,668,526)	-	-	-
At 31 December	5,329,528	-	-	-
Amounts due to customers				
Deposits at 1 January	5,837,319	3,464,117	801,556	771,411
Deposits received during the year	59,943,407	1,646,156	31,215,913	26,730,782
Deposits repaid during the year	(57,289,449)	(5,034,326)	(26,180,150)	(24,038,076)
Deposits at 31 December	8,491,277	75,947	5,837,319	3,464,117
Statement of profit or loss and other comprehensive income				
Interest income	281,130	29,501	25,131	298,647
Interest expense	994,699	4,253	247,209	596,047
Impairment charge/(reversal)	284,521	(49,122)	12,090	54,637

The loans issued to directors and other key management personnel (and close family members) are repayable from 6 months to 10 years and have interest rates of 5.5-24% (2017: 7-24%, 1-15 years). The loans advanced to the directors are collateralised by gold, real estate, cash and other property.

Compensation of key management personnel was comprised of the following:

In thousand Armenian drams	2018	2017
Salaries and bonuses	339,764	313,601
Total key management compensation	339,764	313,601

33 Fair value measurement

The Bank's Board determines the policies and procedures for both recurring fair value measurement, such as unquoted trading and available-for-sale securities, unquoted derivatives and for non-recurring measurement, such as assets held for sale.

External valuers are involved for valuation of significant assets, such as properties, trading and available-for-sale securities and derivatives. Involvement of external valuers is decided upon annually by the investment committee after discussion with and approval by the Bank's audit committee.

At each reporting date, the Board of the Bank analyses the movements in the values of assets and liabilities which are required to be re-measured or re-assessed as per the Bank's accounting policies. For this analysis, the Board of the Bank verifies the major inputs applied in the latest valuation by agreeing the information in the valuation computation to contracts and other relevant documents. The Board of the Bank, in conjunction with the Bank's external valuers, also compares each the changes in the fair value of each asset and liability with relevant external sources to determine whether the change is reasonable.

Financial and non-financial assets and liabilities measured at fair value in the statement of financial position are presented below. This hierarchy groups financial and non-financial assets and liabilities into three levels based on the significance of inputs used in measuring the fair value of the financial assets and liabilities. The fair value hierarchy has the following levels:

- Level 1: quoted prices (unadjusted) in active markets for identical assets or liabilities

- Level 2: inputs other than quoted prices included within Level 1 that are observable for the asset and liability, either directly (i.e. as prices) or indirectly (i.e. derived from prices)

- Level 3: inputs for the asset or liability that are not based on observable market data (unobservable inputs).

33.1 Financial instruments that are not measured at fair value

The table below presents the fair value of financial assets and liabilities not measured at their fair value in the statement of financial position and analyses them by the level in the fair value hierarchy into which teach fair value measurement is categorised.

In thousand Armenian drams					31 December 2018
	Level 1	Level 2	Level 3	Total fair values	Total carrying amount
Financial assets					
Cash and cash equivalents	-	127,342,452	-	127,342,452	127,342,452
Amounts due from financial institutions	-	13,898,845	-	13,898,845	13,898,845
Loans to customers	-	435,135,448	-	435,135,448	435,625,901
Other financial assets	-	1,301,093	-	1,301,093	1,301,093

In thousand Armenian drams					31 December 2018
	Level 1	Level 2	Level 3	Total fair values	Total carrying amount
Financial liabilities					
Amounts due to financial institutions	-	64,996,179	-	64,996,179	64,996,179
Amounts due to the RA Government	-	637,591	-	637,591	637,591
Amounts due to customers	-	473,205,797	-	473,205,797	473,205,797
Debt securities issued	-	11,462,171	-	11,462,171	11,462,171
Other financial liabilities	-	657,599	-	657,599	657,599

In thousand Armenian drams					31 December 2017
	Level 1	Level 2	Level 3	Total fair values	Total carrying amount
Financial assets					
Cash and cash equivalents	-	115,576,209	-	115,576,209	115,576,209
Amounts due from financial institutions	-	14,036,722	-	14,036,722	14,036,722
Loans to customers	-	382,547,013	-	382,547,013	382,547,013
Other financial assets	-	1,031,725	-	1,031,725	1,031,725
Financial liabilities					
Amounts due to financial institutions	-	76,004,421	-	76,004,421	76,004,421
Amounts due to the RA Government	-	692,952	-	692,952	692,952
Amounts due to customers	-	398,967,148	-	398,967,148	398,967,148
Debt securities issued	-	8,967,294	-	8,967,294	8,967,294
Other financial liabilities	-	740,658	-	740,658	740,658

Amounts due from and to financial institutions

For assets and liabilities maturing within one month, the carrying amount approximates fair value due to the relatively short-term maturity of these financial instruments. For the assets and liabilities maturing in over one month, the fair value was estimated as the present value of estimated future cash flows discounted at the appropriate year-end market rates, which are mainly the same as current interest rates.

Loans and advances to customers

The fair value of floating rate instruments is normally their carrying amount. The estimated fair value of fixed interest rate instruments is based on estimated future cash flows expected to be received discounted at current interest rates for new instruments with similar credit risk and remaining maturity. Discount rates used depend on credit risk of the counterparty and ranged from 5% to 24% per annum (2017: 5% to 24% per annum).

The fair value of the impaired loans is calculated based on expected cash flows from the sale of collateral. The value of collateral is based on appraisals performed by independent, professionally-qualified property appraisals.

Due to customers

The fair value of deposits from customers is estimated using discounted cash flow techniques, applying the rates that are offered for deposits of similar maturities and terms. The fair value of deposits payable on demand is the amount payable at the reporting date.

33.2 Financial instruments that are measured at fair value

In thousand Armenian drams				31 December 2018
	Level 1	**Level 2**	**Level 3**	**Total**
Financial assets				
Listed bonds	99,452	-	-	99,452
Unlisted bonds, including securities pledged under repurchase agreement	-	12,456,995	-	12,456,995
Unlisted equity instruments	-	49,661	-	49,661
Total	99,452	12,506,656	-	12,606,108
Financial liabilities				
Derivative financial liabilities	-	8,940	-	8,940
Financial liabilities held for trading	-	23,230,915	-	23,230,915
Total	-	23,239,855	-	23,239,855
Net fair value	99,452	(10,733,199)	-	(10,633,747)

In thousand Armenian drams				31 December 2017
	Level 1	**Level 2**	**Level 3**	**Total**
Financial assets				
Investments available for sale	-	1,625,584	-	1,625,584
Securities pledged under repurchase agreements	-	15,258,125	-	15,258,125
Total	-	16,883,709	-	16,883,709
Financial liabilities				
Financial liabilities held for trading	-	24,556,156	-	24,556,156
Total	-	24,556,156	-	24,556,156
Net fair value	-	(7,672,447)	-	(7,672,447)

The methods and valuation techniques used for the purpose of measuring fair value are unchanged compared to the previous reporting period.

Quoted investments

All the listed securities and bonds have been issued by publicly traded companies in Armenia.

Unquoted debt securities

The fair value of unquoted debt securities at FVOCI is measured using a valuation technique, which uses current market rates to discount future cash flows of the financial instruments.

Unquoted equity investments

For determining the fair value of unquoted equity instruments the Bank uses a combination of market and income approaches. The market approach and the income approach are common valuation techniques for equity investments that are not publicly traded. Under the market approach, the Bank uses prices and other relevant information generated by market transactions involving identical or comparable securities. Under the income approach, future amounts are converted into a single present amount (e.g. a discounted cash flows model). The market approach is preferred as the main inputs used are typically observable. In 2017 unquoted equity instruments were measured at cost and were therefore excluded from this disclosure.

Derivatives

Where derivatives are traded either on exchanges or liquid over-the-counter market the Bank uses the closing price at the reporting date.

Normally, the derivatives entered into by the Group are not traded in active markets. The fair values of these contracts are estimated using valuation techniques that maximises the use of observable market inputs, eg. market exchange rates (Level 2). Most derivatives entered into by the Bank are included in Level 2 and consist of foreign currency swap contracts.

33.3 Fair value measurement of non-financial assets

In thousand Armenian drams				31 December 2018
	Level 1	**Level 2**	**Level 3**	**Total**
Non-financial assets				
Buildings	-	*11,408,894*	-	*11,408,894*
Net fair value	-	11,408,894	-	11,408,894

In thousand Armenian drams				31 December 2017
	Level 1	**Level 2**	**Level 3**	**Total**
Non-financial assets				
Buildings	-	*8,167,272*	-	*8,167,272*
Net fair value	-	8,167,272	-	8,167,272

Fair value measurements in Level 3

The Bank's non-financial assets classified in Level 3 uses valuation techniques based on significant inputs that are not based on observable market data. An analysis of financial assets within this level is represented as follows:

In thousand Armenian drams	2018
	Property and equipment
Non-financial assets	
Balance as of 1 January 2018	8,167,272
Purchases	4,100,700
Sales	(859,078)
Balance as of 31 December 2018	11,408,894
Net fair value	11,408,894

In thousand Armenian drams	2017
	Property and equipment
Non-financial assets	
Balance as of 1 January 2017	8,357,430
Purchases	31,783
Sales	(221,941)
Balance as of 31 December 2017	8,167,272
Net fair value	8,167,272

Fair value of the Bank's main property assets is estimated based on appraisals performed by independent, professionally-qualified property valuers. The significant inputs and assumptions are developed in close consultation with management. The valuation processes and fair value changes are reviewed by the board of directors and audit committee at each reporting date.

The appraisal was carried out using comparative and income approaches that reflect observed prices for recent market transactions for similar properties and includes adjustments related to abovementioned land factors, including plot size, location, pledging and current use, etc.

The buildings were re-valued in 2013.

The significant unobservable input is the adjustment for factors specific to the land in question. The extent and direction of this adjustment depends on the number and characteristics of the observable market transactions in similar properties that are used as the starting point for valuation. Although this input is a subjective judgement, management considers that the overall valuation would not be materially affected by reasonably possible alternative assumptions.

34 Offsetting of financial assets and financial liabilities

In the ordinary course of business, the Bank performs different operations with financial instruments which may be presented in net amounts when there is a legally enforceable right to set off the recognised amounts and there is an intention to settle on a net basis, or realise the asset and settle the liability simultaneously.

The table below presents financial assets and financial liabilities that are offset in the statement of financial position or are subject to an enforceable master netting arrangement or similar agreement that covers similar financial instruments, irrespective of whether they are offset in the statement of financial position.

In thousand Armenian drams						31 December 2018
				Related amounts that are not offset in the statement of financial position		
	Gross amount of recognised financial assets/ liabilities	Gross amount of recognised financial assets/ liabilities in the statement of financial position	Net amount of financial assets/ liabilities in the statement of financial position	Financial instruments	Cash collateral received	Net
Financial assets						
Reverse repurchase and repurchase agreements (Note 17, 18)	23,556,864	-	23,556,864	(23,556,864)	-	-
Financial liabilities						
Loans under repurchase agreements (Note 24)	(7,790,070)	-	(7,790,070)	9,145,216	-	1,355,146

In thousand Armenian drams	31 December 2017					
				Related amounts that are not offset in the statement of financial position		
	Gross amount of recognised financial assets/ liabilities	Gross amount of recognised financial assets/ liabilities in the statement of financial position	Net amount of financial assets/ liabilities in the statement of financial position	Financial instruments	Cash collateral received	Net
Financial assets						
Securities pledged under repurchase agreements (Note 17, 18)	24,972,103	-	24,972,103	(24,972,103)	-	-
Financial liabilities						
Amounts due to financial institutions (Note 24)	(13,847,877)	-	(13,847,877)	15,258,125	-	1,410,248

35 Maturity analysis of assets and liabilities

The table below shows an analysis of financial assets and liabilities analyzed according to when they are expected to be recovered or settled. See Note 36.3 for the Bank's contractual undiscounted repayment obligations.

In thousand Armenian drams	31 December 2018						
	Demand and less than 1 month	From 1 to 12 months	Subtotal less than 12 months	From 1 to 5 years	More than 5 years	Subtotal over 12 months	Total
Assets							
Cash and cash equivalents	127,342,452	-	*127,342,452*	-	-	-	127,342,452
Amounts due from financial institutions	13,531,878	214,367	*13,746,245*	152,600	-	*152,600*	13,898,845
Loans to customers	75,099,920	144,898,352	*219,998,272*	180,580,628	35,047,001	215,627,629	435,625,901
Investment securities at fair value through other comprehensive income	-	229,849	*229,849*	-	3,231,043	*3,231,043*	3,460,892
Securities pledged under repurchase agreements	-	99,452	*99,452*	4,080,323	4,965,441	*9,045,764*	9,145,216
Other financial assets	1,301,093	-	*1,301,093*	-	-	-	1,301,093
	217,275,343	145,442,020	*362,717,363*	184,813,551	43,243,485	*228,057,036*	590,774,399

In thousand Armenian drams	31 December 2018						
	Demand and less than 1 month	From 1 to 12 months	Subtotal less than 12 months	From 1 to 5 years	More than 5 years	Subtotal over 12 months	Total
Liabilities							
Derivative financial liabilities	8,940	-	*8,940*	-	-	-	8,940
Amounts due to financial institutions	27,711,867	9,784,737	*37,496,604*	11,179,386	16,320,189	*27,499,575*	64,996,179
Financial liabilities held for trading	23,230,915	-	*23,230,915*	-	-	-	23,230,915
Amounts due to the RA Government	220,497	71,283	*291,780*	137,969	207,842	*345,811*	637,591
Amounts due to customers	192,535,916	156,213,004	*348,748,920*	118,871,570	5,585,307	*124,456,877*	473,205,797
Debt securities issued	595,560	-	*595,560*	10,866,611	-	10,866,611	11,462,171
Other financial liabilities	657,599	-	*657,599*	-	-	-	657,599
	244,961,294	166,069,024	*411,030,318*	141,055,536	22,113,338	*163,168,874*	574,199,192
Net position	(27,685,951)	(20,627,004)	*(48,312,955)*	43,758,015	21,130,147	*64,888,162*	16,575,207
Accumulated gap	(27,685,951)	(48,312,955)		(4,554,940)	16,575,207		

In thousand Armenian drams	31 December 2017						
	Demand and less than 1 month	From 1 to 12 months	Subtotal less than 12 months	From 1 to 5 years	More than 5 years	Subtotal over 12 months	Total
Assets							
Cash and cash equivalents	115,576,209	-	115,576,209	-	-	-	115,576,209
Amounts due from financial institutions	8,462,159	2,058,935	10,521,094	3,515,628	-	3,515,628	14,036,722
Loans to customers	67,230,983	68,557,836	135,788,819	169,194,795	77,563,399	246,758,194	382,547,013
Investments available for sale	-	527,338	527,338	1,098,246	24,028	1,122,274	1,649,612
Securities pledged under repurchase agreements	15,258,125	-	15,258,125	-	-	-	15,258,125
Other financial assets	1,031,725	-	1,031,725	-	-	-	1,031,725
	207,559,201	71,144,109	278,703,310	173,808,669	77,587,427	251,396,096	530,099,406

In thousand Armenian drams							31 December 2017
	Demand and less than 1 month	From 1 to 12 months	Subtotal less than 12 months	From 1 to 5 years	More than 5 years	Subtotal over 12 months	Total
Liabilities							
Amounts due to financial institutions	29,109,967	4,059,734	33,169,701	22,569,720	20,265,000	42,834,720	76,004,421
Financial liabilities held for trading	24,556,156	-	24,556,156	-	-	-	24,556,156
Amounts due to the RA Government	692,952	-	692,952	-	-	-	692,952
Amounts due to customers	112,531,153	193,355,576	305,886,729	91,305,186	1,775,233	93,080,419	398,967,148
Debt securities issued	10,828	45,846	56,674	8,910,620	-	8,910,620	8,967,294
Other financial liabilities	740,658	-	740,658	-	-	-	740,658
	167,641,714	197,461,156	365,102,870	122,785,526	22,040,233	144,825,759	509,928,629
Net position	39,917,487	(126,317,047)	(86,399,560)	51,023,143	55,547,194	106,570,337	20,170,777
Accumulated gap	39,917,487	(86,399,560)		(35,376,417)	20,170,777		

36 Risk management

The Bank's activities expose it to a variety of financial risks and those activities involve the analysis, evaluation, acceptance and management of some degree of risk or combination of risks.

The risk management procedure is organized in compliance with the Bank's mission, principal and interim goals and is aimed at the improvement of the financial position of the Bank and the Bank's reputation.

The main goals of risk management policy of the Bank is to disclose, assess and make manageable all possible risks that relate immediately to the Bank's activity, help the Bank's management make optimal decisions, assist in realistic planning of the Bank's strategy, taking into account the principles of risk/profitability ratio by taking up manageable risks, determining preferable sectors of resource allocation, providing the maintenance of ratios set forth by the CBA, as well as interbank ratios of the Bank.

The Risk management policy of the Bank arises from the following main principles:

- ✓ The risk management must be mitigating and justified
- ✓ Risks must be fully disclosed, objectively assessed and efficiently managed
- ✓ When reacting to disclosed risks the risk management/supervision expenses and consequences of undesired cases must be weighed against gains expected as a result of risk mitigation
- ✓ Risk management may include such approaches as procedures aimed at risk mitigation, risk transfer to third parties, for example, through insurance, and risk acceptance, when risk mitigation expenses exceed assessed losses or their mitigation is actually impossible. For this purpose, accepted level of risk is determined.

Risk is managed through a process of ongoing identification, measurement and monitoring, subject to risk limits and other controls. The Bank's risk management policy allows to efficiently manage risks relating to assets and liabilities of the Bank and Bank's customers through exclusion and minimization of losses caused by risks by providing acceptable level of profitability, liquidity and solvency

The risk management in the Bank is carried out through limits set forth by all business processes, internal legal acts regulating the activity of the latter, all procedures and operations in a precise and documented manner.

Risk management structure

The Board of the Bank, the Chair of the Executive Board, the Executive Board and the Management of the Bank within the frames of their responsibilities set forth by RA legislation and internal legal acts of the Bank are responsible for the formation, viability and efficiency of proper Risk management system in the Bank; however, there are separate independent bodies responsible for managing and monitoring risks.

Risk management committee and Risk management and planning department

The Risk management committee and risk management and planning departments are responsible for carrying out risk management policy of the Bank.

The risk management and planning department continually supervise risk levels assumed by the Bank and the maintenance of limits relating to these risks, the possible effect of risks on the Bank's activity are assessed through different stress-tests.

Reports, analysis and proposals concerning risks relating to the Bank's activity are presented by the Risk management and planning department (as well as other beneficiary departments) are discussed in Risk management committee meetings and presented to the Executive Board of the Bank with the purpose of making appropriate decision.

Internal audit

Risk management processes throughout the Bank are audited annually by the internal audit function, that examines both the adequacy of the procedures and the Bank's compliance with the procedures. Internal Audit discusses the results of all assessments with management and presents his/her conclusions and suggestions to the Board of the Bank.

Risk characterization and assessment

Depending on a variety of factors the Bank finds it expedient to divide banking risks into external and internal risks.

External risks are country, price, competitive and force major risks.

Internal risks are credit, liquidity, interest rate, foreign currency, operating, personnel and money laundering risks.

Country risk

Country risk is managed by the Bank using rankings assigned by international rating agencies (Moody's, S&P, Fitch) to international banks and institutions. Risk management department performs periodic monitoring of ratings of foreign banks who are counteragents of the Bank.

Price risk

Possible minimum level of price risks is provided within the frames of the following measures: analysis of financial market structural, volume and price index dynamics, analysis of liquidity of separate financial instruments, disclosure of present tendencies, assessment of possible losses through stress tests on monthly basis, determination of financial instruments' limit (by the type of operation with securities, dealer, issuer).

Competitive risk

Management of competitive risk in the Bank is performed by business departments and Marketing analysis department, through periodic comparison of variety of services and terms offered by the Bank and other banks.

Force major risk

The Bank has server reserve center at its disposal according to the requirement of ISO 27001-2005. The location of the center outside the head office of the Bank, in a remote place, will allow providing the Bank's activity in force major situation.

Credit risk

The main issue of management of credit risks for the Bank is timely disclosure of credit risks, assessment and taking appropriate measures for their reduction.

The credit risk in the Bank is assessed not only for each borrower, but also for the loan portfolio in full. According to appropriate methodology elaborated by the Bank the potential solvency of the borrower is assessed before extension of the loan. From the perspective of mitigation of credit risk, the security and expediency of the loan are given significant importance. After loan extension, over the full term of the credit contract, credit monitoring is performed by the Bank for periodically assessing the solvency and security of the loans and taking appropriate measures for mitigating possible credit risks. The Bank's loan portfolio is periodically analyzed by economic sectors, customers and loan types for providing diversification and quality of the loan portfolio.

The activity of the Loan committee is significant in mitigation of credit risk. Loan committee is the body executing loan policy of the Bank, whose purpose is the management of loan policy and formation of quality loan portfolio. The main issue of the Credit committee is to make professional protocol or final decision concerning execution and servicing of instruments exposed to credit risk.

Liquidity risk

The liquidity management purpose in the Bank is to create a volume of such financial means, which would enable to satisfy legal cash requirements of all kinds of creditors, depositors and other clients without serious issues, which may be reflected in the Bank's balance and off-balance sheet articles, as well as provide maximum level of profitability along with all these factors.

Management of assets and liabilities by mutual agreement is carried out in the Bank for providing fluent liquidity and efficient liquidity risk management by providing:

- ✓ Providing existence of highly liquid assets
- ✓ Stability of resources
- ✓ Acceptable limits of maturity gaps of assets and liabilities
- ✓ Opportunities for attracting means from external sources

With the purpose of making correct decision regarding liquidity management of the Bank the maturity analysis of assets and liabilities is given great importance, which is performed by the calculation model of maturity gaps (GAP) by demand and accumulated separations. Demand liquidity is calculated on daily basis for making correct circumstances decision.

36.1 Credit risk

The Bank takes on exposure to credit risk, which is the risk that counterparty will cause a financial loss for the Bank by failing to discharge an obligation. Credit risk is the most important risk for the Bank'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. There is also credit risk in off-balance sheet financial instruments, such as loan commitments. Relevant reports and analysis are periodically presented to the Executive Board of the Bank.

Credit risk in the Bank is managed according to the Bank's lending policy and the field is regulated by other internal legal acts. The risk management executive body performs monitoring of loan portfolio on daily basis, loan portfolio dynamics calculation based on constructed series and analysis of quality of portfolio by products and branches, based on which forecasting of quality indexes of loan portfolio are performed. The risk management executive body performs loan monitoring of several loan types by the approved procedure, and when necessity arises, monitoring of other loans based on deterioration of the financial position of the borrower. Loans extended by the Bank are approved by the risk executive body according to internal legal acts by reducing credit risk.

36.1.1 Credit quality analysis

The following table contains an analysis of the credit risk exposure of financial instruments for which an ECL allowance is recognised. The gross carrying amount of financial assets below also represents

the Bank's maximum exposure to credit risk on these assets, without taking account of any collateral held or other credit enhancements. For loan commitments and financial guarantee contracts, the amounts in the table represent the amounts committed or guaranteed, respectively.

In thousand Armenian drams				31 December 2018	31 December 2017
Internal rating grade	Stage 1 12-month ECL	Stage 2 Lifetime ECL not credit-impaired	Stage 3 Lifetime ECL credit-impaired	Total	Total
Cash and cash equivalents					
Standard	127,348,537	-	-	127,348,537	115,576,209
Gross carrying amount	127,348,537	-	-	127,348,537	115,576,209
Loss allowance	(6,085)	-	-	(6,085)	-
Net carrying amount	127,342,452	-	-	127,342,452	115,576,209
Amounts due from banks and financial institutions					
Standard	13,957,123	-	-	13,957,123	14,036,722
Gross carrying amount	13,957,123	-	-	13,957,123	14,036,722
Loss allowance	(58,278)	-	-	(58,278)	-
Net carrying amount	13,898,845	-	-	13,898,845	14,036,722
Loans to mortgage and consumer customers					
High grade	55,451,030	-	-	55,451,030	51,541,119
Standard grade	5,628,746	1,917,157	-	7,545,903	6,109,090
Substandard grade	-	419,064	-	419,064	516,112
Non-performing grade	-	-	7,094,696	7,094,696	2,909,629
Gross carrying amount	61,079,776	2,336,221	7,094,696	70,510,693	61,075,950
Loss allowance	(1,449,329)	(549,008)	(3,307,809)	(5,306,146)	(3,697,432)
Net carrying amount	59,630,447	1,787,213	3,786,887	65,204,547	57,378,518
Loans to commercial customers					
High grade	330,578,996	-	-	330,578,996	287,165,221
Standard grade	27,577,890	1,349,911	-	28,927,801	26,366,018
Substandard grade	-	2,997,591	-	2,997,591	23,312
Non-performing grade	-	-	20,302,176	20,302,176	17,946,080
Gross carrying amount	358,156,886	4,347,502	20,302,176	382,806,564	331,500,631
Loss allowance	(3,128,802)	(671,688)	(8,584,720)	(12,385,210)	(6,332,136)
Net carrying amount	355,028,084	3,675,814	11,717,456	370,421,354	325,168,495
Debt investment securities at FVOCI, including pledged securities (2017: available-for-sale)					
Standard	12,556,447	-	-	12,556,447	16,883,709
Fair value	12,556,447	-	-	12,556,447	16,883,709
Loss allowance	(11,217)	-	-	(11,217)	-

In thousand Armenian drams				31 December 2018	31 December 2017
Internal rating grade	Stage 1 12-month ECL	Stage 2 Lifetime ECL not credit-impaired	Stage 3 Lifetime ECL credit-impaired	Total	Total
Other financial assets					
Standard grade	1,440,094	-	-	1,440,094	1,031,725
Gross carrying amount	1,440,094	-	-	1,440,094	1,031,725
Loss allowance	(139,001)	-	-	(139,001)	-
Net carrying amount	1,301,093	-	-	1,301,093	1,031,725
Loan commitments and financial guarantee					
Standard grade	87,008,385	-	-	87,008,385	58,296,332
	87,008,385	-	-	87,008,385	58,296,332
Loss allowance*	(853,987)	-	-	(853,987)	-

* The ECL allowance disclosed in loan commitments and financial guarantees of the above table applies only to the guarantees provided. The ECL allowance on loans includes ECL on loan commitments for products such as credit cards and overdrafts, because the Bank cannot separately identify the ECL on the loan commitment component from those on the financial instrument component .

36.1.2 Impairment assessment

Policy applicable from 1 January 2018

The references below show where the Bank's impairment assessment and measurement approach is set out in this report. It should be read in conjunction with the Summary of significant accounting policies (Refer to note 4.4.6).

Significant increase in credit risk

At each reporting date, The Bank assess whether the credit risk on a financial instrument has increased significantly since initial recognition. When making the assessment, The Bank use the change in the risk of a default occurring over the expected life of the financial instrument instead of the change in the amount of expected credit losses.

The bank considers both quantitative and forward-looking qualitative criteria in order to assess whether a significant increase in credit risk has occurred.

However, when information that is more forward-looking than past due status (either on an individual or a collective basis) is not available without undue cost or effort, The Bank use past due information to determine whether there have been significant increases in credit risk since initial recognition.

Criteria for loans and advances to customers

The criteria for Loans and advances to customers are presented in the following paragraphs. All presented criteria have the same weight in determining a significant increase in credit risk.

- 30 days past due. More than 30 days past due is an indicator of a significant increase in credit risk.
- Past due - other than 30 days. Significant increase in credit risk is considered when although at the reporting date, days past due are less than 30, during the last 6 months there was at least one case of more than 60 days past due.
- Relative change in 12-month PD. A significant change in 12-month PD is considered as factor of changes in lifetime PD. This is indicative of a significant increase in credit risk. This criterion is used when The Bank has an internal credit rating system.

- Relative change in lifetime PD. A significant change in lifetime PD is indicative of a significant increase in credit risk. This criterion is used when The Bank has an internal credit rating system
- Default (‘stage 3’) during the last 12 months. Significant increase in credit risk is considered when although at the reporting date the outstanding amount of the facility is not classified as default, during the last 12 months it was at least once in stage 3.
- Loans in the probation period. Significant increase in credit risk is considered in case of a forborne performing loan or forborne non-performing loan, which is in the probation period (period after cure period). wherein, the loan should not have overdue days of more than 30 days or any indication of an unlikeliness to pay.

Criteria for amounts due from financial institutions

The criteria for credit institutions and other financial corporations are presented in the following paragraphs. All presented criteria have the same weight in determining a significant increase in credit risk.

- 30 days past due. More than 30 days past due is an indicator of a significant increase in credit risk.
- For correspondent and current accounts 7 days’ pas due. More than 7 days past due is an indicator of a significant increase in credit risk.
- Past due - other than 30 days. Significant increase in credit risk is considered when although at the reporting date, days past due are less than 30, during the last 6 months there was at least one case of more than 60 days past due.
- Change notches external credit score/ rate. For this criterion, the corporate rating will be taken into account. A significant change notches in the credit score assigned by the Big Three credit rating agencies (Standard & Poor's, Moody's, and Fitch) is indicative of a significant increase in credit risk. A significant increase in credit risk is taken into account when the S & P rating goes down each time by one level, started from B2 (S&P) (or the equivalent of Moody's and Fitch). In cases where a financials institutions don't have a corporate rating in a rating agency and The Bank does not have an equivalent internal rating system, the corporate default rate corresponding to sovereign rating of the country is taken into consideration.
- Relative change in 12-month PD. A significant change in 12-month PD is considered as factor of changes in lifetime PD. This is indicative of a significant increase in credit risk. This criterion is used when The Bank has an internal credit rating system.
- Relative change in lifetime PD. A significant change in lifetime PD is indicative of a significant increase in credit risk. This criterion is used when The Bank has an internal credit rating system
- Default (‘stage 3’) during the last 12 months. Significant increase in credit risk is considered when although at the reporting date the outstanding amount of the facility is not classified in default, during the last 12 months it was at least once in stage 3.

Criteria for Investment securities

The criteria for securities are presented in the following paragraphs. All presented criteria have the same weight in determining a significant increase in credit risk.

- Relative change in 12-month PD. A significant change in 12-month PD is considered as factor of changes in lifetime PD. This is indicative of a significant increase in credit risk. This criterion is used when the Entity has an internal credit rating system.
- Relative change in lifetime PD. A significant change in lifetime PD is indicative of a significant increase in credit risk. This criterion is used when the Entity has an internal credit rating system
- Change notches external credit score/ rate. For this criterion, the country's rating will be taken into account government securities or corporate rating will be taken into account for corporate securities. A significant change notches in the credit score assigned by the Big Three credit rating agencies (Standard & Poor's, Moody's, and Fitch) is indicative of a significant increase in credit risk. A significant increase in credit risk is taken into account when the S & P rating goes down one level each time, beginning with B2 (S&P) (or the equivalent of Moody's and Fitch). In cases where an issuers of securities don't have a corporate rating in a rating agency and The Bank does not have an equivalent internal rating system, the corporate default rate corresponding to sovereign rating of the country is taken into consideration.

Exit criteria from significant deterioration stage

If none of the indicators that are used by The Bank to assess whether significant increase in credit risk has occurred, is present, transfer from stage 2 to stage 1 is performed, with the exception of forborne loans for which a probation period is used.

Credit risk grades

The Bank allocates each exposure to a credit risk grade based on a variety of data that is determined to be predictive of the risk of default and applying experienced credit judgement. Credit risk grades are defined using qualitative and quantitative (primarily driven by days past due) factors that are indicative of risk of default. These factors vary depending on the nature of the exposure and the type of borrower.

Collective or individual assessment

The Bank calculates ECLs either on a collective or an individual basis. Asset classes where the Bank calculates ECL on an individual basis include:

- Individually significant loans of Stage 3, regardless of the class of financial assets
- The large and unique exposures
- The treasury, trading and interbank relationships such as Due from Banks, Securities pledged under repurchase agreements and debt instruments at amortised cost/FVOCI
- Exposures that have been classified as POCI when the original loan was derecognised and a new loan was recognised as a result of a credit driven debt restructuring.

Those assets for which ECL does not calculated individually the bank groups into segment on the basis of shared credit risk characteristics as described below.

- Type of loan (for example, corporate, mortgage, credit card, consumer loan, etc.)
- The type of customer (for example, a physical person or legal entity or by industry type),
- Type of collateral (for example, property, receivables, etc.),
- Currency
- Other relevant characteristics.

Definition of default and cure

The Bank considers a financial instrument defaulted and therefore Stage 3 (credit-impaired) for ECL calculations in all cases when the borrower becomes 90 days past due on its contractual payments.

The Bank considers interbank balances defaulted and takes immediate action when the required intraday payments are not settled by the close of business as outlined in the individual agreements.

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

- lawsuit, execution or enforced execution in order to collect debt,
- license of the borrower is withdrawn,
- the borrower is a co-debtor when the main debtor is in default,
- multiple restructurings on one exposure,
- there are justified concerns about a borrower's future ability to generate stable and sufficient cash flows,
- the borrower's overall leverage level has significantly increased or there are justified expectations of such changes to leverage; equity reduced by 50% within a reporting period due to losses;
- debt service coverage ratio indicates that debt is not sustainable
- loss of major customer or tenant,
- connected customer has filed for bankruptcy,
- restructuring with a material part which is forgiven (net present value (NPV) loss),
- credit institution or leader of consortium starts bankruptcy/insolvency proceedings

It is the Bank's policy to consider a financial instrument as 'cured' and therefore re-classified out of Stage 3 when none of the default criteria have been present for at least three consecutive months. The decision whether to classify an asset as Stage 2 or Stage 1 once cured depends on the updated credit grade, at the

time of the cure, and whether this indicates there has been a significant increase in credit risk compared to initial recognition. The Bank's criterion for 'cure' for ECL purposes is less stringent than the 12 months' requirement for forborne non-performing exposures.

Forborne and modified loan

The Bank sometimes makes concessions or modifications to the original terms of loans as a response to the borrower's financial difficulties, rather than taking possession or to otherwise enforce collection of collateral. The Bank considers a loan forborne when such concessions or modifications are provided as a result of the borrower's present or expected financial difficulties and the Bank would not have agreed to them if the borrower had been financially healthy. Indicators of financial difficulties include defaults on covenants, or significant concerns raised by the Credit Risk Department. Forbearance may involve extending the payment arrangements and the agreement of new loan conditions. Once the terms have been renegotiated, any impairment is measured using the original EIR as calculated before the modification of terms. It is the Bank's policy to monitor forborne loans to help ensure that future payments continue to be likely to occur.

Derecognition decisions and classification between Stage 2 and Stage 3 are determined on a case-by-case basis.

The Bank defines the "cure" period as a 12-month period after forbearance, which is applied for forborne non-performing exposures. Given the fact that it is impossible to determine financial difficulties immediately after forbearance, it is necessary to use the "cure" period to determine whether the loan was effectively cured. All forborne non-performing loans must remain at stage 3 after the forbearance date, despite the behavior of the loan (no overdue days, etc.).

The Bank defines the probation period as 24-month period after "cure" period, which is applied for forborne performing exposures (excluding any grace period). Once an asset has been classified as forborne performing exposures, it will remain forborne for a minimum 24-month probation period.

In order for the loan to be reclassified out of the forborne category, the customer has to meet all of the following criteria:

- All of its facilities has to be considered performing
- The probation period of two years has passed from the date the forborne contract was considered performing
- Regular payments of more than an insignificant amount of principal or interest have been made during at least half of the probation period
- The customer does not have any contract that is more than 30 days past due.

If modifications are substantial, the loan is derecognised, as explained in Note 4.4.4.

Probability of Default (PD)

The PD represents the likelihood of a borrower defaulting on its financial obligation, either over the next 12 months (12mECL), or over the remaining lifetime (LTECLs) of the obligation.

The Lifetime PD is developed by applying a maturity profile to the current 12M PD. The maturity profile looks at how defaults develop on a portfolio from the point of initial recognition throughout the lifetime of the loans. The maturity profile is based on historical observed data and is assumed to be the same across all assets within a portfolio and credit grade band. This is supported by historical analysis.

Loss given default (LGD)

LGD is determined based on the factors which impact the recoveries made post default. These vary by product type.

- For secured products, this is primarily based on collateral type and projected collateral values, historical discounts to market/book values due to forced sales, time to repossession and recovery costs observed.
- For unsecured products, LGD's are typically set at product level due to the limited differentiation in recoveries achieved across different borrowers. These LGD's are influenced by collection strategies, including contracted debt sales and price.

Exposure at default (EAD)

The 12-month and lifetime EADs are determined based on the expected payment profile, which varies by product type.

- For products with contractual terms, this is based on the contractual repayments owed by the borrower over a 12-month or lifetime basis. This will also be adjusted for any expected overpayments made by a borrower. Early repayment/refinance assumptions are also incorporated into the calculation.
- For revolving products, the exposure at default is predicted by taking current drawn balance and adding a "credit conversion factor" which allows for the expected drawdown of the remaining limit by the time of default. These assumptions vary by product type and current limit utilization band, based on analysis of the Bank's recent default data.

Forward looking information

An overview of the approach to estimating ECLs is set out in Note 4.4.6, estimates and assumptions. To ensure completeness and accuracy, the Bank obtains the data used from third party sources (WB, CBA, Government of RA and etc.). In order to generate the influence of the macroeconomic factors, the Bank determining the weights to the selected macroeconomic factors and to the multiple scenarios (Base, Upside and Downside), which are predicted. To calculate the macroeconomic adjustment for ECL the Bank uses a wide range of forecast information as economic inputs for its models, including:

- GDP growth
- Net current transfers from abroad
- Unemployment
- Bank nonperforming loans to total gross loans
- Official exchange rate

Impairment assessment policy applicable before 1 January 2018

The main considerations for the loan impairment assessment include whether any payments of principal or interest are overdue by more than 90 days or there are any known difficulties in the cash flows of counterparties, credit rating downgrades, or infringement of the original terms of the contract. The Bank addresses impairment assessment into areas: individually assessed allowances and collectively assessed allowances.

Individually assessed allowances

The Bank determines the allowances appropriate for each individually significant loan or advance on an individual basis. Items considered when determining allowance amounts include the sustainability of the counterparty's business plan, its ability to improve performance once a financial difficulty has arisen, projected receipts and the expected dividend payout should bankruptcy ensue, the availability of other financial support and the realizable value of collateral, and the timing of the expected cash flows. The impairment losses are evaluated at each reporting date, unless unforeseen circumstances require more careful attention.

Collectively assessed allowances

Allowances are assessed collectively for losses on loans and advances that are not significant (including credit cards, residential mortgages and unsecured consumer lending) and for individually significant loans and advances where there is not yet objective evidence of individual impairment. Allowances are evaluated on each reporting date with each portfolio receiving a separate review.

The collective assessment takes account of impairment that is likely to be present in the portfolio even though there is not yet objective evidence of the impairment in an individual assessment. Impairment losses are estimated by taking into consideration of the following information: historical losses on the portfolio, current economic conditions, the approximate delay between the time a loss is likely to have been incurred and the time it will be identified as requiring an individually assessed impairment allowance, and expected receipts and recoveries once impaired.

Financial guarantees and letters of credit are assessed and provision made in a similar manner as for loans.

Loans and advances neither past due or impaired

The table below shows the credit quality by class of asset for loans and advances neither past due or impaired, based on the historical counterparty default rates.

In thousand Armenian drams	2017
Loans to customers	
Industry	1.0%
Agriculture	1.0%
Construction	4.1%
Trading	2.1%
Consumer	7.2%
Mortgage	1.6%
Other	1.0%

As of 31 December 2017 the Bank has not had any losses on other financial assets bearing credit risk.

Past due but not impaired loans

Past due loans and advances include those that are only past due by a few days. The majority of the past due loans are not considered to be impaired.

Analysis of past due loans by age and by class is provided below.

In thousand Armenian drams					2017
	Less than 30 days	31 to 60 days	61 to 90 days	More than 91 days	Total
Loans to customers					
Industry	-	-	-	7,407,299	7,407,299
Agriculture	14,341	6,974	7,447	18,849	47,611
Construction	-	34,126	-	1,418,233	1,452,359
Trading	-	2,761	811	163,061	166,633
Consumer	747,176	213,831	204,191	2,255,345	3,420,543
Mortgage	64,157	49,020	49,109	82,218	244,504
Other	-	643	97	8,396,677	8,397,417
Total	825,674	307,355	261,655	19,741,682	21,136,366

36.1.3 Risk concentrations

Geographical sectors

The following table breaks down the Bank's main credit exposure at their carrying amounts, as categorized by geographical region as of 31 December.

In thousand Armenian drams	Armenia	OECD countries	Other non-OECD countries	Total
Cash and cash equivalents	116,269,239	6,702,814	4,370,399	127,342,452
Amounts due from financial institutions	2,263,355	981,232	10,654,258	13,898,845
Loans to customers	385,684,603	805,471	49,135,827	435,625,901
Investment securities				
- Investment securities at fair value through other comprehensive income	3,443,219	17,673	-	3,460,892
- Securities pledged under repurchase agreements	9,145,216	-	-	9,145,216
Other assets	1,287,003	2,047	12,043	1,301,093
As of 31 December 2018	518,092,635	8,509,237	64,172,527	590,774,399
As of 31 December 2017	476,011,641	3,829,466	50,258,299	530,099,406

Assets have been classified based on the country in which the counterparty is located.

Industry sectors

The following table breaks down the Bank's main credit exposure at their carrying amounts, as categorized by the industry sectors of the counterparties as of 31 December.

In thousand Armenian drams	Financial institutions	Industry	Construc-tion	Trading	Consumer sector	Mortgage	Other	Total
Cash and cash equivalents	127,342,452	-	-	-	-		-	127,342,452
Amounts due from financial institutions	13,898,845	-	-	-	-		-	13,898,845
Loans to customers	-	50,706,947	45,575,961	136,848,110	53,805,463	11,399,084	137,290,336	435,625,901
Investment securities								
- Investment securities at fair value through other comprehensive income	49,661	-	-	-	-	-	3,411,231	3,460,892
- Securities pledged under repurchase agreements	99,452	-	-	-	-	-	9,045,764	9,145,216
Other assets	-	-	-	-	-	-	1,301,093	1,301,093
As of 31 December 2018	141,390,410	50,706,947	45,575,961	136,848,110	53,805,463	11,399,084	151,048,424	590,774,399
As of 31 December 2017	143,510,005	36,188,340	45,602,996	104,600,854	44,763,130	12,615,388	142,818,693	530,099,406

36.1.4 Collateral and other credit enhancement

The amount and type of collateral required depends on an assessment of the credit risk of the counterparty. Guidelines are in place covering the acceptability and valuation of each type of collateral.

The main types of collateral obtained are, as follows:

- For securities lending and reverse repurchase transactions, cash or securities
- For commercial lending, charges over real estate properties, movable properties, equipment, inventory and trade receivables and, in special circumstances, government guarantees

- For consumer lending residential properties and other collateral.
- For mortgages over residential properties

The Bank also obtains guarantees from parent companies for loans to their subsidiaries. Management monitors the market value of collateral and will request additional collateral in accordance with the underlying agreement.

The Bank did not hold any financial instruments for which no loss allowance is recognised because of collateral.

Longer-term finance and lending to corporate entities are generally secured; revolving individual credit facilities are generally unsecured. In addition, in order to minimise the credit loss, the Bank will seek additional collateral from the counterparty as soon as impairment indicators are noticed for the relevant individual loans and advances.

Collateral held as security for financial assets other than loans and advances is determined by the nature of the instrument. Generally, no collaterals are required for provision of loans and advances to financial institutions, especially to Banks. The exception is collaterals obtained under repurchase agreements and securities borrowing transactions. Debt securities, treasury and other eligible bills are generally unsecured.

The analysis of gross loan portfolio of loans and advances to customers by collateral is represented as follows:

In thousand Armenian drams	31 December 2018	31 December 2017
Loans collateralized by real estate	128,552,782	118,308,308
Loans collateralized by gold	12,067,616	12,044,262
Loans collateralized by securities	23,165,276	24,056,087
Loans collateralized by guarantees of other organizations	84,022,547	80,739,367
Loans collateralized by vehicles	1,219,799	176,238
Loans collateralized by cash	2,542,377	22,671,881
Loans collateralized by stock	12,728,957	7,093,332
Other collateral	189,017,903	127,487,106
Total loans to customers (gross)	453,317,257	392,576,581

The amounts presented in the table above are carrying values of the loans, and do not necessarily represent the fair value of the collaterals. Estimates of market values of collaterals are based on valuation of the collateral at the date when loans were provided. Generally, they are not updated unless loans are assessed as credit-impaired.

36.2 Market risk

Market risk is the risk that the fair value or future cash flows of financial instruments will fluctuate due to changes in market variables such as interest rates and foreign exchange rates. The Bank classifies exposures to market risk into either trading or non-trading portfolios. The market risk for the trading portfolio is managed and monitored based on Value at Risk (“VaR”) methodology which reflects the interdependency between risk variables. Non-trading positions are managed and monitored using other sensitivity analyses. Except for the concentrations within foreign currency, the Bank has no significant concentration of market risk.

36.2.1 Market risk – Non-trading

Interest rate risk

Interest rate risk management issue in the Bank is to maintain the target level of interest rate spread and net interest margin of assets and liabilities. For the purpose of mitigating interest rate risk specially elaborated mechanisms of price formation (interest rate determination) for assets and liabilities are in place.

The model of calculation of maturity gap of interest rate sensitive assets and interest rate sensitive liabilities is the base of assessment of interest rate risk, which allows estimating the effect of interest rate change on the Bank's expected net interest income. The interest rate risk in the Bank is assessed using duration model which indicates the economic value change of equity as a result of interest rate change taking into account the incompliance of maturities of attracted liabilities and allocated assets.

Currency risk

Currency risk is the risk that the value of a financial instrument will fluctuate due to changes in foreign exchange rates. The Bank manages currency risk using standard and VaR methodologies. Foreign currency rates are monitored on daily basis, based on which forecasting of foreign currency rates is performed at the end of the month for the following month. The Executive board has established limits for foreign currency positions.

The tables below indicate the currencies to which the Bank had significant exposure at 31 December 2018 on its non-trading monetary assets and liabilities and its forecast cash flows. The analysis calculated the effect of a reasonably possible movement of the currency rate against the Armenian dram, with all other variables held constant on the income statement (due to the fair value of currency sensitive non-trading monetary assets and liabilities) and equity (due to the change in fair value of currency swaps and forward foreign exchange contracts used as cash flow hedges, and equity instruments). A negative amount in the table reflects a potential net reduction in income statement or equity, while a positive amount reflects a net potential increase.

In thousand Armenian drams	31 December 2018			31 December 2017		
Currency	Change in currency rate in %	Effect on profit before tax	Effect on equity	Change in currency rate in %	Effect on profit before tax	Effect on equity
USD	+5	407,116	407,116	+5	(114,650)	(114,650)
USD	-5	(407,116)	(407,116)	-5	114,650	114,650
EUR	+8	2,748,985	2,748,985	+8	(11,281)	(11,281)
EUR	-8	(2,748,985)	(2,748,985)	-8	11,281	11,281

The Bank's exposure to foreign currency exchange risk is as follow:

In thousand Armenian drams	Armenian Dram	Freely convertible currencies/ precious metals	Non-freely convertible currencies	Total
Assets				
Cash and cash equivalents	58,258,213	67,777,705	1,306,534	127,342,452
Amounts due from financial institutions	1,484,183	2,317,448	10,097,214	13,898,845
Loans to customers	203,807,859	229,136,097	2,681,945	435,625,901
Investment securities				
- Investment securities at fair value through other comprehensive income	3,460,892	-	-	3,460,892
- Securities pledged under repurchase agreements	8,404,656	740,560	-	9,145,216
Other financial assets	1,151,392	147,995	1,706	1,301,093
	276,567,195	300,119,805	14,087,399	590,774,399

In thousand Armenian drams	Armenian Dram	Freely convertible currencies/ precious metals	Non-freely convertible currencies	Total
Liabilities				
Amounts due to financial institutions	50,957,487	11,167,186	2,871,506	64,996,179
Financial liabilities held for trading	23,230,915	-	-	23,230,915
Amounts due to the RA Government	524,291	113,300	-	637,591
Amounts due to customers	186,061,154	275,922,680	11,221,963	473,205,797
Debt securities issued	102,724	11,359,447	-	11,462,171
Other financial liabilities	619,300	38,299	-	657,599
Total	261,495,871	298,600,912	14,093,469	574,190,252
Total effect of derivative financial instruments	(8,940)	-	-	(8,940)
Net position as of 31 December 2018	15,062,384	1,518,893	(6,070)	16,575,207
Commitments and contingent liabilities as of 31 December 2018	23,574,273	63,145,495	288,617	87,008,385
Total financial assets	275,178,795	247,730,445	7,190,166	530,099,406
Total financial liabilities	252,500,539	250,195,585	7,232,505	509,928,629
Net position as of 31 December 2017	22,678,256	(2,465,140)	(42,339)	20,170,777
Commitments and contingent liabilities As of 31 December 2017	21,390,294	36,203,168	702,870	58,296,332

Freely convertible currencies represent mainly US dollar amounts, but also include currencies from other OECD countries. Non-freely convertible amounts relate to currencies of CIS countries, excluding Republic of Armenia.

36.3 Liquidity risk

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

The Bank maintains a portfolio of highly marketable and diverse assets that can be easily liquidated in the event of an unforeseen interruption of cash flow. The Bank also has committed lines of credit that it can access to meet liquidity needs. In addition, the Bank maintains an obligatory minimum reserve deposits with the Central Bank of Armenia equal to 2% of certain obligations of the Bank denominated in Armenian drams and 20% on certain obligations of the Bank denominated in foreign currency. See note 15. The liquidity position is assessed and managed under a variety of scenarios, giving due consideration to stress factors relating to both the market in general and specifically to the Bank.

The liquidity management of the Bank requires considering 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 balance sheet liquidity ratios against regulatory requirements. The Bank calculates liquidity ratios in accordance with the requirement of the Central Bank of Armenia.

As of 31 December, these ratios were as follows:	Unaudited	
	2018, %	2017, %
N21- Total liquidity ratio (Highly liquid assets/ Total assets)	22.21	25.27
H22- Current liquidity ratio (Highly liquid assets /liabilities on demand)	82.07	132.18

Analysis of financial liabilities by remaining contractual maturities.

The table below summarises the maturity profile of the Bank's financial liabilities at 31 December 2018 based on contractual undiscounted repayment obligations. See note 35 for the expected maturities of these liabilities. Repayments which are subject to notice are treated as if notice were to be given immediately. However, the Bank expects that many customers will not request repayment on the earliest date the Bank could be required to pay and the table does not reflect the expected cash flows indicated by the Bank's deposit retention history.

In thousand Armenian drams					31 December 2018
	Demand and less than 1 month	From 1 to 12 months	From 1 to 5 years	More than 5 years	Total
Non-derivative financial liabilities					
Amounts due to financial institutions	27,825,881	10,171,252	13,142,491	20,877,568	72,017,192
Financial liabilities held for trading	23,230,915	-	-	-	23,230,915
Amounts due to the RA Government	220,497	71,458	152,047	230,181	674,183
Amounts due to customers	192,612,059	162,712,688	134,938,506	10,052,460	500,315,713
Debt securities issued	597,907	-	12,688,562	-	13,286,469
Other liabilities	740,658	-	-	-	740,658
Total undiscounted non-derivative financial liabilities	245,227,917	172,955,398	160,921,606	31,160,209	610,265,130
Derivative financial liabilities					
Foreign exchange swap contracts					
Inflow	1,660,950	-	-	-	1,660,950
Outflow	(1,669,890)	-	-	-	(1,669,890)
Commitments and contingent liabilities	3,943,016	41,234,485	34,279,214	7,551,670	87,008,385

In thousand Armenian drams					31 December 2017
	Demand and less than 1 month	From 1 to 12 months	From 1 to 5 years	More than 5 years	Total
Non-derivative financial liabilities					
Amounts due to financial institutions	43,112,888	8,699,426	15,691,735	30,453,111	97,957,160
Financial liabilities held for trading	24,556,156	-	-	-	24,556,156
Amounts due to the RA Government	89,866	16,208	318,091	328,140	752,305
Amounts due to customers	112,052,008	203,184,796	107,309,388	3,714,885	426,261,077
Debt securities issued	598,265	8,480,504	-	-	9,078,769
Other liabilities	740,658	-	-	-	740,658
Total undiscounted non-derivative financial liabilities	181,149,841	220,380,934	123,319,214	34,496,136	559,346,125
Commitments and contingent liabilities	1,333,544	20,713,006	31,861,591	4,388,191	58,296,332

The Bank has attracted means in significant amounts from shareholders and related parties. Any significant repayment of these amounts may negatively affect the Bank's activity. The Management of the Bank is assured that the present level of financing will be maintained in the visible future and in the case of repayment of means it will be informed in advance, which will allow the Bank cash its liquid means and repay the debt.

36.4 Operational risk

Operational risk is the risk of direct or indirect loss arising from a wide variety of causes associated with the Bank's involvement with financial instruments, including processes, personnel, technology and infrastructure, and from external factors other than credit, market and liquidity risks such as those arising from legal and regulatory requirements and generally accepted standards of corporate behaviour.

The Bank's objective is to manage operational risk so as to balance the avoidance of financial losses and damage to the Bank's reputation with overall cost effectiveness.

The primary responsibility for the development and implementation of controls to address operational risk is assigned to the Risk Management department. This responsibility is supported by the development of overall standards for the management of operational risk in the following areas:

- requirements for appropriate segregation of duties, including the independent authorisation of transactions;
- requirements for the reconciliation and monitoring of transactions;
- compliance with regulatory and other legal requirements, including the minimal requirements of the Central Bank of Armenia on internal control system;
- documentation of controls and procedures;
- requirements for the periodic assessment of operational risks faced, and the adequacy of controls and procedures to address the risks identified;
- requirements for the reporting of operational losses and proposed remedial action;
- development of contingency plans;
- training and professional development;
- ethical and business standards; and
- risk mitigation.

Compliance with Bank standards is supported by a programme of periodic reviews undertaken by Internal Audit. The results of Internal Audit reviews are discussed with the management of the Bank to which they relate, with summaries submitted to the Board.

37 Reconciliation of liabilities arising from financing activities

The changes in the Bank's liabilities arising from financing activities can be classified as follows:

In thousand Armenian drams			2018
	Loans to financial institutions	**Debt securities issued**	**Total**
As of 1 January 2018	38,585,043	8,967,294	47,552,337
Cash-flows	*(3,842,738)*	*2,498,092*	*(1,344,646)*
Repayments	(20,768,663)	(1,687,129)	(22,455,792)
Proceeds	16,925,925	4,185,221	21,111,146
Non-cash	*40,926*	*(3,215)*	*37,711*
Foreign exchange gain/loss	40,926	(3,215)	37,711
As of 31 December 2018	34,783,231	11,462,171	46,245,402

In thousand Armenian drams			2017
	Loans to financial institutions	**Debt securities issued**	**Total**
As of 1 January 2017	28,814,598	-	28,814,598
Cash-flows	*9,829,539*	*8,853,026*	*18,682,565*
Repayments	(18,289,846)	(137,603)	(18,427,449)
Proceeds	28,119,385	8,990,629	37,110,014
Non-cash	*(59,094)*	*114,268*	*55,174*
Foreign exchange gain/loss	(59,094)	114,268	55,174
As of 31 December 2017	38,585,043	8,967,294	47,552,337

38 Capital adequacy

The Bank maintains an actively managed capital base to cover risks inherent in the business. The adequacy of the Bank's capital is monitored using, among other measures, the rules and ratios established by the Basel Committee on Banking Supervision ("BIS rules/ratios") and adopted by the Central Bank of Armenia in supervising the Bank.

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

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

The minimum ratio between total capital and risk weighted assets required by the Central Bank of Armenia is 12%.

Regulatory capital consists of Tier 1 capital, which comprises share capital, share premium, retained earnings including current year profit, and general reserve. Regulatory capital is calculated in accordance with the

requirements of the Central Bank of Armenia and accounting standards of the Republic of Armenia. The other component of regulatory capital is Tier 2 capital, which includes revaluation reserves and other reserves.

The risk-weighted assets are measured by means of a hierarchy of risk weights classified according to the nature of and reflecting an estimate of credit, market and operating risks.

As of 31 December 2018 and 2017 the amount of regulatory capital, risk waited assets and capital adequacy ratio calculated in accordance with the requirements of Central Bank of Armenia are provided below.

	Unaudited	
In thousand Armenian drams	**31 December 2018**	**31 December 2017**
Tier 1 capital	32,255,952	30,170,167
Tier 2 capital	2,235,401	2,620,145
Total regulatory capital	34,491,353	32,790,312
Risk-weighted assets	255,454,765	242,891,200
Capital adequacy ratio	13.50%	13.50%

The Bank has complied with all externally imposed capital requirements through the period.

With the aim to enhance the efficiency of the banking system activity, strengthening the ability to resist the shocks in different economic situations, as well as providing more efficient and available banking services, in 2017 the Board of the RA Central Bank decided to determine the minimum size of total capital at 30,000,000 thousand Armenian drams for the banks, as at 1 January 2018 and after that period.

39 Segment reporting

The Bank's operations are highly integrated and constitute a single operating segment for the purposes of IFRS 8 "Operating Segments".

The majority of income from external customers relates to residents of the Republic of Armenia. No single customer exists from which the Bank earned 10% or more of its revenue.