# HSBC Bank Armenia cjsc

## Annual Report and Accounts 2014

HSBC

## The HSBC Group

HSBC Bank Armenia is a member of HSBC Group, one of the largest banking and financial services organizations in the world.
HSBC Group international network comprises around 6,100 offices over 73 countries and territories.

**HSBC Bank Armenia cjsc**
*Registered in the Republic of Armenia: number 67*
*Registered Office:*
66 Teryan Street
Yerevan, 0009
Republic of Armenia
Telephone: 374 60 655000
Facsimile: 374 60 655501
**Web: www.hsbc.am**

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## Statement of management's responsibilities

The management of HSBC Bank Armenia cjsc (the "Bank") is responsible for the preparation of financial statements which give a true and fair view of the financial position and financial performance of the Bank, in all material respects. In preparing these financial statements, the directors are required to:

- select appropriate accounting policies, present them for the Board's approval and apply them consistently;
- make reasonable judgments and estimates;
- keep proper accounting records;
- comply with the requirements of International Financial Reporting Standards, in case discrepancies exist, disclose them in the notes to the financial statements;
- prepare the financial statements on the going concern basis, unless it is inappropriate to presume that the Bank will continue in business;
- design, implement and maintain an effective and reliable internal control system relevant to the internal control minimum requirements specified by the Central Bank of the Republic of Armenia;
- set up an effective accounting system complying with the requirements of the Republic of Armenia legislation and International Financial Reporting Standards, as well providing timely and accurate information on the Bank's financial position;
- take such steps within its authorities to safeguard the assets of the Bank and to prevent and detect fraud and other irregularities.

Thies Clemenz
Chief Executive Officer

Astghik Drembyan
Chief Financial Officer

## Statement of compliance

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

The financial statements present fairly, in all material respects, the financial position of the Bank as at 31 December 2014, and its financial performance and its cash flows for the year then ended.

## Opinion on compliance with the requirements of the Central Bank of Armenia on internal controls

This opinion is prepared based on the results of internal audits and continuing monitoring completed by the Internal Audit function during 2014.

Based on the above, in our opinion, the Bank's activity during 2014 was generally in compliance with legislative and regulatory requirements. Any identified issues with this regard have been escalated to the Board and management through internal audit reports. Appropriate management remediating actions have been agreed and taken.

Internal Audit Department

## Business review and financial analysis

HSBC Bank Armenia cjsc provides a wide range of financial services. In 2014 the Bank has continued to expand its operations, whilst maintaining a strong and healthy financial base.

2014 was a challenging but nevertheless successful year for the Bank. The Bank continued to develop its products and services and maintained the steady growth trend of recent years. The growth strategy and effective risk management of the Bank were grounds for this success.

The main achievements were the growth of the corporate and retail loan portfolios, as well as development and enhancement of products and services.

The Bank remained focused on bridging customers with global opportunities and presenting innovative financing solutions to local businesses. The Bank continued to assist Armenian companies to take part in international programmes on sharing professional experience in trade financing. Linking local clients to international markets through the global presence of HSBC underlines the Bank's ambition to be the leading international bank for business in Armenia.

During the year the Bank continued its strategy to support foreign investments into Armenia by referring lending opportunities to HSBC Bank plc, UK for direct lending to Armenian businesses. The loan portfolio of HSBC Bank plc, UK to Armenian businesses grew from USD 25 million as at 31 December 2013 to USD 95 million as at 31 December 2014, or by 280%, generating net interest income equivalent to USD 2.2 mln during 2014. These financial indicators are not part of the financial statements of HSBC Bank Armenia cjsc, however they present the level of interest and engagement of HSBC Group in Armenia's economy.

In line with its strategy to bring innovative technological solutions to the Armenian market, the Bank introduced mobile banking services to customers in 2014. The HSBC Mobile Banking Application is an innovative solution, which distributes the existing internet banking service to customers in a version customised for smartphones and tablets. The application has recently been recognised as the "Best Mobile Banking App" by Global Finance Magazine. It has more than five million downloads and is used by customers in around 25 countries, including Armenia. To enhance the rapid implementation of the service, a wireless internet connection was made available for customers in the Bank's branches.

In 2014 the Bank presented to its customers a new service of cash deposit machines, which enables customers to make instant deposits to their accounts in addition to other operations already provided by the bank's existing ATMs. During the year the Bank improved lending terms offered to retail clients, as well as expanded product types, thus providing higher flexibility for customers to address their needs.

The Bank continued its active involvement in the developing capital markets in Armenia, acting as a lead manager for a bond issuance for the European Bank for Reconstruction and Development.

In line with HSBC Group's worldwide commitment to the highest compliance standards, the Bank implemented various changes in its systems and processes to ensure compliance with FATCA and other regulatory requirements.

Throughout 2014, in line with HSBC's corporate sustainability strategy, the Bank engaged and participated in more than twentysix projects, allocating over AMD 40 million to implement these. The supported projects have mainly been focused on education of children at risk, environment and the community.

Education of children at risk is one of primary focus areas of corporate social responsibility and benefits from 50% of the Bank's total donation budget. The Bank has cooperated with a number of NGOs, non-profit organizations such as Meghvik, Tumo Centre for Creative Technologies, COAF, Orran Charity organisation, the British Council and Matenadaran.

Approximately AMD 7 million was donated in support of environmental efficiency, with the main focus being on biodiversity, water conservation, and climate change. The Bank has cooperated closely with environmental protection non-for-profit organizations such as World Wide Fund (WWF), Fund for the Preservation of Wildlife and Cultural Assets (FPWC), and supported them in programs aimed towards conservation of endangered species and the promotion of ecotourism.

None of this would have been possible without the commercial success, loyalty and support of our 36 thousand customers, or indeed without the untiring efforts of the Bank's 387 staff.

***Financial review***

The Bank's net profit after tax for the year was AMD 6,565.4 million, which is 18% less than the prior year's result. This is explained by higher impairment charges against the local loan portfolio due to a slowdown in the economy.

Operating income rose to AMD 18,757 million, a 3.4% increase from the previous year. Impairment charges were AMD 2,530 million, which is higher than 2013 by AMD 1,978 million. Personnel and other administrative expenses were AMD 7,684 million, a 3.1% increase from the previous year.

Total assets as at 31 December 2014 were AMD 307 billion, a 23% growth over the previous year. Loans to customer portfolio amounted to AMD 176 billion, a 16% growth over last year. The gross corporate loan portfolio increased by 17% and amounted to AMD 154 billion. The gross retail loan portfolio demonstrated 18% growth amounting to AMD 25 billion. The customer deposit base increased by 9% and amounted to AMD 176 billion.

The cost efficiency ratio for 2014 remains at 41%. The return on equity ratio for 2014 stood at 14.3% compared to 20% for 2013.

During the year the Bank did not pay dividends, having decided to direct earned profits into further business growth.

Philip Alvey
Board Member

Ara Alexanian
Board Member

KPMG

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# Independent Auditors' Report

To the Board of
HSBC Bank Armenia cjsc

We have audited the accompanying financial statements of HSBC Bank Armenia cjsc (the "Bank") set out on pages 10 to 69, which comprise the statement of financial position as at 31 December 2014, and the statements of profit or loss and other comprehensive income, changes in equity and cash flows for the year then ended, and notes, comprising a summary of significant accounting policies and other explanatory information.

*Management's Responsibility for the Financial Statements*

Management is responsible for the preparation and fair presentation of these financial statements in accordance with International Financial Reporting Standards, 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.

*Auditors' Responsibility*

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with International Standards on Auditing. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements 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 entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

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

*Opinion*

In our opinion, the financial statements present fairly, in all material respects, the financial position of the Bank as at 31 December 2014, and its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards.

Tigran Gasparyan
Director

Tigran Gasparyan
Engagement Partner

KPMG Armenia cjsc

KPMG Armenia cjsc
22 April 2015

# Statement of Profit or Loss and Other Comprehensive Income for the year ended 31 December 2014

| | Notes | 2014 AMD'000 | 2013 AMD'000 |
|---|---|---|---|
| Interest income | 4 | 19,942,083 | 18,840,862 |
| Interest expense | 4 | (5,095,267) | (4,489,755) |
| **Net interest income** | | **14,846,816** | **14,351,107** |
| Fee and commission income | 5 | 2,686,738 | 2,640,185 |
| Fee and commission expense | 6 | (546,422) | (461,276) |
| **Net fee and commission income** | | **2,140,316** | **2,178,909** |
| Net gain on financial instruments at fair value through profit or loss | 7 | 1,206,111 | 290,654 |
| Net foreign exchange gain | 8 | 640,198 | 1,370,429 |
| Net gain on available-for-sale financial assets | | - | 9,461 |
| Other operating income | | 136,731 | 145,233 |
| Other operating expenses | | (212,763) | (196,479) |
| **Operating income** | | **18,757,409** | **18,149,314** |
| Impairment losses | 9 | (2,529,580) | (551,958) |
| Personnel expenses | 10 | (3,776,596) | (3,439,331) |
| Other general administrative expenses | 11 | (3,907,228) | (4,014,439) |
| **Profit before income tax** | | **8,544,005** | **10,143,586** |
| Income tax expense | 12 | (1,978,556) | (2,134,083) |
| **Profit for the year** | | **6,565,449** | **8,009,503** |
| **Other comprehensive income, net of income tax** | | | |
| Items that are or may be reclassified subsequently to profit or loss: | | | |
| Revaluation reserve for available-for-sale financial assets: | | | |
| - Net change in fair value | | (889,725) | 827,218 |
| - Net change in fair value transferred to profit or loss | | - | 8,924 |
| **Other comprehensive income (loss) for the year, net of income tax** | | **(889,725)** | **836,142** |
| **Total comprehensive income for the year** | | **5,675,724** | **8,845,645** |

The financial statements as set out on pages 10 to 69 were approved by the Board of the Bank. The financial statements were signed by the Management of the Bank on 22 April 2015.

Thies Clemenz
Chief Executive Officer

Astghik Drambyan
Chief Financial Officer

The statement of profit or loss and other comprehensive income is to be read in conjunction with the notes to, and forming part of, the financial statements.

# Statement of Financial Position as at 31 December 2014

| | Notes | 2014 AMD'000 | 2013 AMD'000 |
|---|---|---|---|
| **ASSETS** | | | |
| Cash and cash equivalents | 13 | 73,626,715 | 53,345,787 |
| Financial instruments at fair value through profit or loss | | | |
| - Held by the Bank | 14 | 1,563,863 | 821,624 |
| Available-for-sale financial assets | | | |
| - Held by the Bank | 15 | 20,735,512 | 32,530,104 |
| - Pledged under sale and repurchase agreements | 15 | 12,338,544 | - |
| Loans and advances to banks | 16 | 4,756,365 | 1,960,267 |
| Loans to customers | 17 | 175,986,458 | 151,532,749 |
| Property, equipment and intangible assets | 18 | 3,865,547 | 4,048,139 |
| Other assets | 19 | 13,736,108 | 5,184,919 |
| **Total assets** | | **306,609,112** | **249,423,589** |
| **LIABILITIES** | | | |
| Deposits and balances from banks | 20 | 55,034,995 | 38,195,064 |
| Amounts payable under repurchase agreements | 21 | 12,013,151 | - |
| Current accounts and deposits from customers | 22 | 175,660,747 | 160,997,179 |
| Current tax liability | | 482,592 | 734,842 |
| Deferred tax liability | 12 | 822,448 | 1,018,426 |
| Other liabilities | 23 | 15,634,777 | 7,196,993 |
| **Total liabilities** | | **259,648,710** | **208,142,504** |
| **EQUITY** | | | |
| Share capital | 24 | 18,434,350 | 18,434,350 |
| Share based payments reserve | | 92,466 | 87,893 |
| Revaluation reserve for available-for-sale financial assets | | 198,167 | 1,087,892 |
| Retained earnings | | 28,235,419 | 21,670,950 |
| **Total equity** | | **46,960,402** | **41,281,085** |
| **Total liabilities and equity** | | **306,609,112** | **249,423,589** |

The statement of financial position is to be read in conjunction with the notes to, and forming part of, the financial statements.

# Statement of Cash Flows for the year ended 31 December 2014

| | Notes | 2014 AMD'000 | 2013 AMD'000 |
|---|---|---|---|
| **CASH FLOWS FROM OPERATING ACTIVITIES** | | | |
| Interest receipts | | 21,015,830 | 17,486,772 |
| Interest payments | | (5,153,382) | (4,202,079) |
| Fee and commission receipts | | 2,854,526 | 2,799,578 |
| Fee and commission payments | | (548,371) | (460,086) |
| Net receipts from financial instruments at fair value through profit or loss | | 382,869 | 238,200 |
| Net receipts from foreign exchange | | 1,411,250 | 1,211,951 |
| Net other income receipts | | 142,439 | 148,906 |
| General administrative and personnel expense payments | | (6,841,241) | (6,552,244) |
| | | | |
| **(Increase) decrease in operating assets** | | | |
| Financial instruments at fair value through profit or loss | | 165,716 | 844,171 |
| Available-for-sale financial assets | | (1,656,353) | 1,403,086 |
| Loans and advances to banks | | (3,319,958) | 1,641,763 |
| Loans to customers | | (6,026,185) | (22,000,179) |
| Other assets | | (8,551,189) | (1,746,748) |
| | | | |
| **Increase (decrease) in operating liabilities** | | | |
| Deposits and balances from banks | | 10,708,147 | 6,500,462 |
| Amounts payable under repurchase agreements | | 11,999,961 | - |
| Current accounts and deposits from customers | | (3,176,997) | 23,036,575 |
| Other liabilities | | 7,546,917 | 1,586,395 |
| **Net cash from operating activities before income tax paid** | | **20,953,979** | **21,936,523** |
| Income tax paid | | (2,204,353) | (2,496,177) |
| **Cash flows from operations** | | **18,749,626** | **19,440,346** |
| | | | |
| **CASH FLOWS FROM INVESTING ACTIVITIES** | | | |
| Purchases of property, equipment and intangible assets | | (712,141) | (911,649) |
| Sales of property, equipment and intangible assets | | 596 | 4,807 |
| **Cash flows used in investing activities** | | **(711,545)** | **(906,842)** |
| | | | |
| **CASH FLOWS FROM FINANCING ACTIVITIES** | | | |
| Dividends paid | | - | (3,075,000) |
| **Cash flows used in financing activities** | | **-** | **(3,075,000)** |
| | | | |
| **Net increase in cash and cash equivalents** | | **18,038,081** | **15,458,504** |
| Effect of changes in exchange rates on cash and cash equivalents | | 1,357,087 | (412,510) |
| Cash and cash equivalents as at the beginning of the year | | 52,531,481 | 37,485,487 |
| **Cash and cash equivalents as at the end of the year** | 13 | **71,926,649** | **52,531,481** |

The statement of cash flows is to be read in conjunction with the notes to, and forming part of, the financial statements.

# Statement of Changes in Equity for the year ended 31 December 2014

| AMD'000 | Share capital | Share based payments reserve | Revaluation reserve for available-for-sale financial assets | Retained earnings | Total |
|---|---|---|---|---|---|
| **Balance as at 1 January 2013** | **18,434,350** | **85,950** | **251,750** | **16,738,880** | **35,510,930** |
| **Total comprehensive income** | | | | | |
| Profit for the year | - | - | | 8,009,503 | 8,009,503 |
| **Other comprehensive income** | | | | | |
| Net change in fair value of available-for-sale financial assets, net of income tax | - | - | 827,218 | - | 827,218 |
| Net change in fair value of available-for-sale financial assets transferred to profit or loss, net of income tax | - | - | 8,924 | - | 8,924 |
| **Total other comprehensive income** | **-** | **-** | **836,142** | **-** | **836,142** |
| **Total comprehensive income for the year** | **-** | **-** | **836,142** | **8,009,503** | **8,845,645** |
| **Transactions with owners, recorded directly in equity** | | | | | |
| Share based payments | - | 1,943 | - | (2,433) | (490) |
| Dividends paid | - | - | - | (3,075,000) | (3,075,000) |
| **Total transactions with owners** | **-** | **1,943** | **-** | **(3,077,433)** | **(3,075,490)** |
| **Balance as at 31 December 2013** | **18,434,350** | **87,893** | **1,087,892** | **21,670,950** | **41,281,085** |
| | | | | | |
| **Balance as at 1 January 2014** | **18,434,350** | **87,893** | **1,087,892** | **21,670,950** | **41,281,085** |
| **Total comprehensive income** | | | | | |
| Profit for the year | - | - | | **6,565,449** | **6,565,449** |
| **Other comprehensive loss** | | | | | |
| Net change in fair value of available-for-sale financial assets, net of income tax | - | - | (889,725) | - | (889,725) |
| **Total other comprehensive loss** | **-** | **-** | **(889,725)** | **-** | **(889,725)** |
| **Total comprehensive income for the year** | **-** | **-** | **(889,725)** | **6,565,449** | **5,675,724** |
| **Transactions with owners, recorded directly in equity** | | | | | |
| Share based payments | - | 4,573 | - | (980) | 3,593 |
| **Total transactions with owners** | **-** | **4,573** | **-** | **(980)** | **3,593** |
| **Balance as at 31 December 2014** | **18,434,350** | **92,466** | **198,167** | **28,235,419** | **46,960,402** |

The statement of changes in equity is to be read in conjunction with the notes to, and forming part of, the financial statements.

# Notes to, and forming part of, the financial statements for the year ended 31 December 2014

## 1 Background

### (a) Organisation and operations

HSBC Bank Armenia CJSC (the Bank) was registered as a closed joint stock company in Armenia in 1995. The Bank provides a wide spectrum of financial and banking services and operates from its head office and branches located in the capital of Armenia. The activities of the Bank are regulated by the Central Bank of Armenia (CBA).

As at 31 December 2014 the Bank had 10 branches. The average number of persons employed by the Bank during the year was 383 (2013: 378).

The Bank's registered office is 66 Teryan Street, Yerevan 0009, Republic of Armenia.

The Bank is owned by HSBC Europe B.V. (70%) and Wings Establishment (30%).

Related party transactions are detailed in note 31.

### (b) Business environment

#### Armenian business environment

The Bank's operations are primarily located in Armenia. Consequently, the Bank is exposed to the economic and financial markets of Armenia which display characteristics of an emerging market. The legal, tax and regulatory frameworks continue development, but are subject to varying interpretations and frequent changes which together with other legal and fiscal impediments contribute to the challenges faced by entities operating in Armenia. The financial statements reflect management's assessment of the impact of the Armenian business environment on the operations and the financial position of the Bank. The future business environment may differ from management's assessment.

## 2 Basis of preparation

### (a) Statement of compliance

The accompanying financial statements are prepared in accordance with International Financial Reporting Standards (IFRS).

### (b) Basis of measurement

The financial statements are prepared on the historical cost basis except that financial instruments at fair value through profit or loss and available-for-sale financial assets are stated at fair value and land and buildings are stated at revalued amounts.

### (c) Functional and presentation currency

The functional currency of the Bank is the Armenian Dram (AMD) as, being the national currency of the Republic of Armenia, it reflects the economic substance of the majority of underlying events and circumstances relevant to the Bank.

The AMD is also the presentation currency for the purposes of these financial statements.

Financial information presented in AMD is rounded to the nearest thousand.

### (d) Use of estimates and judgments

The preparation of financial statements in conformity with IFRS requires management to make judgments, estimates and assumptions that affect the application of accounting policies and the reported amounts of assets, liabilities, income and expenses. Actual results could differ from those estimates.

Estimates and underlying assumptions are reviewed on an on-going basis. Revisions to accounting estimates are recognised in the period in which the estimates are revised and in any future periods affected.

Information about significant areas of estimation uncertainty and critical judgments in applying accounting policies is described in the following notes:

- Loan impairment estimates – note 17; and
- Fair value of financial instruments – note 32.

## 3 Significant accounting policies

The accounting policies set out below are applied consistently to all periods presented in these financial statements.

The Bank has adopted the Amendments to IAS 32 *Financial Instruments: Disclosure and Presentation - Offsetting Financial Assets and Financial Liabilities* with a date of initial application of 1 January 2014. The Amendments do not introduce new rules for offsetting financial assets and liabilities; rather they clarify the offsetting criteria to address inconsistencies in their application. The Amendments specify that an entity currently has a legally enforceable right to set-off if that right is not contingent on a future event; and enforceable both in the normal course of business and in the event of default, insolvency or bankruptcy of the entity and all counterparties. These amendments did not have an impact on these financial statements as the Bank does not present financial assets and financial liabilities on a net basis in the statement of financial position.

### (a) Foreign currency

Transactions in foreign currencies are translated to the functional currency of the Bank at exchange rates at the dates of the transactions. Monetary assets and liabilities denominated in foreign currencies at the reporting date are retranslated to the functional currency at the exchange rate at that date. The foreign currency gain or loss on

monetary items is the difference between amortised cost in the functional currency at the beginning of the period, adjusted for effective interest and payments during the period, and the amortised cost in foreign currency translated at the exchange rate at the end of the reporting period. Non-monetary assets and liabilities denominated in foreign currencies that are measured at fair value are retranslated to the functional currency at the exchange rate at the date that the fair value is determined. Non-monetary items that are measured in terms of historical cost in a foreign currency are translated using the exchange rate at the date of the transaction. Foreign currency differences arising on retranslation are recognised in profit or loss, except for differences arising on the retranslation of available-for-sale equity instruments, unless the difference is due to impairment in which case foreign currency differences that have been recognised in other comprehensive income are reclassified to profit or loss or qualifying cash flow hedges to the extent that the hedge is effective, which are recognised in other comprehensive income.

## (b) Cash and cash equivalents

Cash and cash equivalents include notes and coins on hand, unrestricted balances (nostro accounts, overnight deposits and placements maturing within three days) held with the CBA and other banks. The minimum reserve deposit with the CBA is considered to be a cash equivalent due to the absence of restrictions on its withdrawability. Cash and cash equivalents are carried at amortised cost in the statement of financial position.

## (c) Financial instruments

### *(i) Classification*

*Financial instruments at fair value through profit or loss* are financial assets or liabilities that are:

- acquired or incurred principally for the purpose of selling or repurchasing in the near term
- part of a portfolio of identified financial instruments that are managed together and for which there is evidence of a recent actual pattern of short-term profit-taking
- derivative financial instruments (except for derivative financial instruments that are designated and effective hedging instruments) or,
- upon initial recognition, designated as at fair value through profit or loss.

The Bank may designate financial assets and liabilities at fair value through profit or loss where either:

- the assets or liabilities are managed, evaluated and reported internally on a fair value basis
- the designation eliminates or significantly reduces an accounting mismatch which would otherwise arise or,
- the asset or liability contains an embedded derivative that significantly modifies the cash flows that would otherwise be required under the contract.

All trading derivatives in a net receivable position (positive fair value), as well as options purchased, are reported as assets. All trading derivatives in a net payable position (negative fair value), as well as options written, are reported as liabilities.

Management determines the appropriate classification of financial instruments in this category at the time of the initial recognition. Derivative financial instruments and financial instruments designated as at fair value through profit or loss upon initial recognition are not reclassified out of at fair value through profit or loss category. Financial assets that would have met the definition of loan and receivables may be reclassified out of the fair value through profit or loss or available-for-sale category if the entity has an intention and ability to hold it for the foreseeble future or until maturity. Other financial instruments may be reclassified out of at fair value through profit or loss category only in rare circumstances. Rare circumstances arise from a single event that is unusual and highly unlikely to recur in the near term.

*Loans and receivables* are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market, other than those that the Bank:

- intends to sell immediately or in the near term
- upon initial recognition designates as at fair value through profit or loss
- upon initial recognition designates as available-for-sale or,
- may not recover substantially all of its initial investment, other than because of credit deterioration.

*Held-to-maturity investments* are non-derivative financial assets with fixed or determinable payments and fixed maturity that the Bank has the positive intention and ability to hold to maturity, other than those that:

- the Bank upon initial recognition designates as at fair value through profit or loss
- the Bank designates as available-for-sale or,
- meet the definition of loans and receivables.

*Available-for-sale financial assets* are those non-derivative financial assets that are designated as available-for-sale or are not classified as loans and receivables, held-to-maturity investments or financial instruments at fair value through profit or loss.

### *(ii) Recognition*

Financial assets and liabilities are recognized in the statement of financial position when the Bank becomes a party to the contractual provisions of the instrument. All regular way purchases of financial assets are accounted for at the settlement date.

### *(iii) Measurement*

A financial asset or liability is initially measured at its fair value plus, in the case of a financial asset or liability not at fair value through profit or loss, transaction costs that are directly attributable to the acquisition or issue of the financial asset or liability.

Subsequent to initial recognition, financial assets, including derivatives that are assets, are measured at their fair values, without any deduction for transaction costs that may be incurred on sale or other disposal, except for:

- loans and receivables which are measured at amortized cost using the effective interest method
- held-to-maturity investments that are measured at amortized cost using the effective interest method
- investments in equity instruments that do not have a quoted market price in an active market and whose fair value can not be reliably measured which are measured at cost.

All financial liabilities, other than those designated at fair value through profit or loss and financial liabilities that arise when a transfer of a financial asset carried at fair value does not qualify for derecognition, are measured at amortized cost.

### *(iv) Amortised cost*

The amortised cost of a financial asset or liability is the amount at which the financial asset or liability is measured at initial recognition, minus principal repayments, plus or minus the cumulative amortisation using the effective interest method of any difference between the initial amount recognised and the maturity amount, minus any reduction for impairment. Premiums and discounts, including initial transaction costs, are included in the carrying amount of the related instrument and amortized based on the effective interest rate of the instrument.

### *(v) Fair value measurement principles*

Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date in the principal, or in its absence, the most advantageous market to which the Bank has access at that date. The fair value of a liability reflects its non-performance risk.

When available, the Bank measures the fair value of an instrument using quoted prices in an active market for that instrument. A market is regarded as active if transactions for the asset or liability take place with sufficient frequency and volume to provide pricing information on an ongoing basis.

When there is no quoted price in an active market, the Bank uses valuation techniques that maximise the use of relevant observable inputs and minimise the use of unobservable inputs. The chosen valuation technique incorporates all the factors that market participants would take into account in these circumstances.

The best evidence of the fair value of a financial instrument at initial recognition is normally the transaction price, i.e., the fair value of the consideration given or received. If the Bank determines that the fair value at initial recognition differs from the transaction price and the fair value is evidenced neither by a quoted price in an active market for an identical asset or liability nor based on a valuation technique that uses only data from observable markets, the financial instrument is initially measured at fair value, adjusted to defer the difference between the fair value at initial recognition and the transaction price. Subsequently, that difference is recognised in profit or loss on an appropriate basis over the life of the instrument but no later than when the valuation is supported wholly by observable market data or the transaction is closed out.

If an asset or a liability measured at fair value has a bid price and an ask price, the Bank measures assets and long positions at the bid price and liabilities and short positions at the ask price.

The Bank recognises transfers between levels of the fair value hierarchy as of the end of the reporting period during which the change has occurred.

### *(vi) Gains and losses on subsequent measurement*

A gain or loss arising from a change in the fair value of a financial asset or liability is recognized as follows:

- a gain or loss on a financial instrument classified as at fair value through profit or loss is recognized in profit or loss
- a gain or loss on an available-for-sale financial asset is recognized as other comprehensive income in equity (except for impairment losses and foreign exchange gains and losses on debt financial instruments available-for-sale) until the asset is derecognized, at which time the cumulative gain or loss previously recognised in equity is recognized in profit or loss. Interest in relation to an available-for-sale financial asset is recognized in profit or loss using the effective interest method.

For financial assets and liabilities carried at amortized cost, a gain or loss is recognized in profit or loss when the financial asset or liability is derecognized or impaired, and through the amortization process.

### *(vii) Derecognition*

The Bank derecognises a financial asset when the contractual rights to the cash flows from the financial asset expire, or when it transfers the financial asset in a transaction in which substantially all the risks and rewards of ownership of the financial asset are transferred or in which the Bank neither transfers nor retains substantially all the risks and rewards of ownership and it does not retain control of the financial asset. 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 in the statement of financial position. The Bank derecognises a financial liability when its contractual obligations are discharged or cancelled or expire.

The Bank enters into transactions whereby it transfers assets recognised on its statement of financial position, but retains either all risks and rewards of the transferred assets or a portion of them. If all or substantially all risks and rewards are retained, then the transferred assets are not derecognised.

In transactions where the Bank neither retains nor transfers substantially all the risks and rewards of ownership of a financial asset, it derecognises the asset if control over the asset is lost.

In transfers where control over the asset is retained, 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 assets.

If the Bank purchases its own debt, it is removed from the statement of financial position and the difference between the carrying amount of the liability and the consideration paid is included in gains or losses arising from early retirement of debt.

The Bank writes off assets deemed to be uncollectible.

### *(viii) Repurchase and reverse repurchase agreements*

Securities sold under sale and repurchase (repo) agreements are accounted for as secured financing transactions, with the securities retained in the statement of financial position and the counterparty liability included in amounts payable under repo transactions. The difference between the sale and repurchase prices represents interest expense and is recognized in profit or loss over the term of the repo agreement using the effective interest method.

Securities purchased under agreements to resell (reverse repo) are recorded as amounts receivable under reverse repo transactions within loans and advances to banks or loans to customers, as appropriate. The difference between the purchase and resale prices represents interest income and is recognized in profit or loss over the term of the repo agreement using the effective interest method.

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

### *(ix) Derivative financial instruments*

Derivative financial instruments include swaps, forwards, spots, futures and options in interest rates, foreign exchanges, precious metals and stock markets, and any combinations of these instruments.

Derivatives are initially recognised at fair value on the date on which a derivative contract is entered into and are subsequently remeasured at fair value. All derivatives are carried as assets when their fair value is positive and as liabilities when their fair value is negative.

Changes in the fair value of derivatives are recognised immediately in profit or loss.

### *(x) Offsetting*

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

## (d) Property and equipment

### *(i) Owned assets*

Items of property and equipment are stated at cost less accumulated depreciation and impairment losses, except for land and buildings, which are stated at revalued amounts as described below.

Where an item of property and equipment comprises major components having different useful lives, they are accounted for as separate items of property and equipment.

### *(ii) Revaluation*

Land and buildings are subject to revaluation on a regular basis. The frequency of revaluation depends on the movements in the fair values of the land and buildings being revalued. A revaluation increase on an item of land and building is recognised as other comprehensive income directly in equity except to the extent that it reverses a previous revaluation decrease recognised in profit or loss, in which case it is recognised in profit or loss. A revaluation decrease on an item of land or buildings is recognised in profit or loss except to the extent that it reverses a previous revaluation increase recognised as other comprehensive income directly in equity, in which case it is recognised in other comprehensive income.

Management uses independent valuation firms to estimate the fair value of land and buildings. The valuation firms use the income approach, cost approach and the comparable sales approach, or a combination thereof, depending on availability and reliability of information.

### *(iii) Depreciation*

Depreciation is charged to profit or loss on a straight-line basis over the estimated useful lives of the individual assets. Depreciation commences on the date of acquisition or, in respect of internally constructed assets, from the time an asset is completed and ready for use. Leasehold improvements are depreciated over the shorter of the asset useful life and lease term. Land is not depreciated. The estimated useful lives are as follows:

| | |
|---|---|
| - buildings | 20 years |
| - leasehold improvements | up to 10 years |
| - vehicles | 5 years |
| - computer equipment | 4 to 7 years |
| - other | 5 years |

## (e) Intangible assets

Acquired intangible assets are stated at cost less accumulated amortisation and impairment losses.

Acquired computer software licenses are capitalised on the basis of the costs incurred to acquire and bring to use the specific software.

Subsequent expenditure on intangible assets is capitalized only when it increases the future economic benefits embodied in the specific asset to which it relates.

Costs associated with developing or maintaining computer software programs are recognized as an expense as incurred.

Amortization is charged to profit or loss on a straight-line basis over the estimated useful lives of intangible assets. The estimated useful lives are as follows:

| | |
|---|---|
| - computer software | 3 to 5 years |
| - other | 10 years |

## (f) Impairment

### *(i) Financial assets carried at amortized cost*

Financial assets carried at amortized cost consist principally of loans and other receivables (loans and receivables). The Bank reviews its loans and receivables to assess impairment on a regular basis. A loan or receivable is impaired and impairment losses are incurred if, and only if, there is objective evidence of impairment as a result of one or more events that occurred after the initial recognition of the loan or receivable and that event (or events) has had an impact on the estimated future cash flows of the loan that can be reliably estimated.

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

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

If there is objective evidence that an impairment loss on a loan or receivable has been incurred, the amount of the loss is measured as the difference between the carrying amount of the loan or receivable and the present value of estimated future cash flows including amounts recoverable from guarantees and collateral discounted at the loan or receivable's original effective interest rate. Contractual cash flows and historical loss experience adjusted on the basis of relevant observable data that reflect current economic conditions provide the basis for estimating expected cash flows.

In some cases the observable data required to estimate the amount of an impairment loss on a loan or receivable may be limited or no longer fully relevant to current circumstances. This may be the case when a borrower is in financial difficulties and there is little available historical data relating to similar borrowers. In such cases, the Bank uses its experience and judgment to estimate the amount of any impairment loss.

All impairment losses in respect of loans and receivables are recognized in profit or loss and are only reversed if a subsequent increase in recoverable amount can be related objectively to an event occurring after the impairment loss was recognised.

When a loan is uncollectable, it is written off against the related allowance for loan impairment. The Bank writes off a loan balance (and any related allowances for loan losses) when management determines that the loans are uncollectible and when all necessary steps to collect the loan are completed.

### *(ii) Financial assets carried at cost*

Financial assets carried at cost include unquoted equity instruments included in available-for-sale financial assets that are not carried at fair value because their fair value can not be reliably measured. If there is objective evidence that such investments are impaired, the impairment loss is calculated as the difference between the carrying amount of the investment and the present value of the estimated future cash flows discounted at the current market rate of return for a similar financial asset.

All impairment losses in respect of these investments are recognized in profit or loss and can not be reversed.

### *(iii) Available-for-sale financial assets*

Impairment losses on available-for-sale financial assets are recognised by transferring the cumulative loss that is recognised in other comprehensive income to profit or loss as a reclassification adjustment. The cumulative loss that is reclassified from other comprehensive income to profit or loss is the difference between the acquisition cost, net of any principal repayment and amortisation, and the current fair value, less any impairment loss previously recognised in profit or loss. Changes in impairment provisions attributable to time value are reflected as a component of interest income.

For an investment in an equity security available-for-sale, a significant or prolonged decline in its fair value below its cost is objective evidence of impairment.

If, in a subsequent period, the fair value of an impaired available-for-sale debt security increases and the increase can be objectively related to an event occurring after the impairment loss was recognised in profit or loss, the impairment loss is reversed, with the amount of the reversal recognised in profit or loss. However, any subsequent recovery in the fair value of an impaired available-for-sale equity security is recognised in other comprehensive income.

### *(iv) Non financial assets*

Non financial assets, other than deferred taxes, are assessed at each reporting date for any indications of impairment. The recoverable amount of non financial assets is the greater of their fair value less costs to sell and value in use. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset. For an asset that does not generate cash inflows largely independent of those from other assets, the recoverable amount is determined for the cash-generating unit to which the asset belongs. An impairment loss is recognised when the carrying amount of an asset or its cash-generating unit exceeds its recoverable amount.

All impairment losses in respect of non financial assets are recognized in profit or loss and reversed only if there has been a change in the estimates used to determine the recoverable amount. Any impairment loss reversed is only reversed to the extent that the asset's carrying amount does not exceed the carrying amount that would have been determined, net of depreciation or amortisation, if no impairment loss had been recognised.

## (g) Provisions

A provision is recognised in the statement of financial position when the Bank has a legal or constructive obligation as a result of a past event, and it is probable that an outflow of economic benefits will be required to settle the obligation. If the effect is material, provisions are determined by discounting the expected future cash flows at a pre-tax rate that reflects current market assessments of the time value of money and, where appropriate, the risks specific to the liability.

## (h) Credit related commitments

In the normal course of business, the Bank enters into credit related commitments, comprising undrawn loan commitments, letters of credit and guarantees, and provides other forms of credit insurance.

Financial guarantees are contracts that require the Bank to make specified payments to reimburse the holder for a loss it incurs because a specified debtor fails to make payment when due in accordance with the terms of a debt instrument.

A financial guarantee liability is recognised initially at fair value net of associated transaction costs, and is measured subsequently at the higher of the amount initially recognised less cumulative amortisation or the amount of provision for losses under the guarantee. Provisions for losses under financial guarantees and other credit related commitments are recognised when losses are considered probable and can be measured reliably.

Financial guarantee liabilities and provisions for other credit related commitment are included in other liabilities.

Loan commitments are not recognised, except for the following:

- loan commitments that the Bank designates as financial liabilities at fair value through profit or loss
- if the Bank has a past practice of selling the assets resulting from its loan commitments shortly after origination, then the loan commitments in the same class are treated as derivative instruments
- loan commitments that can be settled net in cash or by delivering or issuing another financial instrument
- commitments to provide a loan at a below-market interest rate.

## (i) Share capital

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

### *(i) Dividends*

The ability of the Bank to declare and pay dividends is subject to the rules and regulations of the Armenian legislation.

Dividends in relation to ordinary shares are reflected as an appropriation of retained earnings in the period when they are declared.

### *(ii) General reserve*

General reserve is created in accordance with regulatory requirement as at each year-end and reflected as an appropriation of retained earnings.

## (j) Taxation

Income tax comprises current and deferred tax. Income tax is recognised in profit or loss except to the extent that it relates to items of other comprehensive income or transactions with shareholders recognised directly in equity, in which case it is recognised within other comprehensive income or directly within equity.

Current tax expense is the expected tax payable on the taxable income for the year, using tax rates enacted or substantially enacted at the reporting date, and any adjustment to tax payable in respect of previous years.

Deferred tax is recognised in respect of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes. Deferred tax is not recognised for the initial recognition of assets or liabilities that affect neither accounting nor taxable profit. Deferred tax is measured at the tax rates that are expected to be applied to the temporary differences when they reverse, based on the laws that have been enacted or substantively enacted by the reporting date.

A deferred tax asset is recognised only to the extent that it is probable that future taxable profits will be available against which the temporary differences, unused tax losses and credits can be utilised. Deferred tax assets are reduced to the extent that it is no longer probable that the related tax benefit will be realised.

## (k) Income and expense recognition

Interest income and expense are recognised in profit or loss using the effective interest method.

Loan origination fees, loan servicing fees and other fees that are considered to be integral to the overall profitability of a loan, together with the related transaction costs, are deferred and amortized to interest income over the estimated life of the financial instrument using the effective interest method.

Other fees, commissions and other income and expense items are recognised in profit or loss when the corresponding service is provided.

Dividend income is recognised in profit or loss on the date that the dividend is declared.

Payments made under operating leases are recognised in profit or loss on a straight-line basis over the term of the lease. Lease incentives received are recognised as an integral part of the total lease expense, over the term of the lease.

## (l) Employee benefits

### *Share-based payment transactions*

Share-based payment arrangements in which the Bank receives goods or services as consideration for equity instruments in the ultimate parent company are accounted for as equity-settled share-based payment transactions.

The grant date fair value of share-based payment awards granted to employees is recognized as an employee expense, with a corresponding increase in equity, over the period that the employees unconditionally become entitled to the awards. The amount recognized as an expense is adjusted to reflect the number of awards for which the related service and non-market vesting conditions are expected to be met, such that the amount ultimately recognized as an expense is based on the number of awards that do meet the related service and non-market performance conditions at the vesting date.

If upon vesting recharge is arranged to fund a group entity, the payment is recorded in equity. The difference between settlement amount and the grant date fair value of share-based payment is recorded in retained earnings in the year the share-based payment award is vested and settled.

## (m) New standards and interpretations not yet adopted

A number of new standards, amendments to standards and interpretations are not yet effective as at 31 December 2014, and are not applied in preparing these financial statements. Of these pronouncements, potentially the following will have an impact on the financial position and performance. The Bank plans to adopt these pronouncements when they become effective.

- IFRS 9 *Financial Instruments* has been issued in phases and is intended ultimately to replace International Financial Reporting Standard IAS 39 *Financial Instruments: Recognition and Measurement*. The first phase of IFRS 9 was issued in November 2009 and relates to the classification and measurement of financial assets. The second phase regarding the classification and measurement of financial liabilities was published in October 2010. The third phase of IFRS 9 was issued in November 2013 and relates to general hedge accounting. The standard was finalized and published in July 2014. The final phase relates to a new expected credit loss model for calculating impairment. The Bank recognises that the new standard introduces many changes to accounting for financial instruments and may have a significant impact on the financial statements. The Bank has not analysed the impact of these changes yet. The Bank does not intend to adopt this standard early. The standard will be effective for annual periods beginning on or after 1 January 2018 and will be applied retrospectively with some exemptions.
- Various *Improvements to IFRSs* have been dealt with on a standard-by-standard basis. The Bank believes that the impact of the amendments will not be significant on its financial position or performance.

# 4 Net interest income

| | 2014<br>AMD'000 | 2013<br>AMD'000 |
|---|---|---|
| **Interest income** | | |
| Loans to customers | 15,841,974 | 14,415,608 |
| Available-for-sale financial assets | 3,443,696 | 3,702,680 |
| Loans and advances to banks | 563,913 | 594,645 |
| Financial instruments at fair value through profit or loss | 36,827 | 78,638 |
| Cash and cash equivalents | 55,673 | 49,291 |
| | **19,942,083** | **18,840,862** |
| **Interest expense** | | |
| Current accounts and deposits from customers | 3,838,993 | 3,304,520 |
| Deposits and balances from banks and other financial institutions | 1,153,860 | 1,185,235 |
| Amounts payable under repurchase agreements | 102,414 | - |
| | **5,095,267** | **4,489,755** |

Included within various line items under interest income for the year ended 31 December 2014 is a total of AMD 435,389 thousand (2013: AMD 405,392 thousand) accrued on impaired financial assets.

# 5 Fee and commission income

| | 2014<br>AMD'000 | 2013<br>AMD'000 |
|---|---|---|
| Credit facilities | 707,533 | 642,524 |
| Remittances | 610,001 | 683,031 |
| Letters of credits and guarantees | 496,007 | 334,165 |
| Credit cards | 478,129 | 518,056 |
| Account services | 240,084 | 289,690 |
| ATM services | 47,197 | 52,637 |
| Insurance agency | 17,398 | 19,337 |
| Other | 90,389 | 100,745 |
| | **2,686,738** | **2,640,185** |

# 6 Fee and commission expense

| | 2014<br>AMD'000 | 2013<br>AMD'000 |
|---|---|---|
| Card transactions fees | 278,518 | 271,552 |
| Other | 267,904 | 189,724 |
| | **546,422** | **461,276** |

# 7 Net gain on financial instruments at fair value through profit or loss

| | 2014<br>AMD'000 | 2013<br>AMD'000 |
|---|---|---|
| Debt financial instruments | (54,279) | 19,326 |
| Foreign currency contracts | 1,260,390 | 271,328 |
| | **1,206,111** | **290,654** |

# 8 Net foreign exchange gain

| | 2014<br>AMD'000 | 2013<br>AMD'000 |
|---|---|---|
| Gain on spot transactions | 1,772,880 | 1,509,589 |
| Net loss from revaluation of financial assets and liabilities | (1,132,682) | (139,160) |
| | **640,198** | **1,370,429** |

# 9 Impairment losses

| | 2014<br>AMD'000 | 2013<br>AMD'000 |
|---|---|---|
| Loans to customers (note 17) | (2,509,938) | (545,129) |
| Other assets | (19,642) | (6,829) |
| | **(2,529,580)** | **(551,958)** |

# 10 Personnel expenses

| | 2014<br>AMD'000 | 2013<br>AMD'000 |
|---|---|---|
| Employee compensation | 3,776,596 | 3,439,331 |
| | **3,776,596** | **3,439,331** |

# 11 Other general administrative expenses

| | 2014 AMD'000 | 2013 AMD'000 |
|---|---|---|
| HSBC Group IT support costs and other charges | 1,447,779 | 1,575,998 |
| Depreciation and amortization | 894,511 | 846,089 |
| Rent of property and equipment | 538,570 | 513,908 |
| Advertising and marketing | 121,123 | 209,844 |
| Communication and information services | 147,975 | 150,961 |
| Insurance | 90,982 | 98,710 |
| Professional services | 67,875 | 65,365 |
| IT related costs | 69,627 | 76,150 |
| Security | 72,634 | 71,212 |
| Utilities | 75,635 | 67,565 |
| Repair and maintenance | 66,608 | 51,275 |
| Currency shipment charges | 31,012 | 33,824 |
| Travel and entertainment expenses | 49,777 | 61,963 |
| Office supplies | 36,232 | 32,104 |
| Charity and sponsorship | 37,666 | 40,417 |
| Other | 159,222 | 119,054 |
| | **3,907,228** | **4,014,439** |

# 12 Income tax expense

| | 2014 AMD'000 | 2013 AMD'000 |
|---|---|---|
| **Current tax expense** | | |
| Current year tax expense | 2,066,000 | 2,111,088 |
| Current tax expense (over) under provided in prior years | (113,897) | 62,456 |
| Origination and reversal of temporary differences | 26,453 | (39,461) |
| **Total income tax expense** | **1,978,556** | **2,134,083** |

In 2014 the applicable tax rate for current and deferred tax is 20% (2013: 20%).

**Reconciliation of effective tax rate:**

| | 2014 AMD'000 | % | 2013 AMD'000 | % |
|---|---|---|---|---|
| Profit before income tax | **8,544,005** | | **10,143,586** | |
| | | | | |
| Income tax at the applicable tax rate | 1,708,801 | 20.0 | 2,028,717 | 20.0 |
| Non-deductible costs | 383,652 | 4.5 | 42,910 | 0.0 |
| (Over) under provided in prior years | (113,897) | (1.3) | 62,456 | 1.0 |
| | **1,978,556** | **23.2** | **2,134,083** | **21.0** |

## (a) Deferred tax asset and liability

Temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes give rise to net deferred tax liabilities as of 31 December 2014 and 2013.

The deductible temporary differences do not expire under current tax legislation.

Movements in temporary differences during the years ended 31 December 2014 and 2013 are presented as follows:

| AMD'000 | Balance 1 January 2014 | Recognised in profit or loss | Recognised in other comprehensive income | Balance 31 December 2014 |
|---|---|---|---|---|
| Cash and cash equivalents | 46,513 | 8,522 | - | 55,035 |
| Financial instruments at fair value through profit or loss | 33,667 | 155,676 | - | 189,343 |
| Available-for-sale financial assets | 271,973 | - | (222,431) | 49,542 |
| Loans and advances to banks | 3,921 | 5,574 | - | 9,495 |
| Loans to customers | 1,172,773 | (135,159) | - | 1,037,614 |
| Property and equipment | (121,195) | (27,335) | - | (148,530) |
| Other assets | 27,327 | (73) | - | 27,254 |
| Other liabilities | (416,553) | 19,248 | - | (397,305) |
| | **1,018,426** | **26,453** | **(222,431)** | **822,448** |

| AMD'000 | Balance 1 January 2013 | Recognised in profit or loss | Recognised in other comprehensive income | Balance 31 December 2013 |
|---|---|---|---|---|
| Cash and cash equivalents | 19,941 | 26,572 | - | 46,513 |
| Financial instruments at fair value through profit or loss | 20,470 | 13,197 | - | 33,667 |
| Available-for-sale financial assets | 62,938 | - | 209,035 | 271,973 |
| Loans and advances to banks | 5,388 | (1,467) | - | 3,921 |
| Loans to customers | 1,149,806 | 22,967 | - | 1,172,773 |
| Property and equipment | (98,670) | (22,525) | - | (121,195) |
| Other assets | - | 27,327 | - | 27,327 |
| Other liabilities | (311,021) | (105,532) | - | (416,553) |
| | **848,852** | **(39,461)** | **209,035** | **1,018,426** |

### (b) Income tax recognised in other comprehensive income

The tax effects relating to components of other comprehensive income for the years ended 31 December 2014 and 2013 comprise the following:

| | 2014 | | | 2013 | | |
|---|---|---|---|---|---|---|
| **AMD'000** | **Amount before tax** | **Tax expense** | **Amount net-of-tax** | **Amount before tax** | **Tax (expense)/ benefit** | **Amount net-of-tax** |
| Net change in fair value of available-for-sale financial assets | (1,112,156) | 222,431 | (889,725) | 1,034,022 | (206,804) | 827,218 |
| Net change in fair value of available-for-sale financial assets transferred to profit or loss | - | - | - | 11,155 | (2,231) | 8,924 |
| **Other comprehensive income** | **(1,112,156)** | **222,431** | **(889,725)** | **1,045,177** | **(209,035)** | **836,142** |

## 13 Cash and cash equivalents

| | **2014 AMD'000** | **2013 AMD'000** |
|---|---|---|
| **Cash on hand** | **6,943,712** | **5,720,203** |
| **Nostro accounts with the CBA (net of credit card settlement deposit)** | **37,471,347** | **21,076,220** |
| **Nostro accounts with other banks** | | |
| - rated from AA- to AA+ | 25,084,633 | 19,109,971 |
| - rated A- to A+ | 278,595 | 79,342 |
| - rated from BB- to BB+ | - | 471 |
| - not rated | 1,050,410 | 38,380 |
| **Total nostro accounts with other banks** | **26,413,638** | **19,228,164** |
| **Cash equivalents** | | |
| **Term deposit with the CBA** | **-** | **2,500,000** |
| Money market overnight placements | | |
| - rated from AA- to AA+ | 1,032,752 | 735,614 |
| - Not rated | 65,200 | 771,280 |
| - Armenian financial institutions (through NASDAQ OMX Armenia) | - | 2,500,000 |
| **Total cash equivalents** | **1,097,952** | **4,006,894** |
| **Cash and cash equivalents in the statement of cash flows** | **71,926,649** | **52,531,481** |
| Credit card settlement deposit with the CBA | 1,700,000 | 810,000 |
| Accrued interest | 66 | 4,306 |
| **Cash and cash equivalents in the statement of financial position** | **73,626,715** | **53,345,787** |

No cash and cash equivalents are impaired or past due. The above ratings are per Standard & Poor's rating agency ratings.

The nostro accounts include mandatory minimum reserve deposits calculated in accordance with regulations promulgated by the CBA at 2% to 20% from the attracted funds depending on currency. Withdrawal of such reserves is not restricted; however,

the Bank is subject to penalties if the required minimum average balance is not periodically maintained.

As at 31 December 2014, in addition to balances with the CBA, the Bank had one bank (2013: two banks) whose balance exceeded 10% of equity. The gross value of these balances as at 31 December 2014 is AMD 22,884,003 thousand (2013: AMD 18,416,502 thousand).

## 14 Financial instruments at fair value through profit or loss

| | 2014 AMD'000 | 2013 AMD'000 |
|---|---|---|
| **Held by the Bank** | | |
| **ASSETS** | | |
| **Debt and other fixed-income instruments** | | |
| Armenian Government treasury bills | 461,065 | 671,642 |
| **Derivative financial instruments** | | |
| Foreign currency contracts | 1,102,798 | 149,982 |
| | **1,563,863** | **821,624** |

Financial instruments at fair value through profit or loss comprise financial instruments held for trading.

No financial assets at fair value through profit or loss are past due.

### Foreign currency contracts

The table below summarises, by major currencies, the contractual amounts of forward currency contracts outstanding at 31 December with details of the contractual exchange rates and remaining periods to maturity. Foreign currency amounts presented below are translated at rates ruling at the reporting date. The resultant unrealised gains and losses on these unmatured contracts, along with the amounts payable and receivable on the matured but unsettled contracts, are recognised in profit or loss and in financial instruments at fair value through profit or loss, as appropriate.

| | Notional amount | | Weighted average contractual exchange rates | |
|---|---|---|---|---|
| | 2014 AMD'000 | 2013 AMD'000 | 2014 | 2013 |
| **Buy USD sell AMD** | | | | |
| Less than 3 months | 2,328,111 | 1,867,251 | 464.7 | 404.0 |
| Between 3 and 12 months | 4,314,345 | 3,536,433 | 397.1 | 398.3 |
| **Buy AMD sell USD** | | | | |
| Less than 3 months | 1,044,940 | 1,972,807 | 548.8 | 407.5 |

# 15 Available-for-sale financial assets

| | 2014<br>AMD'000 | 2013<br>AMD'000 |
|---|---|---|
| **Held by the Bank** | | |
| **Debt and other fixed-income instruments** | | |
| **Armenian Government treasury bills** | **18,116,327** | **31,252,983** |
| **Corporate bonds** | | |
| International financial institutions | 1,404,695 | 375,897 |
| Other corporate bonds | 1,182,362 | 869,123 |
| | **20,703,384** | **32,498,003** |
| **Equity instruments – Unquoted** | | |
| ACRA credit reporting | 19,140 | 19,140 |
| Armenian Card | 12,143 | 12,143 |
| SWIFT | 845 | 818 |
| | **32,128** | **32,101** |
| | **20,735,512** | **32,530,104** |
| **Pledged under sale and repurchase agreements** | | |
| **Debt and other fixed-income instruments** | | |
| **Armenian Government treasury bills** | **12,338,544** | **-** |
| | | |
| | **12,338,544** | **-** |

No available-for-sale financial assets are past due or impaired.

## Investments without a determinable fair value

Available-for-sale investments stated at cost comprise unquoted equity securities in the financial services industry. There is no market for these investments and there have not been any recent transactions that provide evidence of the current fair value. In addition, discounted cash flow techniques yield a wide range of fair values due to the uncertainty regarding future cash flows in this industry.

# 16 Loans and advances to banks

| | 2014<br>AMD'000 | 2013<br>AMD'000 |
|---|---|---|
| **Loans and advances** | | |
| Rated from AA- to AA+ | 17,025 | 6,852 |
| Largest 10 Armenian banks | 4,730,678 | 1,952,492 |
| Not rated | 8,662 | 923 |
| **Total loans and advances** | **4,756,365** | **1,960,267** |

No loans and advances to banks are impaired or past due. The above ratings are per Standard & Poor's rating agency ratings.

As at 31 December 2014 the Bank had one bank (2013: no banks) whose balances exceeded 10% of equity. The gross value of these balances as at 31 December 2014 is AMD 4,730,678 thousand (2013: nil).

# 17 Loans to customers

| | 2014 AMD'000 | 2013 AMD'000 |
|---|---|---|
| **Loans to corporate customers** | | |
| Loans to large corporates | 104,904,852 | 89,653,995 |
| Loans to small and medium size companies | 49,048,029 | 41,431,493 |
| **Total loans to corporate customers** | **153,952,881** | **131,085,488** |
| | | |
| **Loans to retail customers** | | |
| Mortgage loans | 15,150,270 | 13,581,388 |
| Credit cards | 2,738,197 | 2,853,494 |
| Construction loans | 1,044,418 | 1,416,178 |
| Auto loans | 834,074 | 494,546 |
| Consumer loans | 2,013,792 | 1,076,224 |
| Other loans to retail customers | 3,450,863 | 1,873,366 |
| **Total loans to retail customers** | **25,231,614** | **21,295,196** |
| | | |
| **Gross loans to customers** | **179,184,495** | **152,380,684** |
| Impairment allowance | (3,198,037) | (847,935) |
| **Net loans to customers** | **175,986,458** | **151,532,749** |

Movements in the loan impairment allowance by classes of loans to customers for the year ended 31 December 2014 are as follows:

| | Loans to corporate customers AMD'000 | Loans to retail customers AMD'000 | Total AMD'000 |
|---|---|---|---|
| Balance at the beginning of the year | **596,309** | **251,626** | **847,935** |
| Net charge | 2,366,974 | 142,964 | 2,509,938 |
| Net write-offs | - | (322,909) | (322,909) |
| Effect of foreign currency translation | 162,477 | 596 | 163,073 |
| **Balance at the end of the year** | **3,125,760** | **72,277** | **3,198,037** |

Movements in the loan impairment allowance by classes of loans to customers for the year ended 31 December 2013 are as follows:

| | Loans to corporate customers AMD'000 | Loans to retail customers AMD'000 | Total AMD'000 |
|---|---|---|---|
| Balance at the beginning of the year | **133,960** | **228,636** | **362,596** |
| Net charge | 462,083 | 83,046 | 545,129 |
| Net write-offs | - | (60,161) | (60,161) |
| Effect of foreign currency translation | 266 | 105 | 371 |
| **Balance at the end of the year** | **596,309** | **251,626** | **847,935** |

## (a) Credit quality of loans to customers

The following table provides information on the credit quality of loans to customers as at 31 December 2014:

| | Gross loans<br>AMD'000 | Impairment allowance<br>AMD'000 | Net loans<br>AMD'000 | Impairment allowance to gross loans<br>% |
|---|---|---|---|---|
| **Loans to corporate customers** | | | | |
| **Loans to large corporates** | | | | |
| **Loans without individual signs of impairment** | | | | |
| - not overdue | 99,883,754 | (311,743) | 99,572,011 | 0.3 |
| **Overdue but not impaired loans** | | | | |
| - overdue 30-89 days | 372,964 | (1,175) | 371,789 | 0.3 |
| - overdue 90-179 days | 171,328 | (540) | 170,788 | 0.3 |
| - overdue more than 360 days | 238,072 | (750) | 237,322 | 0.3 |
| **Total overdue but not impaired loans** | **782,364** | **(2,465)** | **779,899** | **0.3** |
| **Overdue and impaired loans** | | | | |
| - overdue 30-89 days | 27,451 | (87) | 27,364 | 0.3 |
| - overdue 180-359 days | 3,090,661 | (186,271) | 2,904,390 | 6.0 |
| - overdue more than 360 days | 1,120,622 | (15,881) | 1,104,741 | 1.4 |
| **Total overdue and impaired loans** | **4,238,734** | **(202,239)** | **4,036,495** | **4.8** |
| | | | | |
| **Total loans to large corporates** | **104,904,852** | **(516,447)** | **104,388,405** | **0.5** |
| | | | | |
| **Loans to small and medium size companies** | | | | |
| **Loans without individual signs of impairment** | | | | |
| - not overdue | 36,310,790 | (110,891) | 36,199,899 | 0.3 |
| **Overdue but not impaired loans** | | | | |
| - overdue 30-89 days | 111,855 | (353) | 111,502 | 0.3 |
| - overdue 90-179 days | 351,915 | (1,109) | 350,806 | 0.3 |
| - overdue 180-359 days | 334,355 | (1,054) | 333,301 | 0.3 |
| - overdue more than 360 days | 227,452 | (717) | 226,735 | 0.3 |
| **Total overdue but not impaired loans** | **1,025,577** | **(3,233)** | **1,022,344** | **0.3** |
| **Overdue and impaired loans** | | | | |
| - overdue less than 30 days | 94,994 | (299) | 94,695 | 0.3 |
| - overdue 90-179 days | 109,056 | (343) | 108,713 | 0.3 |
| - overdue 180-359 days | 1,970,075 | (265,024) | 1,705,051 | 13.5 |
| - overdue more than 360 days | 9,537,537 | (2,229,523) | 7,308,014 | 23.4 |
| **Total overdue and impaired loans** | **11,711,662** | **(2,495,189)** | **9,216,473** | **21.3** |
| **Total loans to small and medium size companies** | **49,048,029** | **(2,609,313)** | **46,438,716** | **5.3** |
| **Total loans to corporate customers** | **153,952,881** | **(3,125,760)** | **150,827,121** | **2.0** |

| | Gross loans AMD'000 | Impairment allowance AMD'000 | Net loans AMD'000 | Impairment allowance to gross loans % |
|---|---|---|---|---|
| **Loans to retail customers** | | | | |
| **Mortgage loans** | | | | |
| - not past due | 14,412,734 | (5,865) | 14,406,869 | 0.0 |
| - overdue less than 30 days | 50,664 | (21) | 50,643 | 0.0 |
| - overdue 30-89 days | 107,112 | (44) | 107,068 | 0.0 |
| - overdue 90-179 days | 100,591 | (3,354) | 97,237 | 3.3 |
| - overdue 180-359 days | 158,863 | (64) | 158,799 | 0.0 |
| - overdue more than 360 days | 320,306 | (17,777) | 302,529 | 5.6 |
| **Total mortgage loans** | **15,150,270** | **(27,125)** | **15,123,145** | **0.2** |
| **Credit cards** | | | | |
| - not past due | 2,691,784 | (12,519) | 2,679,265 | 0.5 |
| - overdue less than 30 days | 16,949 | (79) | 16,870 | 0.5 |
| - overdue 30-89 days | 18,029 | (84) | 17,945 | 0.5 |
| - overdue 90-179 days | 11,435 | (53) | 11,382 | 0.5 |
| **Total credit cards** | **2,738,197** | **(12,735)** | **2,725,462** | **0.5** |
| **Construction loans** | | | | |
| - not past due | 934,699 | (672) | 934,027 | 0.1 |
| - overdue less than 30 days | 21,451 | (15) | 21,436 | 0.1 |
| - overdue 30-89 days | 25,582 | (18) | 25,564 | 0.1 |
| - overdue 180-359 days | 13,556 | (10) | 13,546 | 0.1 |
| - overdue more than 360 days | 49,130 | (3,942) | 45,188 | 8.0 |
| **Total construction loans** | **1,044,418** | **(4,657)** | **1,039,761** | **0.4** |
| **Auto loans** | | | | |
| - not past due | 808,828 | (4,280) | 804,548 | 0.5 |
| - overdue less than 30 days | 531 | (3) | 528 | 0.6 |
| - overdue 30-89 days | 3,476 | (18) | 3,458 | 0.5 |
| - overdue 90-179 days | 2,689 | (581) | 2,108 | 21.6 |
| - overdue more than 360 days | 18,550 | (13,266) | 5,284 | 71.5 |
| **Total auto loans** | **834,074** | **(18,148)** | **815,926** | **2.2** |
| **Consumer loans** | | | | |
| - not past due | 1,999,261 | (3,585) | 1,995,676 | 0.2 |
| - overdue less than 30 days | 7,428 | (13) | 7,415 | 0.2 |
| - overdue 30-89 days | 2,697 | (5) | 2,692 | 0.2 |
| - overdue 90-179 days | 392 | (1) | 391 | 0.3 |
| - overdue 180-359 days | 4,014 | (7) | 4,007 | 0.2 |
| **Total consumer loans** | **2,013,792** | **(3,611)** | **2,010,181** | **0.2** |
| **Other loans to retail customers** | | | | |
| - not past due | 3,402,056 | (2,444) | 3,399,612 | 0.1 |
| - overdue 30-89 days | 1,834 | (1) | 1,833 | 0.1 |
| - overdue 90-179 days | 45,981 | (3,555) | 42,426 | 7.7 |
| - overdue 180-359 days | 992 | (1) | 991 | 0.1 |
| **Total other loans to retail customers** | **3,450,863** | **(6,001)** | **3,444,862** | **0.2** |
| **Total loans to retail customers** | **25,231,614** | **(72,277)** | **25,159,337** | **0.3** |
| **Total loans to customers** | **179,184,495** | **(3,198,037)** | **175,986,458** | **1.8** |

The following table provides information on the credit quality of loans to customers as at 31 December 2013:

| | Gross loans | Impairment allowance | Net loans | Impairment allowance to gross loans |
|---|---|---|---|---|
| | AMD'000 | AMD'000 | AMD'000 | % |
| **Loans to corporate customers** | | | | |
| **Loans to large corporates** | | | | |
| **Loans without individual signs of impairment** | | | | |
| - not overdue | 74,515,695 | - | 74,515,695 | - |
| **Overdue but not impaired loans** | | | | |
| - overdue less than 30 days | 295,223 | - | 295,223 | - |
| - overdue 30-89 days | 2,235,248 | - | 2,235,248 | - |
| - overdue 180-359 days | 7,302,172 | - | 7,302,172 | - |
| **Total overdue but not impaired loans** | **9,832,643** | **-** | **9,832,643** | **-** |
| **Overdue and impaired loans** | | | | |
| - overdue 90-179 days | 3,718,783 | (68,148) | 3,650,635 | 1.8 |
| - overdue 180-359 days | 807,597 | (44,720) | 762,877 | 5.5 |
| - overdue more than 360 days | 779,277 | (317,212) | 462,065 | 40.7 |
| **Total overdue and impaired loans** | **5,305,657** | **(430,080)** | **4,875,577** | **8.1** |
| | | | | |
| **Total loans to large corporates** | **89,653,995** | **(430,080)** | **89,223,915** | **0.5** |
| | | | | |
| **Loans to small and medium size companies** | | | | |
| **Loans without individual signs of impairment** | | | | |
| - not overdue | 37,987,708 | - | 37,987,708 | - |
| **Overdue but not impaired loans** | | | | |
| - overdue less than 30 days | 27,124 | - | 27,124 | - |
| - overdue 30-89 days | 53,214 | - | 53,214 | - |
| - overdue 90-179 days | 299,101 | - | 299,101 | - |
| - overdue 180-359 days | 1,444,711 | - | 1,444,711 | - |
| - overdue more than 360 days | 206,937 | - | 206,937 | - |
| **Total overdue but not impaired loans** | **2,031,087** | **-** | **2,031,087** | **-** |
| **Overdue and impaired loans** | | | | |
| - overdue more than 360 days | 1,412,698 | (166,229) | 1,246,469 | 11.8 |
| **Total overdue and impaired loans** | **1,412,698** | **(166,229)** | **1,246,469** | **11.8** |
| **Total loans to small and medium size companies** | **41,431,493** | **(166,229)** | **41,265,264** | **0.4** |
| **Total loans to corporate customers** | **131,085,488** | **(596,309)** | **130,489,179** | **0.5** |

| | Gross loans AMD'000 | Impairment allowance AMD'000 | Net loans AMD'000 | Impairment allowance to gross loans % |
|---|---|---|---|---|
| **Loans to retail customers** | | | | |
| **Mortgage loans** | | | | |
| - not past due | 12,849,203 | (3,057) | 12,846,146 | 0.0 |
| - overdue less than 30 days | 77,153 | (101) | 77,052 | 0.1 |
| - overdue 30-89 days | 18,525 | (9) | 18,516 | 0.0 |
| - overdue 90-179 days | 19,164 | - | 19,164 | 0.0 |
| - overdue more than 180 days | 617,343 | (60,249) | 557,094 | 9.8 |
| **Total mortgage loans** | **13,581,388** | **(63,416)** | **13,517,972** | **0.5** |
| **Credit cards** | | | | |
| - not past due | 2,752,064 | (26,646) | 2,725,418 | 1.0 |
| - overdue less than 30 days | 41,228 | (204) | 41,024 | 0.5 |
| - overdue 30-89 days | 27,300 | (215) | 27,085 | 0.8 |
| - overdue 90-179 days | 19,153 | (428) | 18,725 | 2.2 |
| - overdue more than 180 days | 13,749 | (13,230) | 519 | 96.2 |
| **Total credit cards** | **2,853,494** | **(40,723)** | **2,812,771** | **1.4** |
| **Construction loans** | | | | |
| - not past due | 1,190,305 | (305) | 1,190,000 | 0.0 |
| - overdue more than 180 days | 225,873 | (111,679) | 114,194 | 49.4 |
| **Total construction loans** | **1,416,178** | **(111,984)** | **1,304,194** | **7.9** |
| **Auto loans** | | | | |
| - not past due | 458,139 | (10,233) | 447,906 | 2.2 |
| - overdue less than 30 days | 3,124 | (159) | 2,965 | 5.1 |
| - overdue 30-89 days | 851 | (20) | 831 | 2.4 |
| - overdue more than 180 days | 32,432 | (18,952) | 13,480 | 58.4 |
| **Total auto loans** | **494,546** | **(29,364)** | **465,182** | **5.9** |
| **Consumer loans** | | | | |
| - not past due | 1,061,458 | (2,699) | 1,058,759 | 0.3 |
| - overdue less than 30 days | 2,598 | (22) | 2,576 | 0.8 |
| - overdue 30-89 days | 3,512 | (14) | 3,498 | 0.4 |
| - overdue more than 180 days | 8,656 | (2,937) | 5,719 | 33.9 |
| **Total consumer loans** | **1,076,224** | **(5,672)** | **1,070,552** | **0.5** |
| **Other loans to retail customers** | | | | |
| - not past due | 1,865,115 | (453) | 1,864,662 | 0.0 |
| - overdue less than 30 days | 5,393 | (13) | 5,380 | 0.2 |
| - overdue 30-89 days | 2,858 | (1) | 2,857 | 0.0 |
| **Total other loans to retail customers** | **1,873,366** | **(467)** | **1,872,899** | **0.0** |
| **Total loans to retail customers** | **21,295,196** | **(251,626)** | **21,043,570** | **1.2** |
| | | | | |
| **Total loans to customers** | **152,380,684** | **(847,935)** | **151,532,749** | **0.6** |

## (b) Key assumptions and judgments for estimating the loan impairment

### *(i) Loans to corporate customers*

Loan impairment results from one or more events that occurred after the initial recognition of the loan and that have an impact on the estimated future cash flows associated with the loan, and that can be reliably estimated. Loans without individual signs of impairment do not have objective evidence of impairment that can be directly attributed to them.

The objective indicators of loan impairment for loans to corporate customers include the following:

- Overdue payments under the loan agreement
- Significant difficulties in the financial conditions of the borrower
- Significant deterioration in business environment, negative changes in the borrower's markets.

The Bank estimates loan impairment for loans to corporate customers based on an analysis of the future cash flows (including estimated foreclosure value of collateral in case the Bank will conclude that cash flows from the business activity of the borrower is not sufficient to repay the loan) for loans with individual signs of impairment and based on its past loss experience for portfolios of loans for which no indications of impairment has been identified.

In determining the impairment allowance for loans to corporate customers, management makes the following key assumptions:

- Historical annual loss rate of 0.50% for commercial banking portfolio and 0% for global banking portfolio are determined based on the previous 60 months credit losses.
- Estimated emergence periods of 9 months is defined for whole portfolio.
- A discount up to 30% to the appraised value if the asset pledged is sold. The discount is computed based on several assumptions, including, but not limited to, property type, liquidity and location
- A delay of 12 to 24 months in obtaining proceeds from the foreclosure of collateral for loans with individual signs of impairment.

Changes in these estimates could affect the loan impairment provision. For example, to the extent that the net present value of the estimated cash flows differs by minus one percent, the impairment allowance on loans to corporate customers as at 31 December 2014 would be AMD 1,508,271 thousand higher (2013: AMD 1,304,892 thousand higher).

### *(ii) Loans to retail customers*

The Bank estimates loan impairment for loans to retail customers based on Historical Loss Rate (HLR) methodology for all unsecured loans and secured loans with up to 90 days delinquency and discounted cash-flow (DCF) methodology is applied for secured assets that are 90 or more days past due. The significant assumptions used in determining the impairment losses for loans to retail customers as at 31 December 2014 include:

- Historical annual loss rates of 0.2% for mortgage and other loans secured by real estate, 1.33% for auto loans, 0.24% for consumer loans and 0.82% for credit cards are determined based on the previous 60 months loss data.

- Estimated emergence periods of 3 months for mortgage and other loans secured by real estate, 5 months for car loans, 6 months for unsecured products between occurrence of an impairment loss and identification of the loss.

- In case of DCF it is expected that the cash flow from the sale of the pledged asset will flow in 12 months' time after the repossession decision is made. If property liquidation values provided by the valuation agency are available, then that value is used for discounting, otherwise the average market price per square meter is used by applying a reduction of 20% from market value.

- Unsecured loans overdue more than 180 days are considered as a loss.

Changes in these estimates could affect the loan impairment provision. For example, to the extent that the net present value of the estimated cash flows differs by minus three percent, the impairment allowance on loans to retail customers as at 31 December 2014 would be AMD 754,780 thousand higher (2013: AMD 631,307 thousand higher).

## (c) Analysis of collateral and other credit enhancements

### *(i) Loans to corporate customers*

The following tables provides fair value information on collateral and other credit enhancements securing loans to corporate customers, net of impairment, by types of collateral:

| **31 December 2014**<br><br>**AMD'000** | **Loans to customers, carrying amount** | **Fair value of collateral assessed in the reporting period** |
|---|---|---|
| Loans without individual signs of impairment | | |
| Borrower settlement account | 2,795,024 | - |
| Cash and deposits | 3,629 | 3,629 |
| Armenian Government treasury bills | 2,091,556 | 2,091,556 |
| Real estate | 121,544,185 | 121,544,185 |
| Motor vehicles | 436,839 | 436,839 |
| Equipment | 2,313,767 | 2,313,767 |
| Stock | 2,351,673 | 2,351,673 |
| Other collateral | 1,116,087 | 1,116,087 |
| State guarantees | 1,022,535 | Not applicable |
| Corporate guarantees (unrated) | 1,233,720 | Not applicable |
| No collateral or other credit enhancement | 862,895 | - |
| **Total loans without individual signs of impairment** | **135,771,910** | **129,857,736** |
| Overdue but not impaired loans | | |
| Real estate | 1,430,454 | 1,430,454 |
| Stock | 371,789 | 371,789 |
| **Total overdue but not impaired loans** | **1,802,243** | **1,802,243** |
| Overdue and impaired loans | | |
| Real estate | 13,245,965 | 13,245,965 |
| Motor vehicles | 7,003 | 7,003 |
| **Total overdue and impaired loans** | **13,252,968** | **13,252,968** |
| | | |
| **Total loans to corporate customers** | **150,827,121** | **144,912,947** |

| 31 December 2013<br><br>AMD'000 | Loans to customers, carrying amount | Fair value of collateral assessed in the reporting period |
|---|---|---|
| Loans without individual signs of impairment | | |
| Borrower settlement account | 5,107,333 | - |
| Cash and deposits | 206,360 | 206,360 |
| Armenian Government treasury bills | 2,257,921 | 2,257,921 |
| Real estate | 95,920,119 | 95,727,182 |
| Motor vehicles | 175,909 | 175,909 |
| Equipment | 3,360,111 | 3,360,111 |
| Stock | 2,465,281 | 2,465,281 |
| Other collateral | 188,625 | 188,625 |
| State guarantees | 994,278 | Not applicable |
| Corporate guarantees (unrated) | 1,617,071 | Not applicable |
| No collateral or other credit enhancement | 210,395 | - |
| **Total loans without individual signs of impairment** | **112,503,403** | **104,381,389** |
| Overdue but not impaired loans | | |
| Real estate | 11,836,606 | 11,403,893 |
| No collateral or other credit enhancement | 27,124 | - |
| **Total overdue but not impaired loans** | **11,863,730** | **11,403,893** |
| Overdue and impaired loans | | |
| Real estate | 5,715,019 | 5,715,019 |
| Equipment | 261,711 | 261,711 |
| Stock | 90,000 | 90,000 |
| Corporate guarantees (unrated) | 55,316 | - |
| **Total overdue and impaired loans** | **6,122,046** | **6,066,730** |
| | | |
| **Total loans to corporate customers** | **130,489,179** | **121,852,012** |

The tables above exclude overcollateralization. For loans secured by multiple types of collateral, collateral that is most relevant for impairment assessment is disclosed.

### *(ii) Loans to retail customers*

Mortgage, contsruction and other loans to retail customers are secured by real estate. The Bank's policy is to issue mortgage and construction loans with a loan-to-value ratio of a maximum of 80%.

The fair value of collateral is at least equal to carrying amounts of individual mortgage and construction loans as at 31 December 2014 and 2013.

For mortgage and contsruction loans past due more than 90 days the Bank updates the appraised values of collateral obtained at inception of the loans to the current values considering the approximate changes in property values. The Bank also obtains specific individual valuation of collateral at each reporting date for significant secured loans.

Credit card loans are not secured.

Auto loans are secured by the underlying cars. The Bank's policy is to issue auto loans with a loan-to-value ratio of a maximum of 70%.

Consumer loans represent unsecured personal loans.

## (d) Industry and geographical analysis of the loan portfolio

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

| | 2014<br>AMD'000 | 2013<br>AMD'000 |
|---|---|---|
| Trade | 38,104,411 | 38,175,086 |
| Construction | 19,981,282 | 15,118,663 |
| Food and beverages | 31,572,849 | 25,586,250 |
| Services | 26,499,901 | 21,038,945 |
| Energy | 9,358,077 | 8,201,372 |
| Manufacturing | 15,160,028 | 11,232,459 |
| Agriculture | 4,512,798 | 5,946,094 |
| Finance | 2,617,960 | 2,956,125 |
| Chemicals | 62,041 | 173,976 |
| Other | 6,083,534 | 2,656,518 |
| Loans to individuals | 25,231,614 | 21,295,196 |
| | **179,184,495** | **152,380,684** |
| Impairment allowance | (3,198,037) | (847,935) |
| | **175,986,458** | **151,532,749** |

## (e) Significant credit exposures

As at 31 December 2014 the Bank has seven borrowers or groups of connected borrowers (2013: eight), whose loan balances exceed 10% of equity. The gross value of these loans as at 31 December 2014 is AMD 39,858,526 thousand (2013: AMD 41,879,080 thousand).

## (f) Assets under lien

As at 31 December 2014 loans to customers with a gross value of AMD 337,102 thousand (2013: AMD 246,895 thousand) serve as collateral for loans from banks.

## (g) Loan maturities

The maturity of the loan portfolio is presented in note 25(d), which shows the remaining period from the reporting date to the contractual maturity of the loans. Due to the short-term nature of the loans issued by the Bank, it is likely that many of the loans will be prolonged at maturity. Accordingly, the effective maturity of the loan portfolio may be significantly longer than the term based on contractual terms.

# 18 Property, equipment and intangible assets

| AMD'000 | Land and buildings | Leasehold improvements | Vehicles | Computer equipment | Intangible assets | Other | Total |
|---|---|---|---|---|---|---|---|
| **Cost/revalued amount** | | | | | | | |
| Balance at 1 January 2014 | **1,868,356** | **2,968,553** | **127,213** | **1,449,449** | **2,687,559** | **1,328,375** | **10,429,505** |
| Additions | 7,897 | 8,960 | 39,365 | 175,203 | 433,344 | 47,258 | 712,027 |
| Disposals/write-offs | - | - | - | (13,028) | - | (7,032) | (20,060) |
| **Balance at 31 December 2014** | **1,876,253** | **2,977,513** | **166,578** | **1,611,624** | **3,120,903** | **1,368,601** | **11,121,472** |
| **Depreciation, amortisation and impairment losses** | | | | | | | |
| Balance at 1 January 2014 | **(625,786)** | **(2,074,615)** | **(112,516)** | **(1,160,734)** | **(1,282,306)** | **(1,125,409)** | **(6,381,366)** |
| Depreciation and amortisation charge | (67,504) | (223,874) | (8,940) | (153,464) | (375,049) | (65,680) | (894,511) |
| Disposals/write-offs | - | - | - | 13,028 | - | 6,924 | 19,952 |
| **Balance at 31 December 2014** | **(693,290)** | **(2,298,489)** | **(121,456)** | **(1,301,170)** | **(1,657,355)** | **(1,184,165)** | **(7,255,925)** |
| **Carrying amount** | | | | | | | |
| **At 31 December 2014** | **1,182,963** | **679,024** | **45,122** | **310,454** | **1,463,548** | **184,436** | **3,865,547** |
| **Cost/revalued amount** | | | | | | | |
| Balance at 1 January 2013 | **1,859,368** | **2,953,937** | **140,615** | **1,461,150** | **1,954,657** | **1,270,142** | **9,639,869** |
| Additions | 9,266 | 14,616 | - | 82,754 | 732,902 | 72,113 | 911,651 |
| Disposals/write-offs | (278) | - | (13,402) | (94,455) | - | (13,880) | (122,015) |
| **Balance at 31 December 2013** | **1,868,356** | **2,968,553** | **127,213** | **1,449,449** | **2,687,559** | **1,328,375** | **10,429,505** |
| **Depreciation, amortisation and impairment losses** | | | | | | | |
| Balance at 1 January 2013 | **(562,609)** | **(1,852,924)** | **(119,720)** | **(1,093,182)** | **(983,656)** | **(1,041,161)** | **(5,653,252)** |
| Depreciation and amortisation charge | (63,177) | (221,691) | (6,198) | (158,596) | (298,650) | (97,777) | (846,089) |
| Disposals/write-offs | - | - | 13,402 | 91,044 | - | 13,529 | 117,975 |
| **Balance at 31 December 2013** | **(625,786)** | **(2,074,615)** | **(112,516)** | **(1,160,734)** | **(1,282,306)** | **(1,125,409)** | **(6,381,366)** |
| **Carrying amount** | | | | | | | |
| **At 31 December 2013** | **1,242,570** | **893,938** | **14,697** | **288,715** | **1,405,253** | **202,966** | **4,048,139** |

### Revalued assets

At 31 December 2014 land and buildings were revalued based on the results of an independent appraisal performed by VMRP LLC. The resulting fair values did not differ materially from the carrying value of the land and buildings.

The carrying value of land and buildings as of 31 December 2014, if the land and buildings would not have been revalued would be AMD 1,216,126 thousand (31 December 2013: AMD 1,278,104 thousand).

## 19 Other assets

| | 2014 AMD'000 | 2013 AMD'000 |
|---|---|---|
| Receivables for letters of credit | 13,102,092 | 4,657,790 |
| Prepayments | 198,813 | 212,748 |
| Materials and supplies | 44,045 | 47,965 |
| Other | 391,158 | 266,416 |
| | **13,736,108** | **5,184,919** |

No other assets are past due or impaired.

There are no counterparties in receivables for letters of credit whose balances exceed 10% of equity.

## 20 Deposits and balances from banks

| | 2014 AMD'000 | 2013 AMD'000 |
|---|---|---|
| Loans from banks | 53,679,205 | 37,767,946 |
| Accrued interest | 433,334 | 336,674 |
| Vostro accounts | 922,456 | 90,444 |
| | **55,034,995** | **38,195,064** |

As at 31 December 2014 the Bank has four banks (2013: three banks), whose balances exceed 10% of equity. The gross value of these balances as at 31 December 2014 are AMD 44,611,938 thousand (2013: AMD 30,667,770 thousand).

Included in loans from banks are loans from international and governmental financial institutions and the CBA with arrangements to sub-lend these funds to borrowers for qualifying loans. The qualifying loans under these agreements are loans to small and medium size businesses and the energy efficiency sector. The amount of these borrowings as at 31 December 2014 is AMD 14,904,296 thousand (2013: AMD 15,972,477 thousand).

## 21 Amounts payable under repurchase agreements

| | 2014 AMD'000 | 2013 AMD'000 |
|---|---|---|
| Amounts due to the CBA | 12,013,151 | - |
| | **12,013,151** | **-** |

The Bank has transactions to lend securities and to sell securities under agreements to repurchase and to purchase securities under agreements to resell.

The securities lent or sold under agreements to repurchase are transferred to a third party and the Bank receives cash in exchange. These financial assets may be repledged or resold by counterparties in the absence of default by the Bank, but the counterparty has an obligation to return the securities at the maturity of the contract. The Bank has determined that it retains substantially all the risks and rewards of these securities and therefore has not derecognized them. The cash received is recognised as a financial asset and a financial liability is recognised for the obligation to repay the purchase price for this collateral.

These transactions are conducted under terms that are usual and customary to standard lending, and securities borrowing and lending activities.

## 22 Current accounts and deposits from customers

| | 2014 AMD'000 | 2013 AMD'000 |
|---|---|---|
| Current accounts | | |
| - Retail | 47,820,858 | 44,009,686 |
| - Corporate | 37,391,226 | 39,171,462 |
| Term deposits | | |
| - Retail | 65,325,076 | 55,652,924 |
| - Corporate | 23,602,183 | 20,877,982 |
| Other | 390,710 | 310,708 |
| Accrued interest | 1,130,694 | 974,417 |
| | **175,660,747** | **160,997,179** |

As at 31 December 2014, the Bank maintains customer deposit balances of AMD 2,012,268 thousand (2013: AMD 2,522,371 thousand) that serve as collateral for loans and unrecognised credit instruments granted by the Bank.

As at 31 December 2014, the Bank has two customers (2013: two customers), whose balances exceed 10% of equity. These balances as at 31 December 2014 are AMD 13,025,779 thousand (2013: AMD 11,357,147 thousand).

# 23 Other liabilities

| | 2014 AMD'000 | 2013 AMD'000 |
|---|---|---|
| Payables for letters of credit | 13,102,092 | 4,657,790 |
| Accrued expenses | 858,421 | 864,470 |
| Deferred income | 702,640 | 629,382 |
| Foreign currency derivative contracts at fair value through profit or loss | 128,805 | - |
| Payable to Deposit Guarantee Fund | 53,886 | 48,239 |
| Other | 788,933 | 997,112 |
| | **15,634,777** | **7,196,993** |

# 24 Share capital

## (a) Issued capital

The authorized, issued and outstanding share capital comprises 609,400 ordinary shares of AMD 30.25 thousand each (2013: 609,400 of AMD 30.25 thousand each).

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

## (b) Dividends

Dividends payable are restricted to the maximum retained earnings of the Bank determined according to legislation of the Republic of Armenia.

No dividends were declared and paid during 2014 (2013: AMD 3,075,000 thousand, AMD 5,046 per ordinary share were declared and paid).

# 25 Risk management

Management of risk is fundamental to the business of banking and is an essential element of the Bank's operations. The major risks faced by the Bank are those related to market risk, credit risk and liquidity risk.

## (a) Risk management policies and procedures

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

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

Credit, market and liquidity risks both at portfolio and transactional levels are managed and controlled by the Asset and Liability Management Committee (ALCO) and Risk Management Committee (RMC).

## (b) Market risk

Market risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in market prices. Market risk comprises currency risk, interest rate risk and other price risks. Market risk arises from open positions in interest rate, currency and equity financial instruments, which are exposed to general and specific market movements and changes in the level of volatility of market prices.

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

The Bank manages its market risk by setting open position limits in relation to financial instrument, interest rate maturity and currency positions which are monitored on a regular basis.

The Bank's market risk policy is in line with HSBC Group standards.

### *(i) Interest rate risk*

Interest rate risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in market interest rates.The Bank is exposed to the effects of fluctuations in the prevailing levels of market interest rates on its financial position and cash flows. Interest margins may increase as a result of such changes but may also decrease or create losses in the event that unexpected movements occur.

#### *Interest rate gap analysis*

Interest rate risk is managed principally through monitoring interest rate gaps. A summary of the interest gap position for major financial instruments as at 31 December is as follows:

| AMD'000<br>31 December 2014 | Less than 3 months | 3-12 months | 1-5 years | More than 5 years | Non-interest bearing | Carrying amount |
|---|---|---|---|---|---|---|
| **ASSETS** | | | | | | |
| Cash and cash equivalents | 1,097,952 | - | - | - | 72,528,763 | 73,626,715 |
| Financial instruments at fair value through profit or loss | - | 13,870 | 152,932 | 294,263 | 1,102,798 | 1,563,863 |
| Available-for-sale financial assets | 4,231,412 | 11,535,989 | 16,623,205 | 651,322 | 32,128 | 33,074,056 |
| Loans and advances to banks | 4,756,365 | - | - | - | - | 4,756,365 |
| Loans to customers | 165,814,594 | 3,749,231 | 6,386,136 | 36,497 | - | 175,986,458 |
| | **175,900,323** | **15,299,090** | **23,162,273** | **982,082** | **73,663,689** | **289,007,457** |

| AMD'000 | Less than 3 months | 3-12 months | 1-5 years | More than 5 years | Non-interest bearing | Carrying amount |
|---|---|---|---|---|---|---|
| **LIABILITIES** | | | | | | |
| Deposits and balances from banks | 19,961,945 | 19,661,600 | 14,488,994 | - | 922,456 | 55,034,995 |
| Amounts payable under repurchase agreements | 12,013,151 | - | - | - | - | 12,013,151 |
| Current accounts and deposits from customers | 53,614,278 | 39,886,810 | 3,751,005 | - | 78,408,654 | 175,660,747 |
| | **85,589,374** | **59,548,410** | **18,239,999** | **-** | **79,331,110** | **242,708,893** |
| **Interest rate gap** | **90,310,949** | **(44,249,320)** | **4,922,274** | **982,082** | **(5,667,421)** | **46,298,564** |
| | | | | | | |
| **31 December 2013** | | | | | | |
| **ASSETS** | | | | | | |
| Cash and cash equivalents | 6,506,894 | - | - | - | 46,838,893 | 53,345,787 |
| Financial instruments at fair value through profit or loss | 267,035 | 245,989 | 69,547 | 89,071 | 149,982 | 821,624 |
| Available-for-sale financial assets | 6,916,364 | 10,138,194 | 14,788,058 | 655,387 | 32,101 | 32,530,104 |
| Loans and advances to banks | 1,960,267 | - | - | - | - | 1,960,267 |
| Loans to customers | 139,561,537 | 4,996,472 | 6,812,562 | 162,178 | - | 151,532,749 |
| | **155,212,097** | **15,380,655** | **21,670,167** | **906,636** | **47,020,976** | **240,190,531** |
| **LIABILITIES** | | | | | | |
| Deposits and balances from banks | 16,922,700 | 11,686,783 | 9,340,549 | 154,589 | 90,443 | 38,195,064 |
| Current accounts and deposits from customers | 48,128,091 | 39,227,146 | 243,705 | 29 | 73,398,208 | 160,997,179 |
| | **65,050,791** | **50,913,929** | **9,584,254** | **154,618** | **73,488,651** | **199,192,243** |
| **Interest rate gap** | **90,161,306** | **(35,533,274)** | **12,085,913** | **752,018** | **(26,467,675)** | **40,998,288** |

### *Average interest rates*

The table below displays average effective interest rates for interest bearing assets and liabilities as at 31 December 2014 and 2013. These interest rates are an approximation of the yields to maturity of these assets and liabilities except for the loans to customers of AMD 151,733,128 thousand (2013: AMD 128,156,367 thousand) the interest rates on which are floating on a call basis (the rate is linked to the repo rate announced by the Central Bank of Armenia for AMD loans, and US Federal Reserve rate for USD loans), loans to the employees of AMD 2,088,678 thousand (2013: AMD 2,354,873 thousand) the interest rates on which are reviewed on an annual basis (the next repricing date is 31 March 2015), curent accounts and deposits from customers of AMD 18,647,926 thousand (2013: AMD 13,973,363 thousand) the interest rates on which are floating on a call basis (the rate is linked to the repo rate announced by the Central Bank of Armenia for AMD balances, and US Federal Reserve rate for USD balances) and deposits and balances from banks of AMD 18,597,633 thousand (2013: AMD 12,454,079 thousand) interest rates on which can be reviewed on a call basis, half-yearly or on a triennial basis.

| | 2014 Average effective interest rate, % | | | 2013 Average effective interest rate, % | | |
|---|---|---|---|---|---|---|
| | **AMD** | **USD** | **Other currencies** | **AMD** | **USD** | **Other currencies** |
| **Interest bearing assets** | | | | | | |
| Cash and cash equivalents | - | - | 1.1% | 7.4% | - | 3.2% |
| Financial instruments at fair value through profit or loss | 11.9% | - | - | 9.5% | - | - |
| Available-for-sale financial assets | 10.6% | - | - | 11.2% | - | - |
| Loans and advances to banks | - | 6% | - | 8.4% | - | - |
| Loans to customers | 13.0% | 9.3% | 7.8% | 13.0% | 9.8% | 8.5% |
| | | | | | | |
| **Interest bearing liabilities** | | | | | | |
| Deposits and balances from banks | 7.6% | 2.4% | - | 7.6% | 2.8% | - |
| Amounts payable under repurchase agreements | 20% | - | - | - | - | - |
| Current accounts and deposits from customers | | | | | | |
| - Current accounts and demand deposits | 2.0% | 0.9% | 0.3% | 2.5% | 1.6% | 1.3% |
| - Term deposits | 8.9% | 3.9% | 0.6% | 8.7% | 3.9% | 0.6% |

### *Interest rate sensitivity analysis*

The management of interest rate risk based on interest rate gap analysis is suplemented by monitoring the sensitivity of financial assets and liabilities. An analysis of sensitivity of profit or loss and equity (net of taxes) to changes in interest rates (repricing risk) based on a simplified scenario of a 100 basis point (bp) symmetrical fall or rise in all yield curves and positions of interest-bearing assets and liabilities existing as at 31 December 2014 and 2013 is as follows:

| | 2014 | | 2013 | |
|---|---|---|---|---|
| | **Profit or loss AMD'000** | **Equity AMD'000** | **Profit or loss AMD'000** | **Equity AMD'000** |
| 100 bp parallel rise | 710,198 | 710,198 | 743,394 | 743,394 |
| 100 bp parallel fall | (664,876) | (664,876) | (767,230) | (767,230) |

An analysis of sensitivity of profit or loss and equity as a result of changes in the fair value of financial instruments at fair value though profit or loss and financial assets available-for-sale due to changes in the interest rates based on positions existing as at 31 December 2014 and 2013 and a simplified scenario of a 100 bp symmetrical fall or rise in all yield curves is as follows:

| | 2014 | | 2013 | |
|---|---|---|---|---|
| | **Profit or loss AMD'000** | **Equity AMD'000** | **Profit or loss AMD'000** | **Equity AMD'000** |
| 100 bp parallel rise | (14,357) | (333,406) | (58,534) | (347,581) |
| 100 bp parallel fall | 15,481 | 344,698 | 61,666 | 361,051 |

## *(ii) Currency risk*

The Bank has assets and liabilities denominated in several foreign currencies.

Currency risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in foreign currency exchange rates. Although the Bank hedges its exposure to currency risk, such activities do not qualify as hedging relationships in accordance with IFRS.

The following table shows the foreign currency exposure structure of financial assets and liabilities as at 31 December 2014:

| | AMD | USD | EUR | Other currencies | Total |
|---|---|---|---|---|---|
| | AMD'000 | AMD'000 | AMD'000 | AMD'000 | AMD'000 |
| **ASSETS** | | | | | |
| Cash and cash equivalents | 41,466,816 | 26,727,747 | 2,527,463 | 2,904,689 | 73,626,715 |
| Financial instruments at fair value through profit or loss | 1,563,863 | - | - | - | 1,563,863 |
| Available-for-sale financial assets | 33,073,211 | - | 845 | - | 33,074,056 |
| Loans and advances to banks | 29 | 4,730,854 | 8,662 | 16,820 | 4,756,365 |
| Loans to customers | 33,473,142 | 127,973,012 | 14,540,304 | - | 175,986,458 |
| Other financial assets | 286,363 | 5,505,615 | 7,701,272 | - | 13,493,250 |
| **Total assets** | **109,863,424** | **164,937,228** | **24,778,546** | **2,921,509** | **302,500,707** |
| | | | | | |
| **LIABILITIES** | | | | | |
| Deposits and balances from banks | 4,153,740 | 50,862,300 | - | 18,955 | 55,034,995 |
| Amounts payable under repurchase agreements | 12,013,151 | - | - | - | 12,013,151 |
| Current accounts and deposits from customers | 40,805,596 | 115,018,902 | 17,271,046 | 2,565,203 | 175,660,747 |
| Other financial liabilities | 1,448,198 | 5,495,536 | 7,762,273 | 226,130 | 14,932,137 |
| **Total financial liabilities** | **58,420,685** | **171,376,738** | **25,033,319** | **2,810,288** | **257,641,030** |
| **Net position as at 31 December 2014** | **51,442,739** | **(6,439,510)** | **(254,773)** | **111,221** | **44,859,677** |
| **The effect of derivatives held for risk management and regular way currency contracts** | **(5,588,845)** | **5,588,845** | **-** | **-** | **-** |

The following table shows the foreign currency exposure structure of financial assets and liabilities as at 31 December 2013:

| | AMD<br>AMD'000 | USD<br>AMD'000 | EUR<br>AMD'000 | Other currencies<br>AMD'000 | Total<br>AMD'000 |
|---|---|---|---|---|---|
| **ASSETS** | | | | | |
| Cash and cash equivalents | 28,236,400 | 16,152,908 | 5,665,768 | 3,290,711 | 53,345,787 |
| Financial instruments at fair value through profit or loss | 821,624 | - | - | - | 821,624 |
| Available-for-sale financial assets | 32,529,286 | - | 818 | - | 32,530,104 |
| Loans and advances to banks | 1,952,492 | 923 | - | 6,852 | 1,960,267 |
| Loans to customers | 27,246,881 | 113,853,967 | 10,431,901 | - | 151,532,749 |
| Other financial assets | 194,766 | 122,604 | 4,566,596 | - | 4,883,966 |
| **Total assets** | **90,981,449** | **130,130,402** | **20,665,083** | **3,297,563** | **245,074,497** |
| **LIABILITIES** | | | | | |
| Deposits and balances from banks | 3,431,480 | 34,675,246 | 45 | 88,293 | 38,195,064 |
| Current accounts and deposits from customers | 43,770,881 | 98,055,746 | 16,054,054 | 3,116,498 | 160,997,179 |
| Other financial liabilities | 1,793,838 | 134,548 | 4,615,082 | 24,142 | 6,567,610 |
| **Total financial liabilities** | **48,996,199** | **132,865,540** | **20,669,181** | **3,228,933** | **205,759,853** |
| **Net position as at 31 December 2013** | **41,985,250** | **(2,735,138)** | **(4,098)** | **68,630** | **39,314,644** |
| **The effect of derivatives held for risk management and regular way currency contracts** | **(3,439,785)** | **3,439,785** | **-** | **-** | **-** |

A strengthening of the AMD, as indicated below, against the following currencies at 31 December 2014 and 2013 would have increased (decreased) equity and profit or loss by the amounts shown below. This analysis is based on foreign currency exchange rate variances that the Bank considered to be reasonably possible at the end of the reporting period. The analysis assumes that all other variables, in particular interest rates, remain constant.

| | 2014 | | 2013 | |
|---|---|---|---|---|
| | Profit or loss<br>AMD'000 | Equity<br>AMD'000 | Profit or loss<br>AMD'000 | Equity<br>AMD'000 |
| 10% depreciation of USD against AMD | 85,066 | 85,066 | (70,465) | (70,465) |
| 10% depreciation of EUR against AMD | 25,477 | 25,477 | 410 | 410 |

A weakening of the AMD against the above currencies at 31 December 2014 and 2013 would have had the equal but opposite effect on the above currencies to the amounts shown above, on the basis that all other variables remain constant.

## (c) Credit risk

Credit risk is the risk of financial loss to the Bank if a customer or counterparty to a financial instrument fails to meet its contractual obligations. The Bank has policies and procedures for the management of credit exposures (both for recognised financial assets and unrecognised contractual commitments). The credit policy is reviewed and approved by the Management Board.

The credit policy is in line with HSBC Group standards.

The credit policy establishes:

- procedures for review and approval of loan credit applications
- methodology for the credit assessment of borrowers (corporate and retail)
- methodology for the credit assessment of counterparties, issuers and insurance companies
- methodology for the evaluation of collateral
- credit documentation requirements
- procedures for the ongoing monitoring of loans and other credit exposures

Corporate loan credit applications are originated by the relevant client managers via the Credit Approval and Relationship Management (CARM) system and are then passed on for approval to the Head of Commercial Banking, the Chief Risk Officer or the Chief Executive Officer within the established credit approval limits. Credit applications outside the established limits are referred to HSBC Bank PLC (HBEU) Wholesale Risk for approval. Analysis reports are based on a structured analysis focusing on the customer's business and financial performance. All legal documents regarding credit facilities are prepared and amended based on the approved CARM application.

The Bank continuously monitors the performance of individual credit exposures and regularly reassesses the creditworthiness of its customers. The review is based on the customer's most recent financial statements and other information submitted by the borrower, or otherwise obtained by the Bank.

Retail loan credit applications are reviewed by the Retail Credit department through verification of application data with criteria set in the Retail Banking Wealth Management (RBWM) credit policy approved by the Management Board.

The Bank monitors concentrations of credit risk by industry/sector and by geographic location. The Bank determines asset caps for each loan type, which are monitored on a regular basis.

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

The maximum exposure to credit risk from financial assets at the reporting date is as follows:

| | 2014<br>AMD'000 | 2013<br>AMD'000 |
|---|---|---|
| **ASSETS** | | |
| Cash and cash equivalents | 66,683,003 | 47,625,584 |
| Financial instruments at fair value through profit or loss | 1,563,863 | 821,624 |
| Available-for-sale debt assets | 33,041,928 | 32,498,003 |
| Loans and advances to banks | 4,756,365 | 1,960,267 |
| Loans to customers | 175,986,458 | 151,532,749 |
| Other financial assets | 13,493,250 | 4,883,966 |
| **Total maximum exposure** | **295,524,867** | **239,322,193** |

The Bank holds collateral against loans and advances to customers in the form of mortgage of property, other registered pledge over assets, and guarantees. The current market value of collateral is regularly assessed by independent appraisal companies approved by the Bank in case of properties and by invoice values for goods in turnover and similar items, and in the event of negative movements in market prices the borrower might be requested to put up additional collateral.

Collateral generally is not held against claims under derivative financial instruments, investments in securities, and loans and advances to banks, except when securities are held as part of reverse repurchase and securities borrowing activities.

For the analysis of collateral held against loans to customers and of concentration of credit risk in respect of loans to customers refer to note 17.

The maximum exposure to credit risk from unrecognised contractual commitments at the reporting date is presented in note 27.

**Offsetting financial assets and financial liabilities**

The disclosures set out in the tables below include financial assets and financial liabilities that:

- are offset in the Bank's 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.

The similar agreements include derivative clearing agreements, global master repurchase agreements, and global master securities lending agreements. Similar financial instruments include derivatives, sales and repurchase agreements, reverse sale and repurchase agreements and securities borrowing and lending agreements. Financial instruments such as loans and deposits are not disclosed in the table below unless they are offset in the statement of financial position.

The Bank receives and accepts collateral in the form of marketable securities in respect of sale and repurchase, and reverse sale and repurchase agreements.

Such collateral is subject to standard industry terms. This means that securities received/given as collateral can be pledged or sold during the term of the transaction but must be returned on maturity of the transaction.

The above arrangements do not meet the criteria for offsetting in the statement of financial position. This is because they create a right of set-off of recognized amounts that is enforceable only following an event of default, insolvency or bankruptcy of the Bank or the counterparties.

The table below shows financial assets and financial liabilities subject to offsetting, enforceable master netting arrangements and similar arrangements as at 31 December 2014:

| **2014**<br>**AMD'000**<br>**Types of financial assets/liabilities** | **Gross amounts of recognised financial asset/liability** | **Gross amount of recognised financial liability/asset offset** | **Net amount of financial assets/ liabilities** | **Related amounts not offset Financial Instruments (non-cash collateral)** | **Net amount** |
|---|---|---|---|---|---|
| Reverse sale and repurchase agreements (included in loans to customers) | 2,085,646 | - | 2,085,646 | (2,085,646) | - |
| **Total financial assets** | **2,085,646** | **-** | **2,085,646** | **(2,085,646)** | **-** |
| Sale and repurchase agreements | (12,013,151) | - | (12,013,151) | 12,013,151 | - |
| **Total financial liabilities** | **(12,013,151)** | **-** | **(12,013,151)** | **12,013,151** | **-** |

The table below shows financial assets and financial liabilities subject to offsetting, enforceable master netting arrangements and similar arrangements as at 31 December 2013:

| **2013**<br>**AMD'000**<br>**Types of financial assets/liabilities** | **Gross amounts of recognised financial asset/liability** | **Gross amount of recognised financial liability/asset offset** | **Net amount of financial assets/ liabilities** | **Related amounts not offset Financial Instruments (non-cash collateral)** | **Net amount** |
|---|---|---|---|---|---|
| Reverse sale and repurchase agreements (included in loans to customers) | 2,253,662 | - | 2,253,662 | (2,253,662) | - |
| **Total financial assets** | **2,253,662** | **-** | **2,253,662** | **(2,253,662)** | **-** |

## (d) Liquidity risk

Liquidity risk is the risk that the Bank will encounter difficulty in meeting obligations associated with its financial liabilities that are settled by delivering cash or another financial asset. Liquidity risk exists when the maturities of assets and liabilities do not match. The matching and or controlled mismatching of the maturities and interest rates of assets and liabilities is fundamental to liquidity management. It is unusual for financial institutions ever to be completely matched since business transacted is often of an uncertain term and of different types. An unmatched position potentially enhances profitability, but can also increase the risk of losses.

The Bank maintains liquidity management with the objective of ensuring that funds will be available at all times to honor all cash flow obligations as they become due. The Bank's liquidity policy is developed in accordance with HSBC Group policies and local regulations. The liquidity policy is reviewed and approved by the ALCO committee.

The Bank seeks to actively support a diversified and stable funding base comprising core corporate and retail customer deposits, debt securities in issue, long-term and short-term loans from other banks, accompanied by diversified portfolios of highly liquid assets, in order to be able to respond quickly and smoothly to unforeseen liquidity requirements.

The liquidity management policy requires:

- projecting cash flows by major currencies and considering the level of liquid assets necessary in relation thereto
- maintaining a diverse range of funding sources
- managing the concentration and profile of debts
- maintaining debt financing plans
- maintaining a portfolio of highly marketable assets that can easily be liquidated as protection against any interruption to cash flow
- maintaining liquidity and funding contingency plans
- monitoring liquidity ratios against regulatory requirements.

The Treasury Department receives information from business units regarding the liquidity profile of their financial assets and liabilities and details of other projected cash flows arising from projected future business. The Treasury Department then provides for an adequate portfolio of short-term liquid assets to be maintained, largely made up of short-term liquid securities, loans and advances to banks and other inter-bank facilities, to ensure that sufficient liquidity is maintained within the Bank as a whole.

The daily liquidity position is monitored and regular liquidity stress testing under a variety of scenarios covering both normal and more severe market conditions is performed and reveiwed by ALCO. Decisions on liquidity management are made by the ALCO and implemented by the Treasury department.

The Bank also calculates mandatory liquidity ratios on a daily basis in accordance with the requirements of the CBA.

The following tables show the undiscounted cash flows on financial liabilities and credit-related commitments on the basis of their earliest possible contractual maturity. The total gross inflow and outflow disclosed in the tables is the contractual, undiscounted cash flow on the financial liability or commitment. For issued financial guarantee contracts, the maximum amount of the guarantee is allocated to the earliest period in which the guarantee can be called. The maturity analysis for financial liabilities as at 31 December 2014 is as follows:

| AMD'000 | Demand and less than 1 month | From 1 to 3 months | From 3 to 12 months | From 1 to 5 years | More than 5 years | Total gross amount outflow | Carrying amount |
|---|---|---|---|---|---|---|---|
| **Non-derivative liabilities** | | | | | | | |
| Deposits and balances from banks | 1,585,535 | 4,424,047 | 18,980,942 | 32,067,490 | 24,533 | 57,082,547 | 55,034,995 |
| Amounts payable under repurchase agreements | 12,092,055 | - | - | - | - | 12,092,055 | 12,013,151 |
| Current accounts and deposits from customers | 101,591,544 | 13,642,513 | 48,203,836 | 14,420,956 | 1,183,632 | 179,042,481 | 175,660,747 |
| Other financial liabilities | 2,389,463 | 750,133 | 3,911,750 | 7,880,791 | - | 14,932,137 | 14,932,137 |
| **Total liabilities** | **117,658,597** | **18,816,693** | **71,096,528** | **54,369,237** | **1,208,165** | **263,149,220** | **257,641,030** |
| **Credit related commitments and guarantees** | **30,737,427** | **-** | **-** | **-** | **-** | **30,737,427** | **-** |

The maturity analysis for financial liabilities as at 31 December 2013 is as follows:

| AMD'000 | Demand and less than 1 month | From 1 to 3 months | From 3 to 12 months | From 1 to 5 years | More than 5 years | Total gross amount outflow | Carrying amount |
|---|---|---|---|---|---|---|---|
| **Non-derivative liabilities** | | | | | | | |
| Deposits and balances from banks | 602,104 | 7,579,051 | 8,171,626 | 23,605,789 | 335,517 | 40,294,087 | 38,195,064 |
| Current accounts and deposits from customers | 97,416,361 | 11,960,493 | 43,357,725 | 10,350,518 | 766,745 | 163,851,842 | 160,997,179 |
| Other financial liabilities | 2,226,684 | 203,711 | 1,364,942 | 2,772,273 | - | 6,567,610 | 6,567,610 |
| **Total liabilities** | **100,245,149** | **19,743,255** | **52,894,293** | **36,728,580** | **1,102,262** | **210,713,539** | **205,759,853** |
| **Credit related commitments and guarantees** | **33,312,975** | **-** | **-** | **-** | **-** | **33,312,975** | **-** |

In accordance with Armenian legislation, individuals can withdraw their term deposits at any time, forfeiting, in most cases, the accrued interest. These deposits are classified in accordance with their stated maturity dates. The principal amount of such deposits, by each time band, is as follows:

- less than 1 month: AMD 6,480,539 thousand (2013: AMD 6,442,106 thousand)
- from 1 to 3 months: AMD 11,153,153 thousand (2013: AMD 10,011,334 thousand)
- from 3 to 12 months: AMD 35,170,673 thousand (2013: AMD 29,672,117 thousand)
- from 1 to 5 years: AMD 11,780,413 thousand (2013: AMD 9,093,112 thousand)
- more than 5 years: AMD 740,298 thousand (2013: 434,255 thousand)

The table below shows an analysis, by expected maturities, of the amounts recognised in the statement of financial position as at 31 December 2014:

| AMD'000 | Demand and less than 1 month | From 1 to 3 months | From 3 to 12 months | From 1 to 5 years | More than 5 years | No maturity | Overdue | Total |
|---|---|---|---|---|---|---|---|---|
| Cash and cash equivalents | 73,626,715 | - | - | - | - | - | - | 73,626,715 |
| Financial instruments at fair value through profit or loss | 233,095 | 94,076 | 789,497 | 152,932 | 294,263 | - | - | 1,563,863 |
| Available-for-sale financial assets | 2,531,194 | 1,700,218 | 11,535,989 | 16,623,205 | 651,322 | 32,128 | | 33,074,056 |
| Loans and advances to banks | 4,756,365 | - | - | - | - | - | - | 4,756,365 |
| Loans to customers | 6,865,661 | 15,099,106 | 49,430,699 | 85,761,473 | 9,521,345 | - | 9,308,174 | 175,986,458 |
| Property, equipment and intangible assets | - | - | - | - | - | 3,865,547 | - | 3,865,547 |
| Other assets | 963,851 | 780,786 | 3,980,272 | 7,961,804 | - | 49,395 | - | 13,736,108 |
| **Total assets** | **88,976,881** | **17,674,186** | **65,736,457** | **110,499,414** | **10,466,930** | **3,947,070** | **9,308,174** | **306,609,112** |
| | | | | | | | | |
| Deposits and balances from banks | 1,584,766 | 4,408,562 | 18,588,034 | 30,436,678 | 16,955 | - | - | 55,034,995 |
| Amounts payable under repurchase agreements | 12,013,151 | - | - | - | - | - | - | 12,013,151 |
| Current accounts and deposits from customers | 101,557,543 | 13,572,543 | 46,779,013 | 12,999,437 | 752,211 | - | - | 175,660,747 |
| Current tax liability | - | - | 482,592 | - | - | - | - | 482,592 |
| Deferred tax liability | - | - | - | - | - | 822,448 | - | 822,448 |
| Other liabilities | 2,476,761 | 867,347 | 4,175,442 | 8,110,208 | 5,019 | - | - | 15,634,777 |
| **Total liabilities** | **117,632,221** | **18,848,452** | **70,025,081** | **51,546,323** | **774,185** | **822,448** | **-** | **259,648,710** |
| **Net position as at 31 December 2014** | **(28,655,340)** | **(1,174,266)** | **(4,288,624)** | **58,953,091** | **9,692,745** | **3,124,622** | **9,308,174** | **46,960,402** |

The table below shows an analysis, by expected maturities, of the amounts recognised in the statement of financial position as at 31 December 2013:

| AMD'000 | Demand and less than 1 month | From 1 to 3 months | From 3 to 12 months | From 1 to 5 years | More than 5 years | No maturity | Overdue | Total |
|---|---|---|---|---|---|---|---|---|
| Cash and cash equivalents | 53,345,787 | - | - | - | - | - | - | 53,345,787 |
| Financial instruments at fair value through profit or loss | 211,859 | 205,158 | 245,989 | 69,547 | 89,071 | - | - | 821,624 |
| Available-for-sale financial assets | 2,368,204 | 4,548,160 | 10,138,194 | 14,788,058 | 655,387 | 32,101 | | 32,530,104 |
| Loans and advances to banks | 1,960,267 | - | - | - | - | - | - | 1,960,267 |
| Loans to customers | 7,164,452 | 13,821,453 | 47,373,493 | 69,276,974 | 7,054,308 | - | 6,842,069 | 151,532,749 |
| Property, equipment and intangible assets | - | - | - | - | - | 4,048,139 | - | 4,048,139 |
| Other assets | 602,197 | 228,859 | 1,423,254 | 2,873,310 | - | 57,299 | - | 5,184,919 |
| **Total assets** | **65,652,766** | **18,803,630** | **59,180,930** | **87,007,889** | **7,798,766** | **4,137,539** | **6,842,069** | **249,423,589** |
| | | | | | | | | |
| Deposits and balances from banks | 601,942 | 7,552,909 | 8,061,190 | 21,805,018 | 174,005 | - | - | 38,195,064 |
| Current accounts and deposits from customers | 97,385,191 | 11,883,866 | 42,055,690 | 9,224,498 | 447,934 | - | - | 160,997,179 |
| Current tax liability | - | - | 734,842 | - | - | - | - | 734,842 |
| Deferred tax liability | - | - | - | - | - | 1,018,426 | - | 1,018,426 |
| Other liabilities | 2,297,933 | 328,619 | 1,584,902 | 2,980,317 | 5,222 | - | - | 7,196,993 |
| **Total liabilities** | **100,285,066** | **19,765,394** | **52,436,624** | **34,009,833** | **627,161** | **1,018,426** | **-** | **208,142,504** |
| **Net position as at 31 December 2013** | **(34,632,300)** | **(961,764)** | **6,744,306** | **52,998,056** | **7,171,605** | **3,119,113** | **6,842,069** | **41,281,085** |

The key measures used by the Bank for managing liquidity risk are the ratios of liquid assets to total assets and liquid assets to on demand liabilities. For this purpose liquid assets include cash and cash equivalents, Government treasury bills and amounts receivable under reverse repurchase agreements collateralized by Government treasury bills, which are not pledged or the use of which is not restricted in any way. The ratios at the reporting date are as follows:

| | 2014<br>AMD'000 | 2013<br>AMD'000 |
|---|---|---|
| At 31 December | | |
| Ratio of liquid assets to total assets | 35% | 35% |
| Ratio of liquid assets to on demand liabilities | 108% | 105% |

Similar, but not identical, calculations are used to measure compliance with the liquidity limits established by the CBA.

## 26 Capital management

The CBA sets and monitors capital requirements for the Bank.

The Bank defines as capital those items defined by statutory regulation as capital for credit institutions. Under the current capital requirements set by the CBA, banks have to maintain a ratio of capital to risk weighted assets (statutory capital ratio) above the prescribed minimum level. As at 31 December 2014, this minimum level was 12%. The Bank was in compliance with the statutory capital ratio as at 31 December 2014 and 2013.

Regular stress testing covering both normal and more severe market conditions is performed to assess the impact on statutory capital ratio. The result of stress tests are reviewed by the ALCO on a quarterly basis and by the Board on an annual basis.

The following table shows the composition of the capital position calculated in accordance with the requirements of the CBA, as at 31 December:

| | 2014<br>AMD'000<br>Unaudited | 2013<br>AMD'000<br>Unaudited |
|---|---|---|
| **Tier 1 capital** | | |
| Share capital | 18,434,350 | 18,434,350 |
| Retained earnings | 26,276,581 | 20,085,831 |
| General Reserve (CBA) | 1,958,838 | 1,585,119 |
| Adjustment to CBA accounting principles | (4,737,567) | (5,369,580) |
| Other deductions | (738,119) | (1,153,403) |
| **Total tier 1 capital** | **41,194,083** | **33,582,317** |

| | 2014<br>AMD'000<br>Unaudited | 2013<br>AMD'000<br>Unaudited |
|---|---|---|
| **Tier 2 capital** | | |
| Revaluation reserve for available-for-sale financial assets, gross of tax | 247,709 | 1,359,865 |
| Share -based payment reserve | 92,466 | 87,893 |
| Subordinated debt as per the CBA regulations | - | 576,400 |
| **Total tier 2 capital** | **340,175** | **2,024,158** |
| **Total capital** | **41,534,258** | **35,606,475** |
| **Risk weighted assets, combining credit, market and operational risks** | **292,833,845** | **244,626,820** |
| **Total capital ratio** | **14.18%** | **14.6%** |

The risk-weighted assets are measured by means of a hierarchy of risk weights classified according to the nature and reflecting an estimate of credit, market and other risks associated with each asset and counterparty, taking into account any eligible collateral or guarantees. A similar treatment is adopted for unrecognised contractual commitments, with some adjustments, to reflect the more contingent nature of the potential losses.

## 27 Commitments

The Bank has outstanding commitments to extend loans. These commitments take the form of approved loans and credit card limits and overdraft facilities.

The Bank provides financial guarantees and letters of credit to guarantee the performance of customers to third parties. These agreements have fixed limits and generally extend for a period of up to five years.

The Bank applies the same credit risk management policies and procedures when granting credit commitments, financial guarantees and letters of credit as it does for granting loans to customers.

The contractual amounts of commitments are set out in the following table by category. The amounts reflected in the table for commitments assume that amounts are fully advanced. The amounts reflected in the table for guarantees and letters of credit represent the maximum accounting loss that would be recognised at the reporting date if counterparties failed completely to perform as contracted.

| | 2014<br>AMD'000 | 2013<br>AMD'000 |
|---|---|---|
| **Contracted amount** | | |
| Loan and credit line commitments | 18,675,394 | 20,321,492 |
| Guarantees and letters of credit | 5,170,348 | 6,172,557 |
| Credit card commitments | 4,966,054 | 5,247,129 |
| Undrawn overdraft facilities | 1,925,631 | 1,571,797 |
| | **30,737,427** | **33,312,975** |

The total outstanding contractual commitments above do not necessarily represent future cash requirements, as these commitments may expire or terminate without being funded. However, the majority of loan and credit line commitments do not represent an unconditional commitment by the Bank.

Of these commitments, AMD 13,682,568 thousand are to 10 customers as at 31 December 2014 (2013: AMD 13,174,607 thousand are to 10 customers).

## 28 Operating leases

Non-cancelable operating lease rentals as at 31 December are payable as follows:

| | 2014<br>AMD'000 | 2013<br>AMD'000 |
|---|---|---|
| Less than 1 year | 544,136 | 527,409 |
| Between 1 and 5 years | 1,393,014 | 1,586,336 |
| More than 5 years | 494,902 | 708,181 |
| | **2,432,052** | **2,821,926** |

The Bank leases a number of premises and equipment under operating leases. The leases typically run for an initial period of five to ten years, with an option to renew the lease after that date. Lease payments are usually increased annually to reflect market rentals. None of the leases includes contingent rentals.

## 29 Contingencies

### (a) Litigation

Management is unaware of any significant actual, pending or threatened claims against the Bank.

### (b) Taxation contingencies

The taxation system in the Republic of Armenia continues to evolve and is characterized by frequent changes in legislation, official pronouncements and court decisions, which are sometimes contradictory and subject to varying interpretation by different tax authorities. Taxes are subject to review and investigation by a number of authorities, which have the authority to impose severe fines, penalties and interest charges. A tax year remains open for review by the tax authorities during the three subsequent calendar years.

These circumstances may create tax risks in the Republic of Armenia that are substantially 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 the financial position, if the authorities were successful in enforcing their interpretations, could be significant.

# 30 Custody activities

The Bank provides custody services to its customers, whereby it holds securities on behalf of customers and receives fee income for providing these services. These securities are not assets of the Bank and are not recognised in the statement of financial position.

# 31 Related party transactions

## (a) Control relationships

The Bank's Parent Company is HSBC Europe B.V. The party with ultimate control over the Bank is HSBC Holdings PLC.

## (b) Transactions with the members of the Board and the Management Board

Total remuneration included in personnel expenses for the year ended 31 December is as follows:

| | 2014 AMD'000 | 2013 AMD'000 |
|---|---|---|
| Short term employee benefits | 650,532 | 584,883 |
| Share based payments | 8,319 | 5,949 |

The outstanding balances and average interest rates as at 31 December for transactions with the members of the Board and the Management Board are as follows:

| | 2014 AMD'000 | Average interest rate, % | 2013 AMD'000 | Average interest rate, % |
|---|---|---|---|---|
| **Statement of financial position** | | | | |
| **ASSETS** | | | | |
| Loans to customers | 476,569 | 7.5% | 393,464 | 6.5% |
| **LIABILITIES** | | | | |
| Current accounts and deposits from customers | 227,723 | 2.5% | 339,906 | 2.8% |

Amounts included in profit or loss in relation to transactions with the members of the Board and the Management Board for the year ended 31 December are as follows:

| | 2014 AMD'000 | 2013 AMD'000 |
|---|---|---|
| **Profit or loss** | | |
| Interest income | 24,945 | 24,165 |
| Interest expense | (8,281) | (9,858) |

## (c) Transactions with other related parties

Other related parties include entities under common control of the Bank's ultimate controlling party and other related parties of key management. The outstanding balances and the related average interest rates and other transactions as of and for the years ended 31 December 2014 and 2013 with other related parties are as follows:

| | 2014 | | 2013 | |
|---|---|---|---|---|
| | AMD'000 | Average interest rate | AMD'000 | Average interest rate |
| **Statement of financial position** | | | | |
| **ASSETS** | | | | |
| Cash and cash equivalents | 26,349,544 | 0.03% | 20,635,306 | 0.2% |
| Loans to customers | 6,512 | 11.2% | 2,457 | 22.8% |
| Foreign exchange contracts | 1,102,798 | - | 149,982 | - |
| **LIABILITIES** | | | | |
| Deposits and balances from banks | 36,999,630 | 2.0% | 19,017,724 | 2.0% |
| Current accounts and deposits from customers | 8,331,099 | 4.4% | 6,812,247 | 4.7% |
| Other liabilities | 13,583,722 | - | 3,759,037 | - |
| **Items not recognised in the statement of financial position** | | | | |
| Foreign exchange contracts – notional amounts | 7,687,396 | | 7,376,491 | |
| Guarantees | 992,080 | | 961,276 | |
| **Profit (loss)** | | | | |
| Interest income | 39,740 | | 36,193 | |
| Interest expense | (643,724) | | (482,827) | |
| Fee and commission expense | (114,545) | | (31,535) | |
| Net gain on financial instruments at fair value through profit or loss | 1,260,390 | | 271,293 | |
| Other income | 65,830 | | 111,710 | |
| HSBC Group IT support costs and other charges | (1,447,779) | | (1,575,998) | |

Loans to customers and current accounts and deposits from customers represent balances with related parties of members of Board and Management Board.

# 32 Financial assets and liabilities: fair values and accounting classifications

## (a) Accounting classifications

The table below sets out the carrying amounts of financial assets and financial liabilities as at 31 December 2014:

| AMD'000 | Trading | Loans and receivables | Available-for-sale | Other amortised cost | Total carrying amount |
|---|---|---|---|---|---|
| Cash and cash equivalents | - | 73,626,715 | - | - | 73,626,715 |
| Financial instruments at fair value through profit or loss | 1,563,863 | - | - | - | 1,563,863 |
| Available-for-sale financial assets | - | - | 33,074,056 | - | 33,074,056 |
| Loans and advances to banks | - | 4,756,365 | - | - | 4,756,365 |
| Loans to customers | - | 175,986,458 | - | - | 175,986,458 |
| Other financial assets | - | 13,493,250 | - | - | 13,493,250 |
| | **1,563,863** | **267,862,788** | **33,074,056** | **-** | **302,500,707** |
| | | | | | |
| Deposits and balances from banks | - | - | - | 55,034,995 | 55,034,995 |
| Amounts payable under repurchase agreements | | | | 12,013,151 | 12,013,151 |
| Current accounts and deposits from customers | - | - | - | 175,660,747 | 175,660,747 |
| Other financial liabilities | 128,805 | - | - | 14,803,332 | 14,932,137 |
| | **128,805** | **-** | **-** | **257,512,225** | **257,641,030** |

The table below sets out the carrying amounts of financial assets and financial liabilities as at 31 December 2013:

| AMD'000 | Trading | Loans and receivables | Available-for-sale | Other amortised cost | Total carrying amount |
|---|---|---|---|---|---|
| Cash and cash equivalents | - | 53,345,787 | - | - | 53,345,787 |
| Financial instruments at fair value through profit or loss | 821,624 | - | - | - | 821,624 |
| Available-for-sale financial assets | - | - | 32,530,104 | - | 32,530,104 |
| Loans and advances to banks | - | 1,960,267 | - | - | 1,960,267 |
| Loans to customers | - | 151,532,749 | - | - | 151,532,749 |
| Other financial assets | - | 4,883,966 | - | - | 4,883,966 |
| | **821,624** | **211,722,769** | **32,530,104** | **-** | **245,074,497** |
| Deposits and balances from banks | - | - | - | 38,195,064 | 38,195,064 |
| Current accounts and deposits from customers | - | - | - | 160,997,179 | 160,997,179 |
| Other financial liabilities | - | - | - | 6,567,610 | 6,567,610 |
| | **-** | **-** | **-** | **205,759,853** | **205,759,853** |

## (b) Fair values and fair value hierarchy

The Bank measures fair values for financial instruments using the following fair value hierarchy that reflects the significance of the inputs used in making the measurements:

- Level 1: Quoted market price (unadjusted) in an active market for an identical instrument.
- Level 2: Valuation techniques based on observable inputs, either directly (i.e. as prices) or indirectly (i.e. derived from prices). This category includes instruments valued using: quoted market prices in active markets for similar instruments; quoted prices for identical or similar instruments in markets that are considered less than active; or other valuation techniques where all significant inputs are directly or indirectly observable from market data.
- Level 3: Valuation techniques using significant unobservable inputs. This category includes all instruments where the valuation technique includes inputs not based on observable data and the unobservable inputs have a significant effect on the instrument's valuation. This category includes instruments that are valued based on quoted prices for similar instruments where significant unobservable adjustments or assumptions are required to reflect differences between the instruments.

The estimates of fair value are intended to approximate the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. However given the uncertainties and the use of subjective judgment, the fair value should not be interpreted as being realizable in an immediate sale of the assets or transfer of liabilities.

Valuation techniques include net present value and discounted cash flow models, comparison to similar instruments for which market observable prices exist and other valuation models. Assumptions and inputs used in valuation techniques include risk-free and benchmark interest rates, credit spreads and other premia used in estimating discount rates, bond and equity prices, foreign currency exchange rates, equity and equity index prices. The objective of valuation techniques is to arrive at a fair value determination that reflects the price of the financial instrument at the reporting date that would have been determined by market participants acting at arm's length.

The Bank uses widely recognised valuation models for determining the fair value of common and more simple financial instruments like interest rate and currency swaps that use only observable market data and require little management judgment and estimation. Observable prices and model inputs are usually available in the market for listed debt and equity securities, exchange traded derivatives and simple over the counter derivatives like interest rate swaps.

The estimated fair values of all financial instruments except for unquoted equity securities available-for-sale approximate their carrying values. As at 31 December 2014 fair value of unquoted equity securities available-for-sale with a carrying value of AMD 32,128 thousand (2013: AMD 32,101 thousand) cannot be determined.

The following assumptions are used by management to estimate the fair values of financial instruments:

- discount rates of 6% and 8%-13% are used for discounting future cash flows from loans and advances to banks and loans to customers, respectively;
- discount rates of 1.5% - 8.9% are used for discounting future cash flows for liabilities;
- the fair value of variable rate instruments is not materially different from carrying amount.

The table below analyses financial instruments measured at fair value for the years ended 31 December 2014 and 2013, by the level in the fair value hierarchy into which the fair value measurement is categorised:

| | 2014 | 2013 |
|---|---|---|
| **AMD'000** | **Level 2** | **Level 2** |
| Financial instruments at fair value through profit or loss | | |
| - Government treasury bills | 461,065 | 671,642 |
| - Derivative assets | 1,102,798 | 149,982 |
| - Derivative liabilities | (128,805) | - |
| Available-for-sale financial assets | | |
| - Government treasury bills | 30,454,871 | 31,252,983 |
| - Corporate bonds | 2,587,057 | 1,245,020 |

The following table analyses the fair value of financial instruments not measured at fair value, by the level in the fair value hierarchy into which each fair value measurement is categorised as at 31 December 2014:

| **AMD'000** | **Level 2** | **Level 3** | **Total fair values** | **Total carrying amount** |
|---|---|---|---|---|
| **ASSETS** | | | | |
| Cash and cash equivalents | 73,626,715 | - | 73,626,715 | 73,626,715 |
| Loans to banks | 4,756,365 | - | 4,756,365 | 4,756,365 |
| Loans to customers | - | 175,986,458 | 175,986,458 | 175,986,458 |
| Other financial assets | 13,493,250 | - | 13,493,250 | 13,493,250 |
| **LIABILITIES** | | | | |
| Deposits and balances from banks | 55,034,995 | - | 55,034,995 | 55,034,995 |
| Amounts payable under repurchase agreements | 12,013,151 | - | - | 12,013,151 |
| Current accounts and deposits from customers | 175,660,747 | - | 175,660,747 | 175,660,747 |
| Other financial liabilities | 14,932,137 | - | 14,932,137 | 14,932,137 |

The following table analyses the fair value of financial instruments not measured at fair value, by the level in the fair value hierarchy into which each fair value measurement is categorised as at 31 December 2013:

| AMD'000 | Level 2 | Level 3 | Total fair values | Total carrying amount |
|---|---|---|---|---|
| **ASSETS** | | | | |
| Cash and cash equivalents | 53,345,787 | - | 53,345,787 | 53,345,787 |
| Loans to banks | 1,960,267 | - | 1,960,267 | 1,960,267 |
| Loans to customers | - | 151,532,749 | 151,532,749 | 151,532,749 |
| Other financial assets | 4,883,966 | - | 4,883,966 | 4,883,966 |
| **LIABILITIES** | | | | |
| Deposits and balances from banks | 38,195,064 | - | 38,195,064 | 38,195,064 |
| Current accounts and deposits from customers | 160,997,179 | - | 160,997,179 | 160,997,179 |
| Other financial liabilities | 6,567,610 | - | 6,567,610 | 6,567,610 |

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