HSBC Bank Armenia CJSC

Annual Report and Accounts 2018

The HSBC Group

HSBC Bank Armenia is a member of HSBC Group, one of the largest banking and financial services organisations in the world. HSBC Group international network comprises around 3,800 offices over 66 countries and territories.

HSBC Bank Armenia CJSC
Registered in the Republic of Armenia: number 67
Registered Office:
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Republic of Armenia
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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 and, 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.

Paul Edgar
Chief Executive Officer

Astghik Drambyan
Chief Financial Officer / Deputy CEO

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 2018, 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 2018. It is confirmed that the function had appropriate resources for this activity.

Based on the above, in our opinion, the Bank's activity during 2018 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 either completed or are in progress.

Internal Audit Department

Business review and financial analysis

HSBC Bank Armenia CJSC (the "Bank") continues to actively play its part in the Armenian financial sector, improve its risk management and control framework and reinforce its standards of business conduct. The Bank has also retained a strong capital position and market share in target areas.

We provide banking and financial services to our customers and continuously strive to enhance the quality of the products and services that we offer in Armenia. Throughout 2018, with 8 offices in Yerevan and 392 employees, we continued to serve around 30,000 customers through three Global Businesses: Retail Banking and Wealth Management, Commercial Banking and Global Banking and Markets. As a member of HSBC Group we continued to closely cooperate with other banks and financial institutions within the HSBC Group aiming to provide various high quality services to customers.

2018 was historical year for Armenia. The country has undergone political changes with the new Prime Minister taking over the office in May. Early elections of the National Assembly took place in December with the Prime Minister's party winning with enough votes to have the major share of the seats in the Assembly. The main strategic directions of the new government are fighting the shadow economy and poverty, bringing new investments into the country and decreasing the unemployment rate. The new government is now aiming to transform the 'political revolution' to an 'economic revolution' with improvements being made to the rule of law to encourage increased foreign direct investments.

Armenia has continued to demonstrate macroeconomic and financial stability throughout political volatility and ongoing geopolitical tensions related to Russia. The market is still characterised by socio-economic challenges, driven by mixed macro-economic climate. There are signs of improvement in the economic environment and in investment sentiment and GDP growth is robust.

2018 has been a challenging but successful year for the Bank with the Bank returning to profit. We delivered strong financial performance despite the difficulties in the Armenian economy, lower GDP growth and wider financial problems faced by corporate businesses due to the economic factors in the region. Our diversified business model, effective risk management and cost discipline form the foundation for our current and future progress and position HSBC in Armenia well to deal with today's challenging economic and financial conditions.

We have remained one of the country's leading international banks for trade finance and international cash management. Euromoney Cash Management Survey 2018 named the Bank as the Best Domestic Cash Manager in Armenia. The Euromoney Cash Management Awards are voted for by cash managers, treasury professionals and financial officers around the world, allowing them to comment on the standard of the cash management services they receive, as well as rate the financial institution they bank with. This first domestic award represented our customers' trust in the Bank.

There have been a number of successful business outcomes in Commercial Banking and Global Banking and Markets, as well as several very successful campaigns in Retail Banking and Wealth Management. On the corporate side, we have remained focused on internationally minded businesses - helping customers benefit from our network and expertise and connecting customers to opportunities.

We continued investing in innovation and technology to serve our customers better, as well as enhance security around financial transactions and customer data.

At the end of the year the Bank introduced the new enhanced website, which allows the customers to enjoy personalized and dynamic content tailored to their specific banking needs, assist them in seeing the content relevant to their preferences based on their past experience on the website, and provides new look and feel design.

We initiated an upgrade of our Automatic Teller Machines (ATM) and related software, which aims at effectively meeting our customers' evolving needs, aligning customer experience to the best international standards and providing outstanding service in this sphere.

The Bank continued presenting HSBC's global track record on technological developments by participating in the DigiTec Expo, which is the largest technological exhibition in the region. The focus was on the pre-introduction of new contactless ATMs, promotion of contactless cards and biometric solutions (touch and face identification), which clearly demonstrated HSBC's global track record on technological developments.

During the year we remained committed to our strategy of supporting 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 is roughly equal to the corporate loans in our local book. The loan portfolio of HSBC Bank plc, UK and related income are not part of the financial statements of the Bank, however this lending clearly demonstrates HSBC Group's continued support and interest in Armenia's economy.

We are continuing to take concerted action to improve anti-money laundering and sanctions compliance controls. We are safer today and better protected from the threat of financial crime because of the investments we have been making in this programme. We remain absolutely committed to ensuring financial crime risk is clearly understood and addressed throughout our network.

How we do business is as important as what we do. At HSBC, Sustainability means building our business for the long term by balancing social, environmental and economic considerations in the decisions we make. In 2018 the Bank contributed just over USD 121,000 from its both HSBC in Armenia and the HSBC Group budgets in support of local communities through various projects. Our main charity partners of the year were Junior Achievement, Orran Benevolent NGO, British Council, FPWC and Children of Armenia Fund. For HSBC, there are the key elements of sustainable growth which we can influence. We have three areas of focus: Future Skills - providing our customers, our communities and our people with the skills needed to succeed in a global economy; Sustainable Networks and Entrepreneurs - fostering new business development and sustainable international growth; Sustainable Finance - facilitating the transition to a low carbon economy. The Bank continues to focus on its Global Reduce Programme through suitable and responsible operations. We aim to reduce our waste by 75 per cent and recycle 100 per cent of our office and electronic waste. Despite time and work pressures, 194 of the Bank employees have been active volunteers supporting the communities in which we operate. There was a significant increase in HSBC Armenia staff volunteering hours from some 800 hours in 2017 to over 1,500 hours this year.

On behalf of the Management and Board, we thank our 30,000 customers for their trust and commitment. None of this would have been possible without their commercial success, loyalty and support. We also owe a huge thanks to our 392 colleagues, who have delivered all of the above mentioned activities at the same time as working tirelessly to meet the expectations of our customers.

Financial review

The Bank's net profit after tax for the year was AMD555 million compared to a loss in the prior year. Better actual performance compared to last year was contributed by lower impairments and operating expenses, while revenues exhibited 12% reduction on last year.

Impairment charges were AMD1,513 million versus AMD14,186 million in 2017. Personnel and other administrative expenses were AMD8,594 million, a 4% increase from the previous year.

Total assets as of 31 December 2018 were AMD197 billion, a 6% decrease over the previous year. Loans to customers amounted to AMD104 billion, a 9% increase over last year. The gross corporate loan portfolio increased by 3% and amounted to AMD87 billion. The gross retail loan portfolio showed a 10% increase amounting to AMD24 billion. Current accounts and deposits from customers were AMD153 billion, a 4% decrease from the previous year.

The loan portfolio of HSBC Bank plc, UK to Armenian businesses as at 31 December 2018 was AMD72 billion, a 24% decrease over the previous year. Net profit for the year from loans to customers provided by HSBC Bank plc was AMD3,200 million, which is significantly better compared to the previous year. As we noted above, this loan portfolio and related profit are not part of the financial statements of the Bank, however they are part of the management information used by HSBC Group for Armenian subsidiary business.

Total assets including loans to customers provided by HSBC Bank plc to Armenian businesses as at 31 December 2018 amounted to AMD269 billion versus AMD304 billion in 2017. Profit before taxes for the year including net profit from loans to customers provided by HSBC Bank plc amounted to AMD3,878 million versus AMD10,999 million loss before taxes in 2017.

Nicola Polli
Board Member

Ara Alexanian
Board Member

Independent Auditor's Report

To the Board of HSBC Bank Armenia CJSC

Our opinion

In our opinion, the financial statements present fairly, in all material respects, the financial position of HSBC Bank Armenia CJSC (the "Bank") as at 31 December 2018, and its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards ("IFRS").

What we have audited

The Bank's financial statements comprise:

- the statement of financial position as at 31 December 2018;
- the statement of profit or loss and other comprehensive income for the year then ended;
- the statement of changes in equity for the year then ended;
- the statement of cash flows for the year then ended; and
- the notes to the financial statements, which include significant accounting policies and other explanatory information.

Basis for opinion

We conducted our audit in accordance with International Standards on Auditing (ISAs). Our responsibilities under those standards are further described in the *Auditor's Responsibilities for the Audit of the Financial Statements* section of our report.

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

Independence

We are independent of the Bank in accordance with the International Ethics Standards Board for Accountants' Code of Ethics for Professional Accountants (IESBA Code). We have fulfilled our other ethical responsibilities in accordance with the IESBA Code.

Other information

Management is responsible for the other information. The other information obtained at the date of this auditor's report comprises Business Review and Financial Analysis (but does not include the financial statements and our auditor's report thereon).

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

In connection with our audit of the financial statements, our responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the financial statements or our knowledge obtained in the audit, or otherwise appears to be materially misstated. If, based on the work we have performed on the other information obtained prior to the date of this auditor's report, we conclude that there is a material misstatement of this other information, we are required to report that fact. We have nothing to report in this regard.

Independent Auditor's Report (Continued)

Responsibilities of management and those charged with governance for the financial statements

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

In preparing the financial statements, management is responsible for assessing the Bank's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless management either intends to liquidate the Bank or to cease operations, or has no realistic alternative but to do so.

Those charged with governance are responsible for overseeing the Bank's financial reporting process.

Auditor's responsibilities for the audit of the financial statements

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

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

- Identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.

- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Bank's internal control.

- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management.

- Conclude on the appropriateness of management's use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Bank's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the Bank to cease to continue as a going concern.

Independent Auditor's Report (Continued)

- Evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation.

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

Michael Ahern
Managing Partner

Anahit Gyozalyan
Auditor

PricewaterhouseCoopers Armenia LLC

25 April 2019
Yerevan, Republic of Armenia

In thousands of Armenian Drams	Note	31 December 2018	31 December 2017
ASSETS			
Cash and cash equivalents	7	43,085,915	69,465,410
Financial assets at fair value through profit or loss	8	-	1,314,070
Loans and advances to banks	9	17,359,992	10,566,868
Investments in debt securities	10	23,783,772	-
Investments in equity securities	11	32,093	-
Loans and advances to customers	12	103,780,022	95,431,247
Available-for-sale investment securities	13	-	23,299,746
Current income tax prepayment		-	16,325
Other assets	14	4,849,894	4,267,355
Deferred income tax asset	25	1,059,593	1,152,217
Property, equipment and intangible assets	15	2,718,200	3,135,984
TOTAL ASSETS		**196,669,481**	**208,649,222**
LIABILITIES			
Due to other banks	16	421,388	6,884,250
Current accounts and deposits from customers	17	152,952,355	158,579,491
Other liabilities	18	3,740,031	4,199,145
TOTAL LIABILITIES		**157,113,774**	**169,662,886**
EQUITY			
Share capital	19	18,434,350	18,434,350
Retained earnings		20,752,161	20,047,198
Share-based payments reserve		83,371	95,927
Revaluation reserve for financial assets at fair value through other comprehensive income	20	(123,036)	-
Revaluation reserve for AFS securities	20	175,089	175,089
Revaluation reserve for land and buildings	20	233,772	233,772
TOTAL EQUITY		**39,555,707**	**38,986,336**
TOTAL LIABILITIES AND EQUITY		**196,669,481**	**208,649,222**

Approved for issue by the Board of the Bank and signed by the Management of the Bank on 23 April 2019.

Paul Edgar
Chief Executive Officer

Astghik Dramyan
Chief Financial Officer/Deputy CFO

In thousands of Armenian Drams	Note	2018	2017
Interest income calculated using the effective interest method	21	10,843,490	12,535,649
Other similar income	21	262,603	420,077
Interest and similar expense	21	(3,605,338)	(4,752,407)
Net margin on interest and similar income		**7,500,755**	**8,203,319**
Credit loss allowance		(1,513,411)	(14,185,858)
Net margin on interest and similar income after credit loss allowance		**5,987,344**	**(5,982,539)**
Fee and commission income	22	2,750,969	3,622,549
Fee and commission expense	22	(507,020)	(466,002)
Gains less losses from financial assets at fair value through profit or loss		-	187,691
Gains less losses from financial derivatives		89,317	-
Gains less losses from investments		8,988	-
Gains less losses from trading in foreign currencies	23	717,348	1,044,549
Other operating income		225,135	260,388
Other operating expenses		-	(549,137)
Personnel expenses		(4,213,947)	(4,083,834)
Other general administrative expenses	24	(4,379,596)	(4,155,149)
Profit/(Loss) before tax		**678,538**	**(10,121,484)**
Income tax (expense)/credit	25	(123,385)	2,180,901
PROFIT/(LOSS) FOR THE YEAR		**555,153**	**(7,940,583)**
Other comprehensive loss:			
Items that may be reclassified subsequently to profit or loss:			
Available-for-sale investments:			
- Losses less gains arising during the year	13	-	(82,002)
Debt securities at fair value through other comprehensive income:			
- Losses less gains arising during the year	10	(123,036)	-
Other comprehensive loss for the year		**(123,036)**	**(82,002)**
TOTAL COMPREHENSIVE INCOME / (LOSS) FOR THE YEAR		**432,117**	**(8,022,585)**

In thousands of Armenian Drams	Note	Share capital	Share-based payments reserve	Revaluation reserve for AFS securities	Revaluation reserve for securities at FVOCI	Revaluation reserve for land and buildings	Retained earnings	Total
Balance at 1 January 2017		**18,434,350**	**94,788**	**257,091**	**-**	**233,772**	**27,987,221**	**47,007,222**
Loss for the year		-	-	-	-	-	(7,940,583)	(7,940,583)
Other comprehensive loss	20	-	-	(82,002)	-	-	-	(82,002)
Total comprehensive loss for 2017		-	-	(82,002)	-	-	(7,940,583)	(8,022,585)
Share-based payments		-	1,139	-	-	-	560	1,699
Balance at 31 December 2017		**18,434,350**	**95,927**	**175,089**	**-**	**233,772**	**20,047,198**	**38,986,336**
Adoption of IFRS 9:								
– remeasurement for expected credit losses, net of tax	5	-	-	-	-	-	149,810	149,810
Restated balance at 1 January 2018		**18,434,350**	**95,927**	**175,089**	**-**	**233,772**	**20,197,008**	**39,136,146**
Profit for the year		-	-	-	-	-	555,153	555,153
Other comprehensive loss	20	-	-	-	(123,036)	-	-	(123,036)
Total comprehensive income for 2018		-	-	-	(123,036)	-	555,153	432,117
Share-based payments		-	(12,556)	-	-	-	-	(12,556)
Balance at 31 December 2018		**18,434,350**	**83,371**	**175,089**	**(123,036)**	**233,772**	**20,752,161**	**39,555,707**

In thousands of Armenian Drams	Note	2018	2017
Cash flows from operating activities			
Interest income calculated using the effective interest method received		10,214,666	11,846,215
Interest paid		(3,951,966)	(4,773,406)
Fees and commissions received		3,006,553	3,583,990
Fees and commissions paid		(608,207)	(480,573)
Income received from financial instruments at fair value		-	218,394
Income received from trading in trading securities		43,244	-
Income received from financial derivatives		166,582	-
Income received from trading in foreign currencies		742,042	1,110,776
Net other operating income received		225,135	22,494
Staff costs paid		(4,229,983)	(3,210,068)
Administrative expenses paid		(3,207,231)	(3,154,310)
Income tax received		3,241	-
Cash flows from operating activities before changes in operating assets and liabilities		**2,404,076**	**5,163,512**
Net (increase)/decrease in:			
- financial assets at fair value through profit or loss		-	(427,429)
- investments in debt securities at fair value through profit or loss		357,575	-
- available-for-sale financial assets		-	1,261,341
- investments in debt securities at fair value through other comprehensive income		4,686,062	-
- debt securities carried at amortised cost		(5,011,361)	-
- loans and advances to banks		(6,888,522)	(4,172,054)
- loans and advances to customers		(8,534,602)	13,247,265
- other assets		(1,692,733)	(1,269,005)
Net increase/(decrease) in:			
- due to other banks		(6,175,149)	(5,352,250)
- current accounts and deposits from customers		(4,054,904)	6,901,256
- other liabilities		264,137	(20,341)
Net cash (used in)/from operating activities		**(24,645,421)**	**15,332,295**
Cash flows from investing activities			
Acquisition of property, equipment and intangible assets	15	(752,669)	(650,970)
Proceeds from disposal of property, equipment and intangible assets	15	3,905	4,325
Net cash used in investing activities		**(748,764)**	**(646,645)**
Effect of exchange rate changes on cash and cash equivalents		**(924,130)**	**703,044**
Net (decrease)/increase in cash and cash equivalents		**(26,318,315)**	**15,388,694**
Cash and cash equivalents at the beginning of the year		68,935,410	53,546,716
Cash and cash equivalents at the end of the year	7	**42,617,095**	**68,935,410**

1 Introduction

These financial statements have been prepared in accordance with International Financial Reporting Standards for the year ended 31 December 2018 for HSBC Bank Armenia CJSC (the “Bank”).

The Bank was incorporated and is domiciled in the Republic of Armenia. The Bank is a closed joint stock company and was set up in accordance with Armenian regulations.

The Bank is owned by HSBC Europe B.V. (70%) and Wings Establishment (30%). As of 31 December 2018 and 2017 the Bank’s immediate and ultimate parent company was HSBC Europe B.V. and the Bank was ultimately controlled by HSBC Holdings PLC.

Principal activity. The Bank’s principal business activity is commercial and retail banking operations within the Republic of Armenia. The Bank has operated under a full banking licence issued by the Central Bank of Armenia (“CBA”) since 1995.

The Bank has 8 branches and a National Service Center (2017: 8 branches and a National Service Center) within the Republic of Armenia. The Bank had 403 average number of employees during the year 2018 (2017: 414 employees).

Registered address and place of business. The Bank’s registered address is: 66 Teryan Street, Yerevan 0009, Republic of Armenia.

Presentation currency. These financial statements are presented in Armenian Drams ("AMD"), unless otherwise stated.

2 Operating Environment of the Bank

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 to develop and are subject to frequent changes and varying interpretations, refer to Note 28.

The economic environment of the Republic of Armenia is significantly influenced by the level of business activity in the Russian Federation and significant cash movements flow from the Russian Federation to the Republic of Armenia. Therefore, a decline in business activity, stock market volatility and other risks experienced in the Russian Federation could have a flow-on negative effect on the financial and corporate sectors of the Republic of Armenia. Armenian economy was growing in 2018 after overcoming the economic recession of 2015 and 2016. Growth was driven mainly by a recovery in the external environment and supported by a strong rebound in domestic demand. Consumption benefited from higher incomes and a recovery in remittances, particularly due to the moderate recovery in Russia. The financial markets continue to be volatile. This operating environment has a significant impact on the Bank’s operations and financial position. Management is taking necessary measures to ensure sustainability of the Bank’s operations. However, the future effects of the current economic situation are difficult to predict and management’s current expectations and estimates could differ from actual results.

For the purpose of measurement of expected credit losses (“ECL”) the Bank uses supportable forward-looking information, including forecasts of macroeconomic variables. As with any economic forecast, however, the projections and likelihoods of their occurrence are subject to a high degree of inherent uncertainty and therefore the actual outcomes may be significantly different from those projected. Note 26 provides more information of how the Bank incorporated forward-looking information in the ECL models.

3 Significant Accounting Policies

Basis of preparation. These financial statements have been prepared in accordance with International Financial Reporting Standards (“IFRS”) under the historical cost convention, as modified by the initial recognition of financial instruments based on fair value, and by the revaluation of reposessed collateral, financial instruments categorised at fair value through profit or loss (“FVTPL”) and at fair value through other comprehensive income (“FVOCI”). The principal accounting policies applied in the preparation of these financial statements are set out below. Apart from the accounting policy changes resulting from the adoption of IFRS 9 and IFRS 15 effective from 1 January 2018, these policies have been consistently applied to all the periods presented, unless otherwise stated. Refer to Notes 5 and 35.

3 Significant Accounting Policies (Continued)

Financial instruments – key measurement terms. Depending on their classification financial instruments are carried at fair value or amortised cost as described below.

Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. The best evidence of fair value is price in an active market. An active market is one in which transactions for the asset or liability take place with sufficient frequency and volume to provide pricing information on an ongoing basis. Fair value of financial instruments traded in an active market is measured as the product of the quoted price for the individual asset or liability and the quantity held by the entity. This is the case even if a market's normal daily trading volume is not sufficient to absorb the quantity held and placing orders to sell the position in a single transaction might affect the quoted price.

Valuation techniques such as discounted cash flow models or models based on recent arm's length transactions or consideration of financial data of the investees, are used to measure fair value of certain financial instruments for which external market pricing information is not available. Fair value measurements are analysed by level in the fair value hierarchy as follows: (i) level one are measurements at quoted prices (unadjusted) in active markets for identical assets or liabilities, (ii) level two measurements are valuations techniques with all material inputs observable for the asset or liability, either directly (that is, as prices) or indirectly (that is, derived from prices), and (iii) level three measurements are valuations not based on solely observable market data (that is, the measurement requires significant unobservable inputs). Transfers between levels of the fair value hierarchy are deemed to have occurred at the end of the reporting period. Refer to Note 31.

Transaction costs are incremental costs that are directly attributable to the acquisition, issue or disposal of a financial instrument. An incremental cost is one that would not have been incurred if the transaction had not taken place. Transaction costs include fees and commissions paid to agents (including employees acting as selling agents), advisors, brokers and dealers, levies by regulatory agencies and securities exchanges, and transfer taxes and duties. Transaction costs do not include debt premiums or discounts, financing costs or internal administrative or holding costs.

Amortised cost ("AC") is the amount at which the financial instrument was recognised at initial recognition less any principal repayments, plus accrued interest, and for financial assets less any allowance for expected credit losses. Accrued interest includes amortisation of transaction costs deferred at initial recognition and of any premium or discount to maturity amount using the effective interest method. Accrued interest income and accrued interest expense, including both accrued coupon and amortised discount or premium (including fees deferred at origination, if any), are not presented separately and are included in the carrying values of related items in the statement of financial position.

The effective interest method is a method of allocating interest income or interest expense over the relevant period, so as to achieve a constant periodic rate of interest (effective interest rate) on the carrying amount. The effective interest rate is the rate that exactly discounts estimated future cash payments or receipts (excluding future credit losses) through the expected life of the financial instrument or a shorter period, if appropriate, to the gross carrying amount of the financial instrument.

3 Significant Accounting Policies (Continued)

The effective interest rate discounts cash flows of variable interest instruments to the next interest repricing date, except for the premium or discount, which reflects the credit spread over the floating rate specified in the instrument, or other variables that are not reset to market rates. Such premiums or discounts are amortised over the whole expected life of the instrument. The present value calculation includes all fees paid or received between parties to the contract that are an integral part of the effective interest rate. For assets that are purchased or originated credit impaired ("POCI") at initial recognition, the effective interest rate is adjusted for credit risk, i.e. it is calculated based on the expected cash flows on initial recognition instead of contractual payments.

Financial instruments – initial recognition. Financial instruments at FVTPL are initially recorded at fair value. All other financial instruments are initially recorded at fair value adjusted for transaction costs. Fair value at initial recognition is best evidenced by the transaction price. A gain or loss on initial recognition is only recorded if there is a difference between fair value and transaction price which can be evidenced by other observable current market transactions in the same instrument or by a valuation technique whose inputs include only data from observable markets. After the initial recognition, an ECL allowance is recognised for financial assets measured at AC and investments in debt instruments measured at FVOCI, resulting in an immediate accounting loss.

All purchases and sales of financial assets that require delivery within the time frame established by regulation or market convention ("regular way" purchases and sales) are recorded at trade date, which is the date on which the Bank commits to deliver a financial asset. All other purchases are recognised when the entity becomes a party to the contractual provisions of the instrument.

Financial assets – classification and subsequent measurement – measurement categories. The Bank classifies financial assets in the following measurement categories: FVTPL, FVOCI and AC. The classification and subsequent measurement of debt financial assets depends on: (i) the Bank's business model for managing the related assets portfolio and (ii) the cash flow characteristics of the asset.

Financial assets – classification and subsequent measurement – business model. The business model reflects how the Bank manages the assets in order to generate cash flows – whether the Bank's objective is: (i) solely to collect the contractual cash flows from the assets ("hold to collect contractual cash flows",) or (ii) to collect both the contractual cash flows and the cash flows arising from the sale of assets ("hold to collect contractual cash flows and sell") or, if neither of (i) and (ii) is applicable, the financial assets are classified as part of "other" business model and measured at FVTPL.

Business model is determined for a group of assets (on a portfolio level) based on all relevant evidence about the activities that the Bank undertakes to achieve the objective set out for the portfolio available at the date of the assessment. Factors considered by the Bank in determining the business model include the purpose and composition of a portfolio, past experience on how the cash flows for the respective assets were collected, how risks are assessed and managed, how the assets' performance is assessed and how managers are compensated. Refer to Note 4 for critical judgements applied by the Bank in determining the business models for its financial assets.

Financial assets – classification and subsequent measurement – cash flow characteristics. Where the business model is to hold assets to collect contractual cash flows or to hold contractual cash flows and sell, the Bank assesses whether the cash flows represent solely payments of principal and interest ("SPPI"). Financial assets with embedded derivatives are considered in their entirety when determining whether their cash flows are consistent with the SPPI feature. In making this assessment, the Bank considers whether the contractual cash flows are consistent with a basic lending arrangement, i.e. interest includes only consideration for credit risk, time value of money, other basic lending risks and profit margin.

3 Significant Accounting Policies (Continued)

Where the contractual terms introduce exposure to risk or volatility that is inconsistent with a basic lending arrangement, the financial asset is classified and measured at FVTPL. The SPPI assessment is performed on initial recognition of an asset and it is not subsequently reassessed. Refer to Note 4 for critical judgements applied by the Bank in performing the SPPI test for its financial assets.

Financial assets – reclassification. Financial instruments are reclassified only when the business model for managing the portfolio as a whole changes. The reclassification has a prospective effect and takes place from the beginning of the first reporting period that follows after the change in the business model.

Financial assets impairment – credit loss allowance for ECL. The Bank assesses, on a forward-looking basis, the ECL for debt instruments measured at AC and FVOCI and for the exposures arising from loan commitments and financial guarantee contracts. The Bank measures ECL and recognises credit loss allowance at each reporting date. The measurement of ECL reflects: (i) an unbiased and probability weighted amount that is determined by evaluating a range of possible outcomes, (ii) time value of money and (iii) all reasonable and supportable information that is available without undue cost and effort at the end of each reporting period about past events, current conditions and forecasts of future conditions.

Debt instruments measured at AC are presented in the statement of financial position net of the allowance for ECL. For loan commitments and financial guarantees, a separate provision for ECL is recognised as a liability in the statement of financial position. For debt instruments at FVOCI, changes in amortised cost, net of allowance for ECL, are recognised in profit or loss and other changes in carrying value are recognised in OCI as gains less losses on debt instruments at FVOCI.

The Bank applies a three stage model for impairment, based on changes in credit quality since initial recognition. A financial instrument that is not credit-impaired on initial recognition is classified in Stage 1. Financial assets in Stage 1 have their ECL measured at an amount equal to the portion of lifetime ECL that results from default events possible within the next 12 months or until contractual maturity, if shorter ("12 Months ECL"). If the Bank identifies a significant increase in credit risk ("SICR") since initial recognition, the asset is transferred to Stage 2 and its ECL is measured based on ECL on a lifetime basis, that is, up until contractual maturity but considering expected prepayments, if any ("Lifetime ECL"). Refer to Note 26 for a description of how the Bank determines when a SICR has occurred. If the Bank determines that a financial asset is credit-impaired, the asset is transferred to Stage 3 and its ECL is measured as a Lifetime ECL. For financial assets that are purchased or originated credit-impaired ("POCI Assets"), the ECL is always measured as a Lifetime ECL. Note 26 provides information about inputs, assumptions and estimation techniques used in measuring ECL, including an explanation of how the Bank incorporates forward-looking information in the ECL models.

Expected credit loss model is used to calculate impairment allowance for wholesale book and retail book. Under this model, the financial instruments are subdivided into three sub-portfolios, called stages henceforth, depending on the instruments' increase in credit risk since their origination. ECL allowances on Wholesale portfolios are calculated on a collectively modelled basis for Stage 1 and Stage 2 financial instruments and on an individually assessed basis for Stage 3 credit-impaired financial instruments and POCIs. The impairment calculation is made at instrument level.

Retail ECL methodology is undertaken on a collectively modelled basis for all stages.

There are three stages to the proposed model to reflect the general pattern of deterioration of a financial instrument that ultimate defaults.

• Stage 1: non-impaired instruments where there is no significant increase in credit risk since initial recognition (Good book).

• Stage 2: non-impaired instruments where there is a significant increase in credit risk since initial recognition (Deteriorated book).

• Stage 3: impaired instruments, where an actual default event (or events) has occurred (Defaulted book).

3 Significant Accounting Policies (Continued)

For financial assets that are purchased or originated credit-impaired (“POCI Assets”), the ECL is always measured as a Lifetime ECL.

Expected Credit Losses should be calculated using a small portfolio approach for all retail portfolios, except Credit Cards portfolio. Aggregated Risk-Based (Segment level) approach is applied for Credit Cards portfolio.

Three modelling approaches are adopted for forecasting PIT PDs (Point in Time Probability of Default) and PIT LGDs (Point in Time Loss Given Default) for wholesale book ECL calculation: Sovereign, Banks and Corporate.

The impairment allowance should reflect 12-month ECLs or lifetime ECLs, depending on whether the credit risk of the asset has significantly increased since initial recognition.

Financial assets – write-off. Financial assets are written-off, in whole or in part, when the Bank exhausted all practical recovery efforts and has concluded that there is no reasonable expectation of recovery. The write-off represents a derecognition event. The Bank may write-off financial assets that are still subject to enforcement activity when the Bank seeks to recover amounts that are contractually due, however, there is no reasonable expectation of recovery.

Financial assets – derecognition. The Bank derecognises financial assets when (a) the assets are redeemed or the rights to cash flows from the assets otherwise expired or (b) the Bank has transferred the rights to the cash flows from the financial assets or entered into a qualifying pass-through arrangement while (i) also transferring substantially all risks and rewards of ownership of the assets or (ii) neither transferring nor retaining substantially all risks and rewards of ownership, but not retaining control. Control is retained if the counterparty does not have the practical ability to sell the asset in its entirety to an unrelated third party without needing to impose restrictions on the sale.

Financial assets – modification. The Bank sometimes renegotiates or otherwise modifies the contractual terms of the financial assets. The Bank assesses whether the modification of contractual cash flows is substantial considering, among other, the following factors: any new contractual terms that substantially affect the risk profile of the asset (e.g. profit share or equity-based return), significant change in interest rate, change in the currency denomination, new collateral or credit enhancement that significantly affects the credit risk associated with the asset or a significant extension of a loan when the borrower is not in financial difficulties.

If the modified terms are substantially different, the rights to cash flows from the original asset expire and the Bank derecognises the original financial asset and recognises a new asset at its fair value. The date of renegotiation is considered to be the date of initial recognition for subsequent impairment calculation purposes, including determining whether a SICR has occurred. The Bank also assesses whether the new loan or debt instrument meets the SPPI criterion. Any difference between the carrying amount of the original asset derecognised and fair value of the new substantially modified asset is recognised in profit or loss, unless the substance of the difference is attributed to a capital transaction with owners.

In a situation where the renegotiation was driven by financial difficulties of the counterparty and inability to make the originally agreed payments, the Bank compares the original and revised expected cash flows to assets whether the risks and rewards of the asset are substantially different as a result of the contractual modification. If the risks and rewards do not change, the modified asset is not substantially different from the original asset and the modification does not result in derecognition. The Bank recalculates the gross carrying amount by discounting the modified contractual cash flows by the original effective interest rate (or credit-adjusted effective interest rate for POCI financial assets), and recognises a modification gain or loss in profit or loss.

3 Significant Accounting Policies (Continued)

Financial liabilities – measurement categories. Financial liabilities are classified as subsequently measured at AC, except for financial liabilities at FVTPL: this classification is applied to derivatives, other financial liabilities designated as such at initial recognition and financial guarantee contracts and loan commitments.

Financial liabilities – derecognition. Financial liabilities are derecognised when they are extinguished (i.e. when the obligation specified in the contract is discharged, cancelled or expires).

An exchange between the Bank and its original lenders of debt instruments with substantially different terms, as well as substantial modifications of the terms and conditions of existing financial liabilities, are accounted for as an extinguishment of the original financial liability and the recognition of a new financial liability. The terms are substantially different if the discounted present value of the cash flows under the new terms, including any fees paid net of any fees received and discounted using the original effective interest rate, is at least 10% different from the discounted present value of the remaining cash flows of the original financial liability. If an exchange of debt instruments or modification of terms is accounted for as an extinguishment, any costs or fees incurred are recognised as part of the gain or loss on the extinguishment. If the exchange or modification is not accounted for as an extinguishment, any costs or fees incurred adjust the carrying amount of the liability and are amortised over the remaining term of the modified liability.

Modifications of liabilities that do not result in extinguishment are accounted for as a change in estimate using a cumulative catch up method, with any gain or loss recognised in profit or loss, unless the economic substance of the difference in carrying values is attributed to a capital transaction with owners.

Cash and cash equivalents. Cash and cash equivalents are items which are readily convertible to known amounts of cash and which are subject to an insignificant risk of changes in value. Cash and cash equivalents include notes and coins on hand, mandatory reserve deposits with the CBA, unrestricted balances (nostro accounts, overnight deposits and placements with original maturities of less than three months) held with the CBA and other banks. Funds restricted for a period of more than three months on origination are excluded from cash and cash equivalents, both in the statement of financial position and for the purposes of the statement of cash flows. Cash and cash equivalents are carried at AC because: (i) they are held for collection of contractual cash flows and those cash flows represent SPPI, and (ii) they are not designated at FVTPL.

The payments or receipts presented in the statement of cash flows represent transfers of cash and cash equivalents by the Bank, including amounts charged or credited to current accounts of the Bank's counterparties held with the Bank, such as loan interest income or principal collected by charging the customer's current account or interest payments or disbursement of loans credited to the customer's current account, which represents cash or cash equivalent from the customer's perspective.

Mandatory cash balances with the CBA. Mandatory cash balances with the CBA are carried at AC and represent non-interest bearing mandatory reserve deposits, which are not available to finance the Bank's day to day operations, and hence are not considered as part of cash and cash equivalents for the purposes of the statement of cash flows.

Loans and advances to banks. Amounts of loans and advances to banks are recorded when the Bank advances money to counterparty banks. Amounts of loans and advances to banks are carried at AC when: (i) they are held for the purposes of collecting contractual cash flows and those cash flows represent SPPI, and (ii) they are not designated at FVTPL.

Investments in debt securities. Based on the business model and the cash flow characteristics, the Bank classifies investments in debt securities as carried at AC, FVOCI or FVTPL. Debt securities are carried at AC if they are held for collection of contractual cash flows and where those cash flows represent SPPI, and if they are not voluntarily designated at FVTPL in order to significantly reduce an accounting mismatch.

Debt securities are carried at FVOCI if they are held for collection of contractual cash flows and for selling, where those cash flows represent SPPI, and if they are not designated at FVTPL. Interest income from these assets is calculated using the effective interest method and recognised in profit or loss. An impairment allowance estimated using the expected credit loss model is recognised in profit or loss for the year. All other changes in the carrying value are recognised in OCI. When the debt security is derecognised, the cumulative gain or loss previously recognised in OCI is reclassified from OCI to profit or loss.

3 Significant Accounting Policies (Continued)

Investments in debt securities are carried at FVTPL if they do not meet the criteria for AC or FVOCI. The Bank may also irrevocably designate investments in debt securities at FVTPL on initial recognition if applying this option significantly reduces an accounting mismatch between financial assets and liabilities being recognised or measured on different accounting bases.

Investments in equity securities. Financial assets that meet the definition of equity from the issuer's perspective, i.e. instruments that do not contain a contractual obligation to pay cash and that evidence a residual interest in the issuer's net assets, are considered as investments in equity securities by the Bank. Investments in equity securities are measured at FVTPL, except where the Bank elects at initial recognition to irrevocably designate an equity investments at FVOCI. The Bank's policy is to designate equity investments as FVOCI when those investments are held for strategic purposes other than solely to generate investment returns. When the FVOCI election is used, fair value gains and losses are recognised in OCI and are not subsequently reclassified to profit or loss, including on disposal. Impairment losses and their reversals, if any, are not measured separately from other changes in fair value. Dividends continue to be recognised in profit or loss when the Bank's right to receive payments is established except when they represent a recovery of an investment rather than a return on such investment.

Loans and advances to customers. Loans and advances to customers are recorded when the Bank advances money to purchase or originate a loan due from a customer. Based on the business model and the cash flow characteristics, the Bank classifies loans and advances to customers into AC: loans that are held for collection of contractual cash flows and those cash flows represent SPPI and loans that are not voluntarily designated at FVTPL.

Impairment allowances are determined based on the forward-looking ECL models. Note 26 provides information about inputs, assumptions and estimation techniques used in measuring ECL, including an explanation of how the Bank incorporates forward-looking information in the ECL models.

Repossessed collateral. Repossessed collateral represents financial and non-financial assets acquired by the Bank in settlement of overdue loans. The assets are initially recognised at fair value when acquired and included in premises and equipment, other financial assets, investment properties or inventories within other assets depending on their nature and the Bank's intention in respect of recovery of these assets, and are subsequently remeasured and accounted for in accordance with the accounting policies for these categories of assets.

Loan commitments. The Bank issues commitments to provide loans. These commitments are irrevocable or revocable only in response to a material adverse change. Such commitments are initially recognised at their fair value, which is normally evidenced by the amount of fees received. This amount is amortised on a straight line basis over the life of the commitment, except for commitments to originate loans if it is probable that the Bank will enter into a specific lending arrangement and does not expect to sell the resulting loan shortly after origination; such loan commitment fees are deferred and included in the carrying value of the loan on initial recognition. At the end of each reporting period, the commitments are measured at (i) the remaining unamortised balance of the amount at initial recognition, plus (ii) the amount of the loss allowance determined based on the expected credit loss model, unless the commitment is to provide a loan at a below market interest rate, in which case the measurement is at the higher of these two amounts. The carrying amount of the loan commitments represents a liability. For contracts that include both a loan and an undrawn commitment and where the Bank cannot separately distinguish the ECL on the undrawn loan component from the loan component, the ECL on the undrawn commitment is recognised together with the loss allowance for the loan. To the extent that the combined ECLs exceed the gross carrying amount of the loan, they are recognised as a liability.

3 Significant Accounting Policies (Continued)

Financial guarantees. Financial guarantees require the Bank to make specified payments to reimburse the holder of the guarantee for a loss it incurs because a specified debtor fails to make payment when due in accordance with the original or modified terms of a debt instrument. Financial guarantees are initially recognised at their fair value, which is normally evidenced by the amount of fees received. This amount is amortised on a straight line basis over the life of the guarantee. At the end of each reporting period, the guarantees are measured at the higher of (i) the amount of the loss allowance for the guaranteed exposure determined based on the expected loss model and (ii) the remaining unamortised balance of the amount at initial recognition. In addition, an ECL loss allowance is recognised for fees receivable that are recognised in the statement of financial position as an asset.

Performance guarantees. Performance guarantees are contracts that provide compensation if another party fails to perform a contractual obligation. Such contracts transfer non-financial performance risk in addition to credit risk. Performance guarantees are initially recognised at their fair value, which is normally evidenced by the amount of fees received. This amount is amortised on a straight line basis over the life of the contract. At the end of each reporting period, the performance guarantee contracts are measured at the higher of (i) the unamortised balance of the amount at initial recognition and (ii) the best estimate of expenditure required to settle the contract at the end of each reporting period, discounted to present value. Where the Bank has the contractual right to revert to its customer for recovering amounts paid to settle the performance guarantee contracts, such amounts will be recognised as an asset upon transfer of the loss compensation to the guarantee's beneficiary. These fees are recognised within fee and commission income in profit or loss.

Sale and repurchase agreements. Sale and repurchase agreements ("repo agreements"), which effectively provide a lender's return to the counterparty, are treated as secured financing transactions. Securities sold under such sale and repurchase agreements are not derecognised. The securities are reclassified as repurchase receivables in the statement of financial position if the transferee has the right by contract or custom to sell or repledge the securities. The corresponding liability is presented within amounts due to other banks or other borrowed funds.

Securities purchased under agreements to resell ("reverse repo agreements"), which effectively provide a lender's return to the Bank, are recorded as loans and advances to banks or loans and advances to customers, as appropriate. The difference between the sale and repurchase price, adjusted by interest and dividend income collected by the counterparty, is treated as interest income and accrued over the life of repo agreements using the effective interest method.

Securities lent to counterparties for a fixed fee are retained in the financial statements in their original category in the statement of financial position unless the counterparty has the right by contract or custom to sell or repledge the securities, in which case they are reclassified and presented separately. Securities borrowed for a fixed fee are not recorded in the financial statements, unless these are sold to third parties, in which case the purchase and sale are recorded in profit or loss for the year within gains less losses arising from trading securities. The obligation to return the securities is recorded at fair value in other borrowed funds.

Based on classification of securities sold under the sale and repurchase agreements, the Bank classifies repurchase receivables into one of the following measurement categories: AC, FVOCI, and FVTPL.

3 Significant Accounting Policies (Continued)

Property, equipment and intangible 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.

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 and the comparable sales approach depending on availability and reliability of information.

At the end of each reporting period management assesses whether there is any indication of impairment of premises and equipment. If any such indication exists, management estimates the recoverable amount, which is determined as the higher of an asset's fair value less costs to sell and its value in use. The carrying amount is reduced to the recoverable amount and the impairment loss is recognised in profit or loss for the year to the extent it exceeds the previous revaluation surplus in equity. An impairment loss recognised for an asset in prior years is reversed if there has been a change in the estimates used to determine the asset's value in use or fair value less costs to sell.

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
- equipment fixtures and fittings	4 to 7 years

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 capitalised 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 recognised as an expense as incurred.

Amortisation 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

3 Significant Accounting Policies (Continued)

Operating leases. Where the Bank is a lessee in a lease which does not transfer substantially all the risks and rewards incidental to ownership from the lessor to the Bank, the total lease payments are charged to profit or loss for the year (rental expense) on a straight-line basis over the period of the lease.

Due to other banks. Amounts due to other banks are recorded when money or other assets are advanced to the Bank by counterparty banks.

Current accounts and deposits from customers. Customer accounts are non-derivative liabilities to individuals, state or corporate customers and are carried at AC.

Financial liabilities designated at FVTPL. The Bank may designate certain liabilities at FVTPL at initial recognition. Gains and losses on such liabilities are presented in profit or loss except for the amount of change in the fair value that is attributable to changes in the credit risk of that liability (determined as the amount that is not attributable to changes in market conditions that give rise to market risk), which is recorded in OCI and is not subsequently reclassified to profit or loss. This is unless such a presentation would create, or enlarge, an accounting mismatch, in which case the gains and losses attributable to changes in credit risk of the liability are also presented in profit or loss.

Derivative financial instruments. Derivative financial instruments, including foreign exchange contracts, forwards and spots, are carried at their fair value.

All derivative instruments are carried as assets when fair value is positive, and as liabilities when fair value is negative. Changes in the fair value of derivative instruments are included in profit or loss for the year (gains less losses on derivatives).

Income taxes. Income taxes have been provided for in the financial statements in accordance with legislation enacted or substantively enacted by the end of the reporting period. The income tax charge comprises current tax and deferred tax and is recognised in profit or loss for the year, except if it is recognised in other comprehensive income or directly in equity because it relates to transactions that are also recognised, in the same or a different period, in other comprehensive income or directly in equity.

Current tax is the amount expected to be paid to, or recovered from, the taxation authorities in respect of taxable profits or losses for the current and prior periods. Taxable profits or losses are based on estimates if the financial statements are authorised prior to filing relevant tax returns. Taxes other than on income are recorded within administrative and other operating expenses.

Deferred income tax is provided using the balance sheet liability method for tax loss carry forwards and temporary differences arising between the tax bases of assets and liabilities and their carrying amounts for financial reporting purposes.

3 Significant Accounting Policies (Continued)

In accordance with the initial recognition exemption, deferred taxes are not recorded for temporary differences on initial recognition of an asset or a liability in a transaction other than a business combination if the transaction, when initially recorded, affects neither accounting nor taxable profit. Deferred tax balances are measured at tax rates enacted or substantively enacted at the end of the reporting period, which are expected to apply to the period when the temporary differences will reverse or the tax loss carry forwards will be utilised.

Deferred tax assets for deductible temporary differences and tax loss carry forwards are recorded only to the extent that it is probable that future taxable profit will be available against which the deductions can be utilised.

Provisions for liabilities and charges. Provisions for liabilities and charges are non-financial liabilities of uncertain timing or amount. They are accrued when the Bank has a present legal or constructive obligation as a result of past events, it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation, and a reliable estimate of the amount of the obligation can be made.

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.

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.

Interest income and expense recognition. Interest income and expense are recorded for all debt instruments on an accrual basis using the effective interest method. This method defers, as part of interest income or expense, all fees paid or received between the parties to the contract that are an integral part of the effective interest rate, transaction costs and all other premiums or discounts.

Interest income on debt instruments calculated at nominal interest rate is presented within 'other similar income' line in profit or loss.

Fees integral to the effective interest rate include origination fees received or paid by the entity relating to the creation or acquisition of a financial asset or issuance of a financial liability, for example fees for evaluating creditworthiness, evaluating and recording guarantees or collateral, negotiating the terms of the instrument and for processing transaction documents. Commitment fees received by the Bank to originate loans at market interest rates are integral to the effective interest rate if it is probable that the Bank will enter into a specific lending arrangement and does not expect to sell the resulting loan shortly after origination. The Bank does not designate loan commitments as financial liabilities at FVTPL.

For financial assets that are originated or purchased credit-impaired, the effective interest rate is the rate that discounts the expected cash flows (including the initial expected credit losses) to the fair value on initial recognition (normally represented by the purchase price). As a result, the effective interest is credit-adjusted.

Interest income is calculated by applying the effective interest rate to the gross carrying amount of financial assets, except for (i) financial assets that have become credit impaired (Stage 3), for which interest revenue is calculated by applying the effective interest rate to their AC, net of the ECL provision, and (ii) financial assets that are purchased or originated credit impaired, for which the original credit-adjusted effective interest rate is applied to the AC.

3 Significant Accounting Policies (Continued)

Fee and commission income. Fee and commission income is recognised over time on a straight line basis as the services are rendered, when the customer simultaneously receives and consumes the benefits provided by the Bank's performance. Such income includes recurring fees for account maintenance, account servicing fees, account subscription fees, premium service package fees, etc. Variable fees are recognised only to the extent that management determines that it is highly probable that a significant reversal will not occur.

Other fee and commission income is recognised at a point in time when the Bank satisfies its performance obligation, usually upon execution of the underlying transaction. The amount of fee or commission received or receivable represents the transaction price for the services identified as distinct performance obligations. Such income includes fees for arranging a sale or purchase of foreign currencies on behalf of a customer, fees for processing payment transactions, fees for cash settlements, collection or cash disbursements.

Fiduciary assets and custody services. Assets held by the Bank in its own name, but on the account of third parties, are not reported in the statement of financial position. The amount of the fee received or receivable represents the consideration for the services.

These fees are recognised over time, on a straight-line basis, when the services are rendered because the customer simultaneously receives and consumes the benefits as the Bank performs. Fees from fiduciary activities are presented within fee and commission income.

Sales and purchases of foreign currencies and currency conversion. The Bank sells and purchases foreign currencies in the cash offices and through the bank accounts, as well as exchanges foreign currencies. The transactions are performed at the exchange rates established by the Bank, which are different from the official spot exchange rates at the particular dates. The differences between the official rates and Bank rates are recognised as gains less losses from trading in foreign currencies at a point in time when a particular performance obligation is satisfied.

Foreign currency translation. The functional currency of the Bank's is the currency of the primary economic environment in which the entity operates. The functional currency of the Bank and the Bank's presentation currency, is the national currency of the Republic of Armenia, Armenian Dram ("AMD").

Monetary assets and liabilities are translated into each entity's functional currency at the official exchange rate of the CBA at the end of the respective reporting period. Foreign exchange gains and losses resulting from the settlement of transactions and from the translation of monetary assets and liabilities into the Bank's functional currency at year-end official exchange rates of the CBA, are recognised in profit or loss for the year (as foreign exchange translation gains less losses). Translation at year-end rates does not apply to non-monetary items that are measured at historical cost.

Non-monetary items measured at fair value in a foreign currency, including equity investments, are translated using the exchange rates at the date when the fair value was determined.

Effects of exchange rate changes on non-monetary items measured at fair value in a foreign currency are recorded as part of the fair value gain or loss.

At 31 December 2018, the principal rate of exchange used for translating foreign currency balances was USD 1 = AMD 483.75 (2017: USD 1 = AMD 484.1), EUR 1 = AMD 553.65 (2017: EUR 1=AMD 580.10), GBP 1 = 611.61 (2017: GBP 1 = AMD 653.54).

Offsetting. Financial assets and liabilities are offset and the net amount reported in the statement of financial position only when there is a legally enforceable right to offset the recognised amounts, and there is an intention to either settle on a net basis, or to realise the asset and settle the liability simultaneously. Such a right of set off (a) must not be contingent on a future event and (b) must be legally enforceable in all of the following circumstances: (i) in the normal course of business, (ii) the event of default and (iii) the event of insolvency or bankruptcy.

Staff costs and related contributions. Wages, salaries, contributions to the Republic of Armenian state pension and social insurance funds, paid annual leave and sick leave, bonuses, and non-monetary benefits are accrued in the year in which the associated services are rendered by the employees of the Bank.

3 Significant Accounting Policies (Continued)

Presentation of statement of financial position in order of liquidity. The Bank does not have a clearly identifiable operating cycle and therefore does not present current and non-current assets and liabilities separately in the statement of financial position. Instead, assets and liabilities are presented in order of their liquidity. Refer to Note 26 for analysis of financial instruments by expected maturity.

Changes in presentation. Where necessary, corresponding figures have been adjusted to conform to the presentation of the current year amounts.

4 Critical Accounting Estimates, and Judgements in Applying Accounting Policies

The Bank makes estimates and assumptions that affect the amounts recognised in the financial statements, and the carrying amounts of assets and liabilities within the next financial year. Estimates and judgements are continually evaluated and are based on management's experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances. Management also makes certain judgements, apart from those involving estimations, in the process of applying the accounting policies. Judgements that have the most significant effect on the amounts recognised in the financial statements and estimates that can cause a significant adjustment to the carrying amount of assets and liabilities within the next financial year include:

ECL measurement. Measurement of ECLs is a significant estimate that involves determination of methodology, models and data inputs. Details of ECL measurement methodology are disclosed in Note 26. The following components have a major impact on credit loss allowance: definition of default, SICR, probability of default ("PD"), exposure at default ("EAD"), and loss given default ("LGD"), as well as models of macro-economic scenarios. The Bank regularly reviews and validates the models and inputs to the models to reduce any differences between expected credit loss estimates and actual credit loss experience.

Significant increase in credit risk ("SICR"). Financial instruments are allocated into appropriate stages before ECL calculations are performed. Stage allocation reflects whether the instrument constitutes part of the 'Good', 'Deteriorated' or 'Credit-Impaired' book based on approved stage allocation/transfer criteria. Stage allocation comprises a series of quantitative and qualitative criteria that are applied to identify significant increase in credit risk since initial recognition, and determine whether an instrument is to be allocated to Stage 1 or Stage 2 for up to 12 months or lifetime ECL calculation respectively.

The below listed indicators are considered to determine whether an instrument is allocated to Stage 1 or Stage 2.

- Residual average forward looking point in time PD (primary indicator)
- Watch/Worry list (backstop/secondary indicator)
- 30+DPD (backstop/secondary indicator)

Under IFRS 9, when assessing whether credit risk has significantly increased on a financial instrument since initial recognition the change in the risk of a default occurring over the expected life of the instrument is considered, particularly, a comparison is made between a Residual Average Term Forward Probability of Default (RAT FPD) projected (i) at point of origination and (ii) at the reporting date.

RAT FPD represents the average of 1 year forward PDs calculated over the residual life of the instrument. The change in RAT FPD indicates whether 'significant increase in credit risk' thresholds have been exceeded and determines whether the instrument must be allocated into Stage 1 or Stage 2, for calculation of up to 12 months or life time ECL respectively.

The quantitative comparison above is the primary stage allocation trigger. In addition, the credit risk rating (CRR) deterioration between origination date and reporting date is a further quantitative criterion for existing instruments that were originated before IRFS 9 model deployment (January 2018). This criteria is applied only in relation to the "Transition book" only, which are financial instruments that originated prior to January 2018 where origination RAT FPD needs to be approximated because economic forecasts are not available retrospectively. Where a financial instrument is originated on or after 1st January 2018 the Transitory Approach must not be used.

4 Critical Accounting Estimates, and Judgements in Applying Accounting Policies (Continued)

The 'Watch/Worry' and '30+ DPD' indicators are the secondary/qualitative measures that must be applied for stage allocation. Once the RAT FPD has been applied, and Stage 2 cases identified, the measures of Watch/Worry and 30+ DPD must be used to further identify cases which, whilst they have not met the primary test of significant credit deterioration, are nevertheless regarded as having deteriorated and must be reported in Stage 2.

All instruments that are 30+ days in arrears at the end of the reporting period must be allocated to Stage 2 in order to receive a lifetime ECL calculation, irrespective of whether or not the primary indicator has breached the significant increase in credit risk threshold, or the obligor has been placed on the Worry or Watch list.

Where primary or secondary stage allocation measures outlined above are no longer present at the reporting date, the financial instrument must be reported as Stage 1 for appropriate ECL calculation (excludes POCI assets which are not subject to the normal staging model given ECL will always be measured on a lifetime basis).

In case of Retail portfolio, Stage allocation is determined for all accounts as follows:

- Exposures 90+ Days Past Due are assigned to Stage 3
- Exposures 1+ Days Past Due are assigned to Stage 2
- Up-to-Date exposures are assigned to Stage 1

Business model assessment. The business model drives classification of financial assets. Management applied judgement in determining the level of aggregation and portfolios of financial instruments when performing the business model assessment. When assessing sales transactions, the Bank considers their historical frequency, timing and value, reasons for the sales and expectations about future sales activity. Sales transactions aimed at minimising potential losses due to credit deterioration are considered consistent with the "hold to collect" business model. Other sales before maturity, not related to credit risk management activities, are also consistent with the "hold to collect" business model, provided that they are infrequent or insignificant in value, both individually and in aggregate. The Bank assesses significance of sales transactions by comparing the value of the sales to the value of the portfolio subject to the business model assessment over the average life of the portfolio. In addition, sales of financial asset expected only in stress case scenario, or in response to an isolated event that is beyond the Bank's control, is not recurring and could not have been anticipated by the Bank, are regarded as incidental to the business model objective and do not impact the classification of the respective financial assets.

The "hold to collect and sell" business model means that assets are held to collect the cash flows, but selling is also integral to achieving the business model's objective, such as, managing liquidity needs, achieving a particular yield, or matching the duration of the financial assets to the duration of the liabilities that fund those assets.

The residual category includes those portfolios of financial assets, which are managed with the objective of realising cash flows primarily through sale, such as where a pattern of trading exists. Collecting contractual cash flow is often incidental for this business model.

4 Critical Accounting Estimates, and Judgements in Applying Accounting Policies (Continued)

Assessment whether cash flows are solely payments of principal and interest ("SPPI"). Determining whether a financial asset's cash flows are solely payments of principal and interest required judgement.

The time value of money element may be modified, for example, if a contractual interest rate is periodically reset but the frequency of that reset does not match the tenor of the debt instrument's underlying base interest rate, for example a loan pays three months interbank rate but the rate is reset every month. The effect of the modified time value of money was assessed by comparing relevant instrument's cash flows against a benchmark debt instrument with SPPI cash flows, in each period and cumulatively over the life of the instrument. The assessment was done for all reasonably possible scenarios, including reasonably possible financial stress situation that can occur in financial markets. The Bank applied a threshold of 5% to determine whether differences against a benchmark instruments are significantly different. In case of a scenario with cash flows that significantly differ from the benchmark, the assessed instrument's cash flows are not SPPI and the instrument is then carried at FVTPL.

The Bank identified and considered contractual terms that change the timing or amount of contractual cash flows. The SPPI criterion is met if a loan allows early settlement and the prepayment amount substantially represents principal and accrued interest, plus a reasonable additional compensation for the early termination of the contract. The asset's principal is the fair value at initial recognition less subsequent principal repayments, i.e. instalments net of interest determined using the effective interest method. As an exception to this principle, the standard also allows instruments with prepayment features that meet the following condition to meet SPPI: (i) the asset is originated at a premium or discount, (ii) the prepayment amount represents contractual par amount and accrued interest and a reasonable additional compensation for the early termination of the contract, and (ii) the fair value of the prepayment feature is immaterial at initial recognition.

The Banks' loans include cross-selling clauses that represent a reduction in the interest rate upon the customer entering into other contracts with the Bank or achieving certain criteria, such as maintaining a minimum turnover on current bank accounts held with the Bank. The cash flows are SPPI if such clauses merely reduce the Bank's overall profit margin on the instrument and there are no other features inconsistent with a basic lending arrangement.

The Bank considered examples in the standard and concluded that features that arise solely from legislation and that are not part of the contract, that is, if legislation changed, the features would no longer apply (such as bail in legislation in certain countries), are not relevant for assessing whether cash flows are SPPI.

The Bank's loan agreements allow adjusting interest rates in response to certain macro-economic or regulatory changes. Management applied judgement and assessed that competition in the banking sector and the practical ability of the borrowers to refinance the loans would prevent it from resetting the interest rates at an above-market level and hence cash flows were assessed as being SPPI.

The instruments that failed the SPPI test are measured at FVTPL.

Modification of financial assets. When financial assets are contractually modified (e.g. renegotiated), the Bank assesses whether the modification is substantial and should result in derecognition of the original asset and recognition of a new asset at fair value. This assessment is based primarily on qualitative factors, described in the relevant accounting policy and it requires significant judgment. In particular, the Bank applies judgment in deciding whether credit impaired renegotiated loans should be derecognised and whether the new recognised loans should be considered as credit impaired on initial recognition. The derecognition assessment depends on whether the risks and rewards, that is, the variability of expected (rather than contractual) cash flows, change as a result of such modifications. Management determined that risks and rewards did not change as a result of modifying such loans and therefore in substantially all such modifications, the loans were neither derecognised nor reclassified out of the credit-impaired stage.

4 Critical Accounting Estimates, and Judgements in Applying Accounting Policies (Continued)

Write-off policy. Financial assets (and the related impairment allowances) are normally written off, either partially or in full, when there is no realistic prospect of recovery. In circumstances where the net realisable value of any collateral has been determined and there is no reasonable expectation of further recovery, write-off may be earlier.

Write-off (or, synonymously, charge-off) is defined as the removal from the books of all or part of the value of a financial instrument, and of any related ECL allowances.

Financial instruments are to be fully written off when, after realisation of any available security, there is no realistic prospect of further recoveries. Partial write-offs may be made where appropriate.

Any portion of an instrument that is not covered by security should be written off when there is no realistic prospect of further recovery, and final write - off should occur upon receipt of proceeds following the realisation of security. Recovery activity may continue after write-off.

Unsecured retail accounts should normally be fully written off at 180 days past due. In the case of some products, e.g. credit cards, it is common for accounts to be written off at the end of the month in which they fall six months past due, or for some other technical feature of a product to give rise to a similar short excess over the 180-day ‘norm’.

In the case of secured retail facilities, any portion of the balance not covered by security should be written off when there is no realistic prospect of further recovery, and final write-off should occur upon:

- Repossession of collateral, or

- Receipt of proceeds via settlement; or

- Determination that recovery of the collateral will not be pursued; or

- Within 60 months of the default at the latest (i.e. 90 + 1825 = 1915 days past due).

Deferred income tax asset recognition. The recognised deferred tax asset represents income taxes recoverable through future deductions from taxable profits, and is recorded in the statement of financial position. Deferred income tax assets are recorded to the extent that realisation of the related tax benefit is probable. The future taxable profits and the amount of tax benefits that are probable in the future are based on a medium term business plan prepared by management and extrapolated results thereafter. The business plan is based on management expectations that are believed to be reasonable under the circumstances.

Valuation of repossessed collateral. Reposessed collateral of the Bank is stated at fair value. The valuation was based on the reports of an independent valuation company, which holds a recognised and relevant professional qualification and who has recent experience in valuation of assets of similar location and category. The basis used for the appraisal was market value. The market value of premises was assessed using the sales comparison method and the income capitalisation method.

5 Adoption of New or Revised Standards and Interpretations

Adoption of IFRS 9 "Financial Instruments". The Bank adopted IFRS 9, *Financial Instruments*, from 1 January 2018. The Bank elected not to restate comparative figures and recognised any adjustments to the carrying amounts of financial assets and liabilities in the opening retained earnings as of the date of initial application of the standard, 1 January 2018. Consequently, the revised requirements of the IFRS 7, *Financial Instruments: Disclosures*, have only been applied to the current period. The comparative period disclosures repeat those disclosures made in the prior year.

The significant new accounting policies applied in the current period are described in Note 3. Accounting policies applied prior to 1 January 2018 and applicable to the comparative information are disclosed in Note 35.

The following table reconciles the carrying amounts of each class of financial assets as previously measured in accordance with IAS 39 and the new amounts determined upon adoption of IFRS 9 on 1 January 2018.

In thousands of Armenian Drams	**Measurement category IAS 39**	**Measurement category IFRS 9**	**Carrying value per IAS 39 (closing balance at 31 December 2017)**	**Effect Remeasurement ECL**	**Carrying value per IFRS 9 (opening balance at 1 January 2018)**
Cash and cash equivalents	L&R	AC	68,935,410	(174,395)	68,761,015
Mandatory cash balances with the Central Bank of Armenia	L&R	AC	530,000	-	530,000
Investments in debt securities	FVTPL	FVTPL (mandatory)	1,117,957	-	1,117,957
Investments in debt securities	AFS	FVOCI	23,267,614	-	23,267,614
Total investments in debt securities			**24,385,571**	**-**	**24,385,571**
Investments in equity securities	AFS	FVOCI	32,132	-	32,132
Due to other banks	L&R	AC	10,566,868	(473)	10,566,395
Loans and advances to customers	L&R	AC	95,431,247	486,576	95,917,823
Other financial assets	L&R	AC	2,813,698	(44,514)	2,769,184
Total financial assets			**202,694,926**	**267,194**	**202,962,120**

(a) Cash and cash equivalents

All classes of cash and cash equivalents as disclosed in Note 7 were reclassified from loans and receivables ("L&R") measurement category under IAS 39 to AC measurement category under IFRS 9 at the adoption date of the standard.

(b) Loans and advances to banks

All classes of loans and advances to banks balances were reclassified from L&R measurement category under IAS 39 to AC measurement category under IFRS 9.

(c) Investments in debt securities

The reasons for reclassifications were as follows:

- *Investments in debt securities previously designated at FVTPL.* The Bank holds some investments in a portfolio of debt securities, which had previously been designated at FVTPL as these securities were managed on a fair value basis. As part of transition to IFRS 9, these securities are now part of an 'other' business model and so are required to be classified as at FVTPL (mandatory), instead of FVTPL (designated) as such on initial recognition.
- *Reclassification from retired categories with no change in measurement*. In addition to the above, the following debt instruments have been reclassified to new categories under IFRS 9, as their previous categories under IAS 39 were retired, with no changes to their measurement basis:
  - those previously classified as AFS and now classified as measured at FVOCI.

5 Adoption of New or Revised Standards and Interpretations (Continued)

(d) Investments in equity securities

The Bank has elected to irrevocably designate some strategic investments in a portfolio of non-trading equity securities as at FVOCI as permitted under IFRS 9. These securities were previously classified as AFS. The changes in fair value of such securities will no longer be reclassified to profit or loss when they are impaired or disposed of.

IFRS 9 does not provide an exemption to measure investments in unquoted equity securities at cost. The Bank remeasured all such investments at fair value on adoption of IFRS 9 and designated as at FVOCI.

Reconciliation of provision for impairment at 31 December 2017 and credit loss allowance at 1 January 2018. The following table reconciles the prior period's closing provision for impairment measured in accordance with incurred loss model under IAS 39 to the new credit loss allowance measured in accordance with expected loss model under IFRS 9 at 1 January 2018:

In thousand or Armenian Drams	**Provision under IAS 39 or IAS 37 at 31 December 2017**	**Effect** **Remeasurement from incurred to expected loss**	**Credit loss allowance under IFRS 9 at 1 January 2018**
Loans and receivables measurement category			
- Cash and cash equivalents	-	(174,395)	(174,395)
- Loans and advances to banks	-	(473)	(473)
- Loans and advances to customers	(10,610,810)	486,576	(10,124,234)
- Other financial assets	-	(44,514)	(44,514)
Available-for-sale financial assets	-	(46,172)	(46,172)
Loan commitments	-	(52,206)	(52,206)
Guarantees and other commitments	-	(19,006)	(19,006)

At 31 December 2017, all of the Bank's financial liabilities except for derivatives were carried at AC. The derivatives belonged to the FVTPL measurement category under IAS 39. There were no changes to the classification and measurement of financial.

The following table analyses the impact, net of tax, of transition to IFRS 9 on reserves and retained earnings as of 1 January 2018.

In thousands of Armenian Drams	**Revaluation reserve for securities at FVOCI**	**Retained earnings**	**Total**
Amounts at 31 December 2017 prior to adoption of IFRS 9			
Recognition of ECL under IFRS 9 for debt financial assets at FVOCI	(46,172)	-	(46,172)
Recognition of ECL under IFRS 9 for debt financial assets at AC and credit related commitments	-	195,982	195,982
At 1 January 2018 (under IFRS 9)	**(46,172)**	**195,982**	**149,810**

5 Adoption of New or Revised Standards and Interpretations (Continued)

Amendments to IFRS 9 - "Prepayment Features with Negative Compensation" (issued on 12 October 2017 and effective at the latest for annual periods beginning on or after 1 January 2019). The amendments enable measurement at amortised cost of certain loans and debt securities that can be prepaid at an amount below amortised cost, for example at fair value or at an amount that includes a reasonable compensation payable to the borrower equal to present value of an effect of increase in market interest rate over the remaining life of the instrument. In addition, the text added to the standard's basis for conclusion reconfirms existing guidance in IFRS 9 that modifications or exchanges of certain financial liabilities measured at amortised cost that do not result in the derecognition will result in an gain or loss in profit or loss. The Bank is therefore not be able to revise effective interest rate for the remaining life of the loan in order to avoid an impact on profit or loss upon a loan modification. The standard did not have a material impact on the Bank.

Adoption of IFRS 15 "Revenue from Contracts with Customers" (issued on 28 May 2014 and effective for the periods beginning on or after 1 January 2018) and Amendments to IFRS 15 "Revenue from Contracts with Customers" (issued on 12 April 2016 and effective for annual periods beginning on or after 1 January 2018). The Bank has adopted IFRS 15, *Revenue from Contracts with Customers*, with the date of initial application of 1 January 2018. The new standard was applied using the modified retrospective method, with the cumulative effect recognised in retained earnings on 1 January 2018. The standard introduced the core principle that revenue must be recognised when the goods or services are transferred to the customer, at the transaction price. Any bundled goods or services that are distinct must be separately recognised, and any discounts or rebates on the contract price must generally be allocated to the separate elements. When the consideration varies for any reason, minimum amounts must be recognised if they are not at significant risk of reversal. Costs incurred to secure contracts with customers have to be capitalised and amortised over the period when the benefits of the contract are consumed. The standard did not have a material impact on the Bank.

The following amended standards became effective for the Bank from 1 January 2018, but did not have any material impact on the Bank:

- Amendments to IFRS 2 "Share-based Payment" (issued on 20 June 2016 and effective for annual periods beginning on or after 1 January 2018).
- Amendments to IFRS 4 - "Applying IFRS 9 Financial Instruments with IFRS 4 Insurance Contracts" (issued on 12 September 2016 and effective, depending on the approach, for annual periods beginning on or after 1 January 2018 for entities that choose to apply temporary exemption option, or when the entity first applies IFRS 9 for entities that choose to apply the overlay approach).
- Annual Improvements to IFRSs 2014-2016 cycle – Amendments to IFRS 1 an IAS 28 (issued on 8 December 2016 and effective for annual periods beginning on or after 1 January 2018).
- IFRIC 22 "Foreign Currency Transactions and Advance Consideration" (issued on 8 December 2016 and effective for annual periods beginning on or after 1 January 2018).
- Amendments to IAS 40 – "Transfers of Investment Property" (issued on 8 December 2016 and effective for annual periods beginning on or after 1 January 2018).

6 New Accounting Pronouncements

Certain new standards and interpretations have been issued that are mandatory for the annual periods beginning on or after 1 January 2019 or later, and which the Bank has not early adopted.

IFRS 16 "Leases" (issued on 13 January 2016 and effective for annual periods beginning on or after 1 January 2019). The new standard sets out the principles for the recognition, measurement, presentation and disclosure of leases. All leases result in the lessee obtaining the right to use an asset at the start of the lease and, if lease payments are made over time, also obtaining financing. Accordingly, IFRS 16 eliminates the classification of leases as either operating leases or finance leases as is required by IAS 17 and, instead, introduces a single lessee accounting model. Lessees will be required to recognise: (a) assets and liabilities for all leases with a term of more than 12 months, unless the underlying asset is of low value; and (b) depreciation of lease assets separately from interest on lease liabilities in the income statement. IFRS 16 substantially carries forward the lessor accounting requirements in IAS 17. Accordingly, a lessor continues to classify its leases as operating leases or finance leases, and to account for those two types of leases differently. The Bank decided that it will apply the standard using the modified retrospective method, without restatement of comparatives. The Bank recognised a right of use asset of AMD 1,273,885 thousand against lease liability on 1 January 2019. A reconciliation of the operating lease commitments disclosed in Note 28 to this liability is as follows:

In thousands of Armenian Drams	**31 December 2018 / 1 January 2019**
Total future minimum lease payments for non-cancellable operating leases (Note 28)	1,465,081
- Effect of discounting to present value	(193,236)
Total lease liabilities	**1,271,845**

IFRIC 23 "Uncertainty over Income Tax Treatments" (issued on 7 June 2017 and effective for annual periods beginning on or after 1 January 2019). IAS 12 specifies how to account for current and deferred tax, but not how to reflect the effects of uncertainty. The interpretation clarifies how to apply the recognition and measurement requirements in IAS 12 when there is uncertainty over income tax treatments. An entity should determine whether to consider each uncertain tax treatment separately or together with one or more other uncertain tax treatments based on which approach better predicts the resolution of the uncertainty. An entity should assume that a taxation authority will examine amounts it has a right to examine and have full knowledge of all related information when making those examinations. If an entity concludes it is not probable that the taxation authority will accept an uncertain tax treatment, the effect of uncertainty will be reflected in determining the related taxable profit or loss, tax bases, unused tax losses, unused tax credits or tax rates, by using either the most likely amount or the expected value, depending on which method the entity expects to better predict the resolution of the uncertainty. An entity will reflect the effect of a change in facts and circumstances or of new information that affects the judgments or estimates required by the interpretation as a change in accounting estimate. Examples of changes in facts and circumstances or new information that can result in the reassessment of a judgment or estimate include, but are not limited to, examinations or actions by a taxation authority, changes in rules established by a taxation authority or the expiry of a taxation authority's right to examine or re-examine a tax treatment. The absence of agreement or disagreement by a taxation authority with a tax treatment, in isolation, is unlikely to constitute a change in facts and circumstances or new information that affects the judgments and estimates required by the Interpretation. The Bank is currently assessing the impact of the interpretation on its financial statements.

6 New Accounting Pronouncements (Continued)

IFRS 17 "Insurance Contracts"(issued on 18 May 2017 and effective for annual periods beginning on or after 1 January 2021). IFRS 17 replaces IFRS 4, which has given companies dispensation to carry on accounting for insurance contracts using existing practices. As a consequence, it was difficult for investors to compare and contrast the financial performance of otherwise similar insurance companies. IFRS 17 is a single principle-based standard to account for all types of insurance contracts, including reinsurance contracts that an insurer holds. The standard requires recognition and measurement of groups of insurance contracts at: (i) a risk-adjusted present value of the future cash flows (the fulfilment cash flows) that incorporates all of the available information about the fulfilment cash flows in a way that is consistent with observable market information; plus (if this value is a liability) or minus (if this value is an asset) (ii) an amount representing the unearned profit in the group of contracts (the contractual service margin). Insurers will be recognising the profit from a group of insurance contracts over the period they provide insurance coverage, and as they are released from risk. If a group of contracts is or becomes loss-making, an entity will be recognising the loss immediately. The Bank is currently assessing the impact of the new standard on its financial statements.

Amendments to IAS 28 “Long-term Interests in Associates and Joint Ventures” (issued on 12 October 2017 and effective for annual periods beginning on or after 1 January 2019).The amendments clarify that reporting entities should apply IFRS 9 to long-term loans, preference shares and similar instruments that form part of a net investment in an equity method investee before they can reduce such carrying value by a share of loss of the investee that exceeds the amount of investor's interest in ordinary shares. The Bank does not expect a material impact of the amendments on its financial statements.

Annual Improvements to IFRSs 2015-2017 cycle - amendments to IFRS 3, IFRS 11, IAS 12 and IAS 23 (issued on 12 December 2017 and effective for annual periods beginning on or after 1 January 2019).The narrow scope amendments impact four standards. IFRS 3 was clarified that an acquirer should remeasure its previously held interest in a joint operation when it obtains control of the business. Conversely, IFRS 11 now explicitly explains that the investor should not remeasure its previously held interest when it obtains joint control of a joint operation, similarly to the existing requirements when an associate becomes a joint venture and vice versa. The amended IAS 12 explains that an entity recognises all income tax consequences of dividends where it has recognised the transactions or events that generated the related distributable profits, e.g. in profit or loss or in other comprehensive income. It is now clear that this requirement applies in all circumstances as long as payments on financial instruments classified as equity are distributions of profits, and not only in cases when the tax consequences are a result of different tax rates for distributed and undistributed profits. The revised IAS 23 now includes explicit guidance that the borrowings obtained specifically for funding a specified asset are excluded from the pool of general borrowings costs eligible for capitalisation only until the specific asset is substantially complete. The Bank is currently assessing the impact of the amendments on its financial statements.

Amendments to IAS 19 “Plan Amendment, Curtailment or Settlement” (issued on 7 February 2018 and effective for annual periods beginning on or after 1 January 2019).The amendments specify how to determine pension expenses when changes to a defined benefit pension plan occur. When a change to a plan—an amendment, curtailment or settlement—takes place, IAS 19 requires to remeasure net defined benefit liability or asset. The amendments require to use the updated assumptions from this remeasurement to determine current service cost and net interest for the remainder of the reporting period after the change to the plan. Before the amendments, IAS 19 did not specify how to determine these expenses for the period after the change to the plan. By requiring the use of updated assumptions, the amendments are expected to provide useful information to users of financial statements. The Bank does not expect a material impact of the amendments on its financial statements.

Amendments to the Conceptual Framework for Financial Reporting (issued on 29 March 2018 and effective for annual periods beginning on or after 1 January 2020).The revised Conceptual Framework includes a new chapter on measurement; guidance on reporting financial performance; improved definitions and guidance - in particular the definition of a liability; and clarifications in important areas, such as the roles of stewardship, prudence and measurement uncertainty in financial reporting.

Unless otherwise described above, the new standards and interpretations are not expected to affect significantly the Bank’s financial statements.

7 Cash and Cash Equivalents

In thousands of Armenian Drams	**2018**	**2017**
Cash on hand	4,127,102	3,475,849
Cash balances with the CBA (other than mandatory reserve deposits)	20,968,462	31,179,930
Deposit with the CBA with original maturities of less than three months	-	3,001,110
Mandatory cash balances with CBA	542,000	530,000
Correspondent accounts and overnight placements with other banks	17,521,531	31,278,521
Less credit loss allowance	(73,180)	-
Total cash and cash equivalents	**43,085,915**	**69,465,410**

The table below discloses the credit quality of cash and cash equivalents balances based on credit risk grades at 31 December 2018. Refer to Note 26 for the description of the Bank's credit risk grading system.

In thousands of Armenian Drams	**Cash balances with the CBA, including mandatory reserves**	**Correspondent accounts and overnight placements**	**Total**
- Strong	-	17,521,531	17,521,531
- Satisfactory	21,510,462	-	21,510,462
Less credit loss allowance	(73,180)	-	(73,180)
Total cash and cash equivalents, excluding cash on hand	**21,437,282**	**17,521,531**	**38,958,813**

For the purpose of ECL measurement cash and cash equivalents balances are included in Stage 1. Refer to Note 26 for the ECL measurement approach.

The credit quality of cash and cash equivalents balances at 31 December 2017, was as follows:

In thousands of Armenian Drams	**Balances with the CBA, including mandatory reserves**	**Correspondent accounts and overnight placements**	**Total**
Neither past due nor impaired			
- Central Bank of the Republic of Armenia	34,711,040	-	34,711,040
- AA- rated	-	31,078,161	31,078,161
- A- to A+ rated	-	200,360	200,360
Total cash and cash equivalents, excluding cash on hand	**34,711,040**	**31,278,521**	**65,989,561**

The credit ratings in the above table are based on Standard & Poor's ratings.

Amounts of cash and cash equivalents are not collateralised.

Mandatory cash balances with the CBA include mandatory minimum reserve deposits calculated in accordance with regulations promulgated by the CBA at 2% to 18% (31 December 2017: 2% to 18%) from the attracted funds for AMD and foreign currency funds correspondingly, depending on currency. Withdrawal from such reserves is not restricted; however, the Bank is subject to penalties if the required minimum average balance is not periodically maintained.

At 31 December 2018 the Bank had one counterparty bank (2017: two banks) whose balance exceeded 10% of equity. The total aggregate amount of this balance was AMD 5,963,353 thousand (2017: AMD 30,897,633 thousand).

Interest rate analysis of cash and cash equivalents is disclosed in Note 26. Information on related party balances is disclosed in Note 33.

8 Financial Instruments at FVTPL

Financial Instruments at FVTPL at 31 December 2017 were as follows:

In thousands of Armenian Drams	Note	31 December 2017
Debt and other fixed-income instruments		
Armenian Government treasury bills		
- rated B+		1,117,957
Total debt securities		1,117,957
Derivative financial instruments		
Foreign exchange forward contracts		
- rated AA-	30	196,113
Total financial instruments at fair value through profit or loss		**1,314,070**

The Bank irrevocably designated the above securities, which are not part of its trading book, at fair value through profit or loss. The securities meet the criteria for classification at fair value through profit or loss.

The debt securities are not collateralised.

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

The credit ratings in the above table are based on Standard & Poor's ratings. In the cases when Standard & Poor's rating agency ratings are not available, rating agency Fitch IBCA's ratings are used by applying the rating correspondence table of Bloomberg information system.

Interest rate analysis of other securities at fair value through profit or loss is disclosed in Note 26. Information on other securities at fair value through profit or loss issued by related parties is disclosed in Note 33.

9 Loans and Advances to Banks

In thousands of Armenian Drams	2018	2017
Placements with other banks with original maturities of less than three months	17,360,444	8,682,759
Reverse sale and repurchase agreements with other banks with original maturities of less than three months	-	1,884,109
Less credit loss allowance	(452)	-
Total loans and advances to banks	**17,359,992**	**10,566,868**

The following table contains an analysis of loans and advances to banks balances by credit quality at 31 December 2018 based on credit risk grades and discloses loans and advances to banks balances by three stages for the purpose of ECL measurement. Refer to Note 26 for the description of credit risk grading system used by the Bank and the approach to ECL measurement, including the definition of default and SICR as applicable to loans and advances to banks balances. The carrying amount of loans and advances to banks balances at 31 December 2018 below also represents the Bank's maximum exposure to credit risk on these assets:

9 Loans and Advances to Banks (Continued)

In thousands of Armenian Drams	**Stage 1 (12-months ECL)**	**Total**
Placements with other banks		
- Strong	12,126,735	12,126,735
- Satisfactory	3,832,768	3,832,768
- Sub-standard	1,400,941	1,400,941
Total loans and advances to banks (gross carrying amount)	**17,360,444**	**17,360,444**
Credit loss allowance	(452)	(452)
Total loans and advances to banks (carrying amount)	**17,359,992**	**17,359,992**

Analysis by credit quality of loans and advances to banks outstanding at 31 December 2017, is as follows:

In thousands of Armenian Drams	**Placements with other banks**	**Reverse sale and repurchase agreements**	**Total**
Neither past due nor impaired			
- Local banks	1,401,206	1,884,109	3,285,315
- Rated AA-	7,268,919	-	7,268,919
- Unrated	12,634	-	12,634
Total loans and advances to banks	**8,682,759**	**1,884,109**	**10,566,868**

No loans and advances to banks are impaired or past due. The above ratings are per Standard & Poor's rating agency ratings. In the cases when Standard & Poor’s rating agency ratings are not available, rating agency Fitch IBCA's ratings are used.

As at 31 December 2018 the Bank had one bank (2017: one bank) whose balances exceeded 10% of equity. These balances as at 31 December 2018 were AMD 12,096,988 thousand (2017: 7,262,811).

The loans and advances to local banks as at 31 December 2018 have been repaid by 31 January 2019 and 31 December 2017 were repaid by 31 January 2018.

9 Loans and Advances to Banks (Continued)

The loans and advances to local banks in AMD 1,884,109 thousand are secured by Armenian government treasury bonds as at 31 December 2017. The amount excludes overcollateralization. At 31 December 2018 loans and advances to banks are not collateralised.

Refer to Note 31 for the estimated fair value of each class of amounts loans and advances to banks. Interest rate analysis of loans and advances to is disclosed in Note 26. Information on related party balances is disclosed in Note 33.

10 Investments in Debt Securities

In thousands of Armenian Drams	**2018**
Debt securities mandatorily measured at FVTPL	723,437
Debt securities at FVOCI	18,051,818
Debt securities at AC	5,008,517
Total investments in debt securities	**23,783,772**

The table below discloses investments in debt securities at 31 December 2018 by measurement categories and classes:

In thousands of Armenian Drams	**Debt securities mandatorily measured at FVTPL**	**Debt securities at FVOCI**	**Debt securities at AC**	**Total**
Armenian government bonds	723,437	18,051,818	5,011,361	23,786,616
Total investments in debt securities at 31 December 2018 (fair value or gross carrying value)	723,437	18,051,818	5,011,361	23,786,616
Credit loss allowance	-	-	(2,844)	(2,844)
Total investments in debt securities at 31 December 2018 (carrying value)	**723,437**	**18,051,818**	**5,008,517**	**23,783,772**

(a) Investments in debt securities at FVTPL

Debt securities mandatorily classified as at FVTPL by the Bank represent securities held for trading and securities in a ‘held to sell’ business model.

Debt securities at FVTPL are carried at fair value, which also reflects any credit risk related write-downs and best represents Bank’s maximum exposure to credit risk.

The debt securities at FVTPL are not collateralised.

10 Investments in Debt Securities (Continued)

(b) Investments in debt securities at FVOCI

The table below contains an analysis of the credit risk exposure of debt securities measured at FVOCI at 31 December 2018, for which an ECL allowance is recognised, based on credit risk grades. Refer to Note 26 for the description of credit risk grading system used by the Bank and the approach to ECL measurement, including the definition of default and SICR as applicable to debt securities at FVOCI:

In thousands of Armenian Drams	**Stage 1 (12-months ECL)**	**Total**
Armenian government bonds		
- Strong	18,004,473	18,004,473
Total AC gross carrying amount	18,004,473	18,004,473
Plus fair value adjustment from AC to FV	47,345	47,345
Carrying value (fair value)	18,051,818	18,051,818
Total investments in debt securities measured at FVOCI (fair value)	**18,051,818**	**18,051,818**

The debt securities at FVOCI are not collateralised.

(c) Investments in debt securities at AC

The following table contains an analysis of debt securities at AC by credit quality at 31 December 2018 based on credit risk grades and discloses the balances by three stages for the purpose of ECL measurement. Refer to Note 26 for the description of credit risk grading system used by the Bank and the approach to ECL measurement, including the definition of default and SICR as applicable to debt securities at AC. The carrying amount of debt securities at AC at 31 December 2018 below also represents the Bank's maximum exposure to credit risk on these assets:

In thousands of Armenian Drams	**Stage 1 (12-months ECL)**	**Total**
Armenian government bonds		
- Strong	5,011,361	5,011,361
Total investments in debt securities measured at AC (gross carrying amount)	**5,011,361**	**5,011,361**
Credit loss allowance	(2,844)	(2,844)
Total investments in debt securities measured at AC (carrying amount)	**5,008,517**	**5,008,517**

The debt securities at AC are not collateralised.

11 Investments in Equity Securities

In thousands of Armenian Drams	**2018**
Equity securities at FVOCI	32,093
Total investments in equity securities	**32,093**

The table below discloses investments in equity securities at 31 December 2018 by measurement categories and classes:

In thousands of Armenian Drams	**Equity securities at FVOCI**	**Total**
Corporate shares		
ACRA credit bureau	19,140	19,140
Armenian Card	12,143	12,143
SWIFT	810	810
Total investments in equity securities at 31 December 2018	**32,093**	**32,093**

Investments in equity securities at FVOCI

At 1 January 2018, the Bank designated investments disclosed in the following table as equity securities at FVOCI. In 2017, these investments were classified as AFS. Refer to Note 13. The FVOCI designation was made because the investments are expected to be held for strategic purposes rather than with a view to profit on a subsequent sale, and there are no plans to dispose of these investments in the short or medium term.

In thousands of Armenian Drams	**Fair value at 31 December 2018**	**Dividend income recognised for the year**
Investment in ACRA credit reporting bureau ordinary shares	19,140	1,067
Total investments in equity securities at FVOCI	**19,140**	**1,067**

At 31 December 2018 securities at FVOCI include equity securities with a carrying value of AMD 32,093 thousand which are not publicly traded. Due to the nature of the local financial markets, it is not possible to obtain current market value for these investments. For these investments, fair value is estimated by reference to the discounted operating cash flows of the investee, the earnings of the investee, the investee's net asset value. Refer to Note 31.

None of these strategic investments was disposed of during 2018, and there were no transfers of any cumulative gain or loss within equity relating to these investments.

12 Loans and Advances to Customers

In thousands of Armenian Drams	31 December 2018	31 December 2017
Gross carrying amount of loans and advances to customers at AC	110,754,407	106,042,057
Less credit loss allowance	(6,974,385)	(10,610,810)
Total loans and advances to customers	**103,780,022**	**95,431,247**

The carrying amount presented in the statement of financial position best represents the Bank's maximum exposure to credit risk arising from loans and advances to customers.

Gross carrying amount and credit loss allowance amount for loans and advances to customers at AC by classes at 31 December 2018 and 31 December 2017 are disclosed in the table below:

	31 December 2018			31 December 2017		
In thousands of Armenian Drams	Gross carrying amount	Credit loss allowance	Carrying amount	Gross carrying amount	Provision for loan impairment	Carrying amount
Loans to corporate customers						
Loans to large corporates	59,325,577	(3,471,281)	55,854,296	56,269,712	(7,079,898)	49,189,814
Loans to SME	27,289,324	(3,295,425)	23,993,899	27,772,189	(3,312,107)	24,460,082
Loans to individuals						
Mortgage loans	15,204,508	(93,709)	15,110,799	14,013,030	(166,789)	13,846,241
Credit cards	2,026,438	(14,917)	2,011,521	2,287,820	(20,367)	2,267,453
Construction loans	254,334	(30,927)	223,407	415,702	(7,166)	408,536
Car loans	130,036	(376)	129,660	167,540	(2,860)	164,680
Consumer loans	3,318,796	(14,205)	3,304,591	2,513,515	(9,616)	2,503,899
Other loans to retail customers	3,205,394	(53,545)	3,151,849	2,602,549	(12,007)	2,590,542
Total loans and advances to customers at AC	**110,754,407**	**(6,974,385)**	**103,780,022**	**106,042,057**	**(10,610,810)**	**95,431,247**

More detailed explanation of classes of loans to legal entities is provided below:

- Loans to large corporates – loans issued to large commercial entities under the standard terms, mainly for working capital financing;
- Loans to SME – loans issued to small and medium-sized enterprises, where the Bank defines such as average number of employees no greater than 250, prior year profit no greater than AMD 1,500,000 thousand or total assets at prior year end no greater than AMD 1,000,000 thousand.

The Bank has a right to sell or repledge securities with a fair value of AMD 3,196,301 thousand (2017: AMD 4,105,951 thousand) received under reverse sale and repurchase agreements.

12 Loans and Advances to Customers (Continued)

The following table discloses the changes in the credit loss allowance and gross carrying amount for loans and advances to customers carried at amortised cost between the beginning and the end of the reporting period.

	Credit loss allowance				Gross carrying amount			
In thousands of Armenian Drams	**Stage 1 (12-months ECL)**	**Stage 2 (lifetime ECL for SICR)**	**Stage 3 (lifetime ECL for credit im-paired)**	**Total**	**Stage 1 (12-months ECL)**	**Stage 2 (lifetime ECL for SICR)**	**Stage 3 (lifetime ECL for credit im-paired)**	**Total**
Loans to corporate customers								
At 1 January 2018	**(601,447)**	**(842,394)**	**(8,456,392)**	**(9,900,233)**	**32,852,076**	**13,401,639**	**34,620,734**	**80,874,449**
Movements with impact on credit loss allowance charge for the period:								
Transfers:								
- to lifetime (from Stage 1 to Stage 2)	203,541	(203,541)	-	-	(8,634,203)	8,634,203	-	-
- to credit-impaired (from Stage 1 and Stage 2 to Stage 3)	-	132,991	(132,991)	-	(608,587)	(2,618,153)	3,226,740	-
- to 12-months ECL (from Stage 2 and Stage 3 to Stage 1)	(25,081)	25,081	-	-	425,573	(419,184)	(6,389)	-
New originated or purchased	(917,050)	-	-	(917,050)	78,467,316	-	-	78,467,316
Derecognised during the period	253,621	106,445	1,702,700	2,062,766	(25,510,225)	(4,744,824)	(6,867,813)	(37,122,862)
Changes to ECL measurement model assumptions	365,518	323,024	(3,544,352)	(2,855,810)	(23,460,961)	(5,952,512)	(1,949,130)	(31,362,603)
Net remeasurement of ECL arising from transfer of stage	-	(64)	(3,420)	(3,484)	-	-	-	-
Other movements	40,312	(25,004)	(772,399)	(757,091)	(417,052)	417,705	(400,938)	(400,285)
Total movements with impact on credit loss allowance charge for the period	**(79,139)**	**358,932**	**(2,750,462)**	**(2,470,669)**	**20,261,861**	**(4,682,765)**	**(5,997,530)**	**9,581,566**
Movements without impact on credit loss allowance charge for the period:								
Write-offs	-	-	4,255,943	4,255,943	-	-	(4,255,943)	(4,255,943)
Foreign exchange and other movements	5,915	(2,083)	2,784	6,616	(75,741)	23,304	6,195	(46,242)
Unwinding of discount (for Stage 3)	-	-	1,342,702	1,342,702	-	-	-	-
At 31 December 2018	**(674,671)**	**(485,545)**	**(5,605,425)**	**(6,765,641)**	**53,038,196**	**8,742,178**	**24,373,456**	**86,153,830**

The movements in gross carrying amount do not include movements of the accrued interests of the loans to coroporates. As at 31 December 2018 this amount was AMD 461,071 thousand.

12 Loans and Advances to Customers (Continued)

In thousands of Armenian Drams	Credit loss allowance				Gross carrying amount			
	Stage 1 (12-months ECL)	**Stage 2 (lifetime ECL for SICR)**	**Stage 3 (lifetime ECL for credit im-paired)**	**Total**	**Stage 1 (12-months ECL)**	**Stage 2 (lifetime ECL for SICR)**	**Stage 3 (lifetime ECL for credit im-paired)**	**Total**
Loans to Individuals								
At 1 January 2018	**(36,568)**	**(5,181)**	**(182,253)**	**(224,002)**	**20,597,296**	**148,536**	**1,088,446**	**21,834,278**
Movements with impact on credit loss allowance charge for the period:								
Transfers:								
- to lifetime (from Stage 1 to Stage 2)	734	(734)	-	-	(645,257)	645,257	-	-
- to credit-impaired (from Stage 1 and Stage 2 to Stage 3)	14,298	14,505	(28,803)	-	(15,830)	(368,884)	384,714	-
- to 12-months ECL (from Stage 2 and Stage 3 to Stage 1)	(28,084)	(454)	28,538	-	284,950	(110,620)	(174,330)	-
New originated or purchased	(11,195)	-	-	(11,195)	11,436,871	-	-	11,436,871
Derecognised during the period	5,694	3,079	83,497	92,270	(3,404,558)	(15,203)	(314,777)	(3,734,538)
Changes to ECL measurement model assumptions	(11,500)	2,837	(292,976)	(301,639)	(5,036,786)	(155,569)	(216,895)	(5,409,250)
Net remeasurement of ECL arising from transfer of stage	23,474	(21,288)	(81)	2,105	-	-	-	-
Other movements	(53)	-	(151)	(204)	(30,262)	(17,428)	68,556	20,866
Total movements with impact on credit loss allowance charge for the period	**(6,632)**	**(2,055)**	**(209,976)**	**(218,663)**	**2,589,128**	**(22,447)**	**(252,732)**	**2,313,949**
Movements without impact on credit loss allowance charge for the period:								
Write-offs	-	-	233,700	233,700	-	-	(233,700)	(233,700)
Foreign exchange and other movements	748	(2)	(524)	222	12,549	69	1,370	13,988
At 31 December 2018	**(42,452)**	**(7,238)**	**(159,053)**	**(208,743)**	**23,198,973**	**126,158**	**603,384**	**23,928,515**

The movements in gross carrying amount do not include movements of the accrued interests of the loans to individuals. As at 31 December 2018 this amount was AMD 210,991 thousand.

12 Loans and Advances to Customers (Continued)

Movements in the provision for loan impairment of loans to customers during 2017 of are as follows:

In thousands of Armenian Drams	**Loans to corporate customers**	**Loans to retail customers**	**Total**
Balance at the beginning of the year	**11,300,623**	**189,686**	**11,490,309**
Net charge	13,607,384	200,543	13,807,927
Net write-offs	(13,209,954)	(171,476)	(13,381,430)
Unwinding of discount on impairment allowance and restructured loans provision adjustment	(1,476,875)	-	(1,476,875)
Effect of foreign currency translation	170,830	49	170,879
Balance at the end of the year	**10,392,008**	**218,802**	**10,610,810**

The credit loss allowance for loans and advances to customers recognised in the period is impacted by a variety of factors, details of ECL measurement are provided in Note 26. Below main movements in the table are described:

- Transfers between Stage 1, 2 and 3 due to balances experiencing significant increases (or decreases) of credit risk or becoming credit-impaired in the period, and the consequent "step up" (or "step down") between 12-month and Lifetime ECL;
- Additional allowances for new financial instruments recognised during the period, as well as releases for financial instruments derecognised in the period;
- Impact on the measurement of ECL due to changes to model assumptions, including changes in PDs, EADs and LGDs in the period, arising from update of inputs to ECL models;
- Unwinding of discount due to the passage of time because ECL is measured on a present value basis;
- Foreign exchange translations of assets denominated in foreign currencies and other movements; and
- Write-offs of allowances related to assets that were written off during the period.

The following table contains an analysis of the credit risk exposure of loans and advances to customers measured at AC and for which an ECL allowance is recognised. The carrying amount of loans and advances to customers below also represents the Bank's maximum exposure to credit risk on these loans.

12 Loans and Advances to Customers (Continued)

The credit quality of loans to corporate customers carried at amortised cost is as follows at 31 December 2018:

In thousands of Armenian Drams	Stage 1 (12-months ECL)	Stage 2 (lifetime ECL for SICR)	Stage 3 (lifetime ECL for credit impaired)	Total
Loans to large corporates				
- Strong	1,088,194	-	-	1,088,194
- Satisfactory	37,585,459	-	-	37,585,459
- Sub-standard	540,517	7,779,212	-	8,319,729
- Credit impaired	-	-	12,332,195	12,332,195
Gross carrying amount	**39,214,170**	**7,779,212**	**12,332,195**	**59,325,577**
Credit loss allowance	(489,848)	(461,570)	(2,519,863)	(3,471,281)
Carrying amount	**38,724,322**	**7,317,642**	**9,812,332**	**55,854,296**
Loans to SME				
- Strong	5,133,963	-	-	5,133,963
- Satisfactory	8,802,547	-	-	8,802,547
- Sub-standard	98,444	975,968	-	1,074,412
- Credit impaired	-	-	12,278,402	12,278,402
Gross carrying amount	**14,034,954**	**975,968**	**12,278,402**	**27,289,324**
Credit loss allowance	(184,825)	(23,976)	(3,086,624)	(3,295,425)
Carrying amount	**13,850,129**	**951,992**	**9,191,778**	**23,993,899**

The credit quality of loans to individuals carried at amortised cost is as follows at 31 December 2018:

12 Loans and Advances to Customers (Continued)

In thousands of Armenian Drams	**Stage 1 (12-months ECL)**	**Stage 2 (lifetime ECL for SICR)**	**Stage 3 (lifetime ECL for credit impaired)**	**Total**
Mortgage loans				
- Strong	14,822,540	-	-	14,822,540
- Satisfactory	-	92,859	-	92,859
- Credit impaired	-	-	289,109	289,109
Gross carrying amount	**14,822,540**	**92,859**	**289,109**	**15,204,508**
Credit loss allowance	(11,926)	(4,917)	(76,866)	(93,709)
Carrying amount	**14,810,614**	**87,942**	**212,243**	**15,110,799**
Credit cards				
- Strong	866	-	-	866
- Good	2,018,381	3,517	-	2,021,898
- Satisfactory	-	156	-	156
- Sub-standard	-	2,888	-	2,888
- Credit impaired	-	-	630	630
Gross carrying amount	**2,019,247**	**6,561**	**630**	**2,026,438**
Credit loss allowance	(13,235)	(1,127)	(555)	(14,917)
Carrying amount	**2,006,012**	**5,434**	**75**	**2,011,521**
Construction loans				
- Strong	96,783	-	-	96,783
- Satisfactory	-	196	-	196
- Credit impaired	-	-	157,355	157,355
Gross carrying amount	**96,783**	**196**	**157,355**	**254,334**
Credit loss allowance	(82)	(10)	(30,835)	(30,927)
Carrying amount	**96,701**	**186**	**126,520**	**223,407**

12 Loans and Advances to Customers (Continued)

In thousands of Armenian Drams	**Stage 1 (12-months ECL)**	**Stage 2 (lifetime ECL for SICR)**	**Stage 3 (lifetime ECL for credit impaired)**	**Total**
Car loans				
- Strong	130,036	-	-	130,036
Gross carrying amount	**130,036**	**-**	**-**	**130,036**
Credit loss allowance	(376)	-	-	(376)
Carrying amount	**129,660**	**-**	**-**	**129,660**
Consumer loans				
- Strong	3,317,286	-	-	3,317,286
- Satisfactory	-	1,122	-	1,122
- Credit impaired	-	388	-	388
Gross carrying amount	**3,317,286**	**1,510**	**-**	**3,318,796**
Credit loss allowance	(13,399)	(806)	-	(14,205)
Carrying amount	**3,303,887**	**704**	**-**	**3,304,591**
Other loans to retail customers				
- Strong	2,963,039	-	-	2,963,039
- Satisfactory	-	28,226	-	28,226
- Credit impaired	-	-	214,129	214,129
Gross carrying amount	**2,963,039**	**28,226**	**214,129**	**3,205,394**
Credit loss allowance	(2,372)	(1,058)	(50,115)	(53,545)
Carrying amount	**2,960,667**	**27,168**	**164,014**	**3,151,849**

For description of the credit risk grading used in the tables above refer to Note 26.

12 Loans and Advances to Customers (Continued)

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

In thousands of Armenian Drams	Corporate loans	Mortgage loans	Credit cards	Construc tion loans	Car loans	Consumer loans	Other loans to retail customers	Total
Neither past due nor impaired								
- Loans to large corporates	35,414,164	-	-	-	-	-	-	35,414,164
- Loans to SME	12,362,472	-	-	-	-	-	-	12,362,472
- Loans to retail customers	-	13,201,044	2,262,817	257,702	167,540	2,506,852	2,293,981	20,689,936
Total neither past due nor impaired	**47,776,636**	**13,201,044**	**2,262,817**	**257,702**	**167,540**	**2,506,852**	**2,293,981**	**68,466,572**
Past due but not impaired								
- less than 30 days overdue	820,219	85,869	19,543	953	-	1,685	18,993	947,262
- 30 to 90 days overdue	-	21,416	193	-	-	558	-	22,167
- 91 to 180 days overdue	-	1,959	5,267	-	-	20	-	7,246
- 181 to 360 days overdue	-	-	-	-	-	-	230,403	230,403
- over 360 days overdue	2,670,862	164,346	-	-	-	-	13,192	2,848,400
Total past due but not impaired	**3,491,081**	**273,590**	**25,003**	**953**	**-**	**2,263**	**262,588**	**4,055,478**
Loans individually determined to be impaired (gross)								
- less than 30 days overdue	11,869,907	38,445	-	-	-	-	-	11,908,352
- 30 to 90 days overdue	989,496	-	-	-	-	-	-	989,496
- 91 to 180 days overdue	-	-	-	157,047	-	-	-	157,047
- 181 to 360 days overdue	2,264,705	42,426	-	-	-	-	-	2,307,131
- over 360 days overdue	17,650,076	457,525	-	-	-	4,400	45,980	18,157,981
Total individually impaired loans (gross)	**32,774,184**	**538,396**	-	**157,047**	-	**4,400**	**45,980**	**33,520,007**
Less impairment provisions	(10,392,005)	(166,789)	(20,367)	(7,166)	(2,860)	(9,616)	(12,007)	(10,610,810)
Total loans and advances to customers	**73,649,896**	**13,846,241**	**2,267,453**	**408,536**	**164,680**	**2,503,899**	**2,590,542**	**95,431,247**

12 Loans and Advances to Customers (Continued)

Economic sector risk concentrations within the customer loan portfolio are as follows:

	2018		2017	
In thousands of Armenian Drams	**Amount**	**%**	**Amount**	**%**
Trade	37,635,375	34	26,774,573	25
Construction	1,609,971	1	7,292,929	7
Food and beverages	13,973,076	13	17,423,484	16
Services	14,567,521	13	10,344,031	10
Energy	3,507,858	3	3,738,103	4
Manufacturing	5,723,360	5	6,661,754	6
Agriculture	1,817,075	2	3,381,459	3
Finance	3,038,994	3	2,092,333	2
Other	4,741,671	4	6,333,235	6
Loans to individuals	24,139,506	22	22,000,156	21
Total gross loans and advances to customers	**110,754,407**	**100**	**106,042,057**	**100**

As at 31 December 2018 the Bank had three borrowers or groups of connected borrowers (2017: three), whose loan balances exceeded 10% of equity. The gross value of these loans as at 31 December 2018 was AMD 15,016,778 thousand (2017: AMD 15,629,537 thousand).

The Bank's policies regarding obtaining collateral have not significantly changed during the reporting period and there has been no significant change in the overall quality of the collateral held by the Bank since the prior period. Description of collateral held for loans to corporate customers carried at amortised cost is as follows at 31 December 2018:

In thousands of Armenian Drams	**Loans and advances to customers, carrying amount**	**Fair value of collateral assessed in the reporting period**
Borrower settlement account	253,159	-
Cash and deposits	2,363	2,363
Armenian Government treasury bills	3,038,455	3,038,455
Real estate	63,185,752	63,185,752
Motor vehicles	73,700	73,700
Equipment	1,779,912	1,779,912
Stock	2,306,039	2,306,039
Other collateral	187,975	187,975
Corporate guarantees (unrated)	2,835,869	2,835,869
Bank guarantees	1,649,845	1,649,845
No collateral or other credit enhancement – personal guarantees	4,535,126	-
Total loans and advances to corporate customers	**79,848,195**	**75,059,910**

12 Loans and Advances to Customers (Continued)

The following table provides fair value information on collateral and other credit enhancements securing loans to corporate customers, net of impairment, by types of collateral as at 31 December 2017.

In thousands of Armenian Drams	**Loans and advances to customers, carrying amount**	**Fair value of collateral assessed in the reporting period**
Loans without individual signs of impairment		
Cash and deposits	263	263
Armenian Government treasury bills	2,091,701	2,091,701
Real estate	36,695,738	36,695,738
Motor vehicles	73,700	73,700
Equipment	501,152	501,152
Stock	2,829,859	2,829,859
Other collateral	68,051	68,051
Corporate guarantees (unrated)	2,169,545	2,169,545
No collateral or other credit enhancement – personal guarantees	1,127,902	-
Total loans without individual signs of impairment	**45,557,911**	**44,430,009**
Overdue but not impaired loans		
Real estate	3,369,209	3,369,209
Motor vehicles	42,800	42,800
Stock	39,464	39,464
Total overdue but not impaired loans	**3,451,473**	**3,451,473**
Overdue and impaired loans		
Borrower settlement account	3,519,004	-
Real estate	19,177,045	19,177,045
Equipment	1,461,310	1,461,310
Stock	133,336	133,336
Other	327,787	327,787
No collateral or other credit enhancement – personal guarantees	22,030	-
Total overdue and impaired loans	**24,640,512**	**21,099,478**
Total loans and advances to corporate customers	**73,649,896**	**68,980,960**

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

Loans secured with borrower settlement accounts also have other collateral pledged to the Bank.

The Bank can not reliably estimate the fair value of personal guarantees.

Loans to retail customers

Mortgage, construction 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 2018 and 2017.

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.

12 Loans and Advances to Customers (Continued)

The outstanding contractual amounts of loans and advances to customers written off that are still subject to enforcement activity was as follows at 31 December 2018:

In thousands of Armenian Drams	**31 December 2018**
Loans to corporate customers	23,355,736
Loans to individuals	652,481
Total	**24,008,217**

The Bank's policy is to complete legal enforcement steps that were initiated even though the loans were written off as there is no reasonable expectation of recovery.

Refer to Note 31 for the estimated fair value of each class of loans and advances to customers. Interest rate analysis of loans and advances to customers is disclosed in Note 26. Information on related party balances is disclosed in Note 33.

13 Investment Securities AFS

In thousands of Armenian Drams	**2017**
Armenian Government treasury bills	
- rated B+	23,267,614
Equity instruments – Unquoted	
ACRA credit reporting	19,140
Armenian Card	12,143
SWIFT	849
Total investment securities AFS	**23,299,746**

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

Available-for-sale financial assets of the Bank are classified as per Standard & Poor's rating agency ratings. In the cases when Standard & Poor's rating agency ratings are not available, rating agency Fitch IBCA's ratings are used by applying the rating correspondence table of Bloomberg information system.

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.

At 31 December 2017 investment securities AFS include equity securities with a carrying value of AMD 32,132 thousand which are not publicly traded. Due to the nature of the local financial markets, it is not possible to obtain current market value for these investments. For these investments, fair value is estimated by reference to the discounted operating cash flows of the investee, the earnings of the investee, the investee's net asset value. Refer to Note 31.

The debt securities AFS are not collateralised.

Interest rate analysis of investment securities AFS is disclosed in Note 26.

14 Other Assets

In thousands of Armenian Drams	Note	2018	2017
Other financial assets at AC			
Receivables for letters of credit		810,656	1,855,092
Accrued commissions		233,954	504,215
Receivables from HSBC Group		344,199	-
Other		399,233	454,391
Less credit loss allowance		(8,841)	-
Total other financial assets at AC		**1,779,201**	**2,813,698**
Other financial assets at FVTPL			
Foreign exchange forward contracts	30	148,291	-
Total other financial assets at FVTPL		**148,291**	**-**
Other non-financial assets			
Prepayments		524,347	52,986
Materials and supplies		35,721	45,393
Repossessed collateral		2,362,334	1,355,278
Total non-financial assets		**2,922,402**	**1,453,657**
Total other assets		**4,849,894**	**4,267,355**

The table below contains an analysis of the credit risk exposure of other financial assets at AC. The carrying amount of other financial assets at AC at 31 December 2018 below also represents the Bank's maximum exposure to credit risk on these assets:

In thousands of Armenian Drams	Stage 1 (12-months ECL)	Total
Receivables for letters of credit		
- Satisfactory	810,656	810,656
Gross carrying amount	**810,656**	**810,656**
Credit loss allowance	(8,841)	(8,841)
Carrying amount	**801,815**	**801,815**

For the purpose of ECL measurement all other assets are included in Stage 1 and except for receivables for letters of credit the Bank did not recognise any credit loss allowance for other assets.

14 Other Assets (Continued)

No other financial assets were impaired at 31 December 2017. Movements in the provision for impairment of other financial assets during 2017 were as follows:

In thousands of Armenian Drams	Accrued commissions	Receivables for letters of credit	Receivables for other assets	Total
Provision for impairment at 1 January 2017	-	-	-	-
Provision for impairment during the year	256,903	80,768	40,260	377,931
Amounts written off during the year as uncollectible	(256,903)	(80,768)	(40,260)	(377,931)
Provision for impairment at 31 December 2017	-	-	-	-

Other financial assets are not collateralised. Settlements of receivables for letters of credit did not require the use of cash and cash equivalents and was excluded from the statement of cash flows.

Repossessed collateral represents real estate assets acquired by the Bank in settlement of overdue loans. The Bank expects to dispose of the assets in the foreseeable future.

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

Receivables for letters of credit are represented by receivables from local Armenian companies.

15 Property, Equipment and Intangible Assets

In thousands of Armenian Drams	No-te	Land and buildings	Leasehold improvements	Equipment fixtures and fittings	Intangible assets	Total
Cost at 1 January 2017		1,499,918	2,981,598	3,257,631	3,880,939	11,620,086
Accumulated depreciation		(101,394)	(2,648,801)	(2,880,840)	(2,570,726)	(8,201,761)
Carrying amount at 1 January 2017		**1,398,524**	**332,797**	**376,791**	**1,310,213**	**3,418,325**
Additions		-	14,462	157,324	479,183	650,969
Disposals/write-offs		-	(170,634)	(52,221)	(10,527)	(233,382)
Depreciation and amortisation charge	24	(101,418)	(102,054)	(171,817)	(558,021)	(933,310)
Disposals/write-offs		-	170,634	52,221	10,527	233,382
Carrying amount at 31 December 2017		**1,297,106**	**245,205**	**362,298**	**1,231,375**	**3,135,984**
Cost at 31 December 2017		1,499,918	2,825,426	3,362,734	4,349,595	12,037,673
Accumulated depreciation		(202,812)	(2,580,221)	(3,000,436)	(3,118,220)	(8,901,689)
Carrying amount at 31 December 2017		**1,297,106**	**245,205**	**362,298**	**1,231,375**	**3,135,984**
Additions		-	-	628,619	124,050	752,669
Disposals/write-offs		-	-	(103,822)	(353,225)	(457,047)
Depreciation and amortisation charge	24	(98,941)	(64,153)	(202,045)	(452,006)	(817,145)
Disposals/write-offs		-	-	103,739	-	103,739
Carrying amount at 31 December 2018		**1,198,165**	**181,052**	**788,789**	**550,194**	**2,718,200**
Cost at 31 December 2018		1,499,918	2,825,426	3,887,531	4,120,421	12,333,296
Accumulated depreciation		(301,753)	(2,644,374)	(3,098,742)	(3,570,227)	(9,615,096)
Carrying amount at 31 December 2018		**1,198,165**	**181,052**	**788,789**	**550,194**	**2,718,200**

15 Property, Equipment and Intangible Assets (Continued)

At 31 December 2018 land and buildings were revalued based on the results of an independent appraisal performed by an independent valuator. The resulting fair values were not materially different from the carrying value of the land and buildings and no revaluation impact was recorded in the financial statements.

The carrying value of land and buildings as of 31 December 2018, if the land and buildings would not have been revalued would be AMD 952,648 thousand (31 December 2017: AMD 1,024,345 thousand).

16 Due to Other Banks

In thousands of Armenian Drams	**2018**	**2017**
Correspondent accounts and overnight placements of other banks	381,428	618,931
Members of HSBC Group	-	5,816,459
Loans received from the CBA	-	375,588
Financial institutions	39,960	73,272
Total due to other banks	**421,388**	**6,884,250**

As at 31 December 2018 the Bank had no bank (31 December 2017: one bank), whose balances exceeded 10% of equity. The gross value of these balances as at 31 December 2018 were nil (2017: AMD 5,816,459 thousand).

Refer to Note 31 for the disclosure of the fair value of each class of amounts due to other banks. Interest rate analysis of due to other banks is disclosed in Note 26. Information on related party balances is disclosed in Note 33.

17 Current Accounts and Deposits from Customers

In thousands of Armenian Drams	**2018**	**2017**
Current accounts		
- Retail	46,475,636	40,918,548
- Corporate	32,645,016	34,508,917
Term deposits		
- Retail	63,645,154	72,753,233
- Corporate	10,179,813	10,392,097
- Other	6,736	6,696
Total current accounts and deposits from customers	**152,952,355**	**158,579,491**

As at 31 December 2018, the Bank maintained customer deposit balances of AMD 255,369 thousand (31 December 2017: AMD 1,024,402 thousand) that served as collateral for loans and unrecognised credit instruments granted by the Bank.

As at 31 December 2018, the Bank had two customers (31 December 2017: two customers), whose balances exceeded 10% of equity. These balances as at 31 December 2018 were AMD 13,170,753 thousand (2017: AMD 18,176,949 thousand).

Refer to Note 31 for the disclosure of the fair value of each class of current accounts and deposits from customers. Interest rate analysis of current accounts and deposits from customers is disclosed in Note 26. Information on related party balances is disclosed in Note 33.

18 Other Liabilities

Other liabilities comprise the following:

In thousands of Armenian Drams	Note	2018	2017
Other financial liabilities at AC			
Payables for letters of credit		810,656	1,855,092
Payables to HSBC Group		1,053,420	691,475
Accrued expenses		69,092	117,642
Credit loss allowance		72,943	-
Other		140,647	333,396
Total other financial liabilities at AC		**2,146,758**	**2,997,605**
Other financial liabilities mandatorily measured at FVTPL			
Foreign exchange forward contracts	30	34,015	6,489
Total other financial liabilities at FVTPL		**34,015**	**6,489**
Other non-financial liabilities			
Accrued employee benefit costs		800,257	833,540
Contract liability - deferred income		194,082	301,769
Payable to Deposit Guarantee Fund		63,489	59,742
Prepayments received		501,430	-
Total non-financial liabilities		**1,559,258**	**1,195,051**
Total other liabilities		**3,740,031**	**4,199,145**

Refer to Note 28 for analysis of exposure from financial guarantees and loan commitments by credit risk grades.

Refer to Note 31 for disclosure of the fair value of each class of other financial liabilities.

19 Share Capital

Issued capital

The authorised, issued and outstanding share capital comprises 609,400 ordinary shares of AMD 30.25 thousand each (2017: 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.

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 2018 (2017: nil).

20 Other Comprehensive Income Recognised in Each Component of Equity

An analysis of other comprehensive income by item for each component of equity is as follows:

In thousands of Armenian Drams	**Revaluation reserve for AFS securities**	**Total equity**
Year ended 31 December 2017	**257,091**	**257,091**
AFS investments:		
- Gains less losses arising during the year	(82,002)	**(82,002)**
Total other comprehensive income	**175,089**	**175,089**

In thousands of Armenian Drams	**Revaluation reserve for AFS securities**	**Revaluation reserve for investment securities at FVOCI**	**Total equity**
Year ended 31 December 2018	**175,089**	**-**	**175,089**
Securities as FVOCI:			
- Gains less losses arising during the year	-	(123,036)	**(123,036)**
Total other comprehensive income	**175,089**	**(123,036)**	**52,053**

21 Interest Income and Expense

In thousands of Armenian Drams	**2018**	**2017**
Interest income calculated using the effective interest method		
Loans and advances to customers at AC	8,612,984	10,165,117
Debt securities at FVOCI	1,094,684	-
Debt securities at AC	252,813	-
Debt securities AFS	-	1,801,934
Loans and advances to banks at AC	883,009	568,598
Total interest income calculated using the effective interest method	**10,843,490**	**12,535,649**
Other similar income		
Debt securities at FVTPL	101,337	96,070
Cash and cash equivalents	161,266	324,007
Total other similar income	**262,603**	**420,077**
Total interest income	**11,106,093**	**12,955,726**
Interest and similar expense		
Current accounts and deposits from customers	3,523,285	4,575,930
Due to other banks	82,053	176,477
Total interest and expense	**3,605,338**	**4,752,407**
Net interest income	**7,500,755**	**8,203,319**

21 Interest Income and Expense (Continued)

Included within loans to customers line under interest income for the year ended 31 December 2018 is a total of AMD 1,342,702 thousand (2017: AMD 2,080,876 thousand) accrued on impaired financial assets

22 Fee and Commission Income and Expense

In thousands of Armenian Drams	2018	2017
Fee and commission income		
Fee and commission income not relating to financial instruments at FVTPL:		
- Credit facilities	1,358,412	2,198,901
- Credit cards	637,830	429,074
- Letters of credit and guarantees (Note 28)	305,484	490,175
- Remittances	292,508	320,911
- Account services	93,668	111,906
- ATM services	16,829	19,687
- Insurance agency	7,993	8,471
- Other	38,245	43,424
Total fee and commission income	**2,750,969**	**3,622,549**
Fee and commission expense		
Fee and commission expense not relating to financial instruments at FVTPL		
- Card transactions fees	378,228	343,926
- Settlement transactions	96,279	70,212
- Loans and borrowings	-	10,913
- Other	32,513	40,951
Total fee and commission expense	**507,020**	**466,002**
Net fee and commission income	**2,243,949**	**3,156,547**

23 Gains Less Losses from Trading in Foreign Currencies

In thousands of Armenian Drams	2018	2017
Gain on foreign exchange transactions	742,042	1,110,776
Net loss from revaluation of financial assets and liabilities	(24,694)	(66,227)
Total gains less losses from trading in foreign currencies	**717,348**	**1,044,549**

24 Other General Administrative Expenses

In thousands of Armenian Drams	**Note**	**2018**	**2017**
HSBC Group IT support costs and other charges		1,618,819	1,552,834
Depreciation and amortisation of property, equipment and intangibles	15	817,145	933,310
Rent of property		482,480	536,091
Payments to Deposit Guarantee Fund		247,587	-
Communication and information services		140,918	140,527
Advertising and marketing		116,602	111,348
Security		111,841	105,797
Training costs		87,745	50,179
Professional services		79,388	84,146
IT related costs		74,904	69,346
Travel and entertainment expenses		65,707	74,235
Insurance		64,918	68,652
Repair and maintenance		62,729	67,689
Utilities		58,559	73,842
Office supplies		39,461	23,318
Currency shipment charges		24,131	27,848
Charity and sponsorship		20,828	23,442
Other		265,834	212,545
Total other general administrative expenses		**4,379,596**	**4,155,149**

25 Income Taxes

(a) Components of income tax expense/(credit)

Income tax expense/ (credit) recorded in profit or loss for the year comprises the following:

In thousands of Armenian Drams	**2018**	**2017**
Current tax	-	(149,756)
Deferred tax	123,385	(2,031,145)
Income tax expense/(credit) for the year	**123,385**	**(2,180,901)**

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

The income tax rate applicable to the majority of the Bank's 2018 income is 20% (2017: 20%). A reconciliation between the expected and the actual taxation charge is provided below.

In thousands of Armenian Drams	**2018**	**2017**
Profit/(Loss) before tax	**678,538**	**(10,121,484)**
Theoretical tax charge/(credit) at statutory rate (2018: 20%; 2017: 20%)	135,708	(2,024,297)
Tax effect of items which are not deductible or assessable for taxation purposes:		
- (Non-deductible expenses)/income exempt from taxation, net	(12,323)	(6,848)
Over provided in prior years	-	(149,756)
Income tax expense/(credit) for the year	**123,385**	**(2,180,901)**

25 Income Taxes (Continued)

(c) Tax loss carry forwards

According to Armenian tax legislation the maximum term for recovery of tax losses is 5 years. Based on the above, tax loss carry forwards expire as follows:

In thousands of Armenian Drams	2018	2017
Tax loss carry-forwards expiring by the end of:		
- 31 December 2021	1,133,961	1,373,794
- 31 December 2022	180,000	180,000
Total tax loss carry forwards	**1,313,961**	**1,553,794**

(d) Deferred taxes analysed by type of temporary difference

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

In thousands of Armenian Drams	1 January 2018	Credited/ (charged) to profit or loss	Credited/(charged) to other compre-hensive income	31 December 2018
Tax effect of deductible/(taxable) temporary differences and tax loss carry forwards				
Cash and cash equivalents	62,557	(43,486)	-	19,071
Fair valuation of securities at FVTPL	55,683	(44,244)	-	11,439
Fair valuation of securities at FVOCI	43,772	-	(30,761)	13,011
Securities at AC	-	(569)	-	(569)
Loans and advances to banks	17,366	17,205	-	34,571
Loans and advances to customers	558,783	(88,315)	-	470,468
Property and equipment	(77,816)	(32,328)		(110,144)
Other assets	18,178	11,434	-	29,612
Other liabilities	(276,946)	63,854	-	(213,092)
Tax loss carry forwards	(1,553,794)	239,834	-	(1,313,960)
Net deferred tax asset	**(1,152,217)**	**123,385**	**(30,761)**	**(1,059,593)**

In thousands of Armenian Drams	1 January 2017	Credited/ (charged) to profit or loss	Credited/(charged) to other compre-hensive income	31 December 2017
Tax effect of deductible/(taxable) temporary differences and tax loss carry forwards				
Cash and cash equivalents	26,476	36,081	-	62,557
Fair valuation of securities at FVTPL	64,086	(8,403)	-	55,683
Fair valuation of securities AFS	64,273	-	(20,501)	43,772
Loans and advances to banks	2,832	14,534	-	17,366
Loans and advances to customers	2,427,214	(1,868,431)	-	558,783
Property and equipment	(73,863)	(3,953)	-	(77,816)
Other assets	55,376	(37,198)	-	18,178
Other liabilities	(264,965)	(11,981)	-	(276,946)
Tax loss carry forwards	(1,402,000)	(151,794)	-	(1,553,794)
Net deferred tax asset	**899,429**	**(2,031,145)**	**(20,501)**	**(1,152,217)**

25 Income Taxes (Continued)

(e) Current and deferred tax effects relating to each component of other comprehensive income

Current and deferred tax effects relating to each component of other comprehensive income are as follows:

In thousands of Armenian Drams	2018 Before-tax amount	2018 Income tax (expense)/ benefit	2018 Net-of-tax amount	2017 Before-tax amount	2017 Income tax (expense)/ benefit	2017 Net-of-tax amount
Debt securities at FVOCI:						
- Gains arising during the year	(153,797)	30,761	(123,036)	-	-	-
AFS investments						
- Gains arising during the year	-	-	-	(102,503)	20,501	(82,002)
Other comprehensive income	**(153,797)**	**30,761**	**(123,036)**	**(102,503)**	**20,501**	**(82,002)**

26 Financial Risk Management

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

Credit risk. The Bank exposes itself to credit risk, which is the risk that one party to a financial instrument will cause a financial loss for the other party by failing to meet an obligation.

Exposure to credit risk arises as a result of the Bank's lending and other transactions with counterparties, giving rise to financial assets and off-balance sheet credit-related commitments.

The Bank's maximum exposure to credit risk is reflected in the carrying amounts of financial assets in the statement of financial position. For financial guarantees issued, commitments to extend credit, undrawn credit lines and export/import letters of credit, the maximum exposure to credit risk is the amount of the commitment.

Credit risk management. Credit risk is the single largest risk for the Bank's business; management therefore carefully manages its exposure to credit risk.

The estimation of credit risk for risk management purposes is complex and involves the use of models, as the risk varies depending on market conditions, expected cash flows and the passage of time. The assessment of credit risk for a portfolio of assets entails further estimations of the likelihood of defaults occurring, the associated loss ratios and default correlations between counterparties.

Limits. The Bank structures the levels of credit risk it undertakes by placing limits on the amount of risk accepted in relation to one borrower, or groups of borrowers, and to geographical and industry segments. Limits on the level of credit risk by product and industry sector are approved regularly by management. Such risks are monitored on a revolving basis and are subject to an annual, or more frequent, review.

Loan applications originating with the relevant client relationship managers are passed on to the relevant credit approving authorities for the approval of the credit limit. Exposure to credit risk is also managed, in part, by obtaining collateral as well as corporate and personal guarantees. In order to monitor exposure to credit risk, regular reports are produced by Finance, Risk and Commercial Banking departments based on a structured analysis focusing on the customer's business and financial performance. Any significant interaction with customers with deteriorating creditworthiness are reported to and reviewed by Risk Management and Commercial Banking senior executives, Regional Risk teams, Country Risk Management Meetings and any other not formal committees created for the management of such accounts.

26 Financial Risk Management (Continued)

Credit risk grading system. For measuring credit risk and grading financial instruments by the amount of credit risk, the Bank applies Internal Risk-Based (IRB) rating system as disclosed in the table below:

Master scale credit risk grade	Sovereign debt securities and bills - External credit rating	Other debt securities and bills - External credit rating	Wholesale lending and derivatives-Internal credit rating	Wholesale lending and derivatives-12-month Basel probability of default %	Retail lending-Internal credit rating	Retail lending-12 month probability weighted PD %
Strong	BBB and above	A- and above	CRR 1 to CRR 2	0 – 0.169	Band 1 and 2	0.000 - 0.500
Good	BBB- to BB	BBB+ to BBB-	CRR 3	0.170 – 0.740	Band 3	0.501 - 1.500
Satisfactory	BB- to B and unrated	BB+ to B and unrated	CRR 4 to CRR 5	0.741 – 4.914	Band 4 and 5	1.501 - 20.000
Sub-standard	B- to C	B- to C	CRR 6 to CRR 8	4.915 – 99.999	Band 6	20.001 - 99.999
Credit impaired	Default	Default	CRR 9 to CRR 10	100	Band 7	100

Each master scale credit risk grade is assigned a specific degree of creditworthiness:

- ‘Strong’ exposures demonstrate a strong capacity to meet financial commitments, with negligible or low probability of default and/or low levels of expected loss;
- ‘Good’ exposures require closer monitoring and demonstrate a good capacity to meet financial commitments, with low default risk;
- ‘Satisfactory’ exposures require closer monitoring and demonstrate an average-to-fair capacity to meet financial commitments, with moderate default risk;
- ‘Sub-standard’ exposures require varying degrees of special attention and default risk is of greater concern;
- ‘Credit-impaired’ exposures have been assessed as described in Note 3.

Expected credit loss (ECL) measurement. *ECL* is a probability-weighted estimate of the present value of future cash shortfalls (i.e., the weighted average of credit losses, with the respective risks of default occurring in a given time period used as weights). An ECL measurement is unbiased and is determined by evaluating a range of possible outcomes. ECL measurement is based on four components used by the Bank: Probability of Default (“PD”), Exposure at Default (“EAD”), Loss Given Default (“LGD”) and Discount Rate.

EAD is an estimate of exposure at a future default date, taking into account expected changes in the exposure after the reporting period, including repayments of principal and interest, and expected drawdowns on committed facilities. The EAD on credit related commitments is estimated using Credit Conversion Factor (“CCF”). CCF is a coefficient that shows the probability of conversion of the committed amounts to an on-balance sheet exposure within a defined period. PD is an estimate of the likelihood of default to occur over a given time period. LGD is an estimate of the loss arising on default. It is based on the difference between the contractual cash flows due and those that the lender would expect to receive, including from any collateral. It is usually expressed as a percentage of the EAD. The expected losses are discounted to present value at the end of the reporting period. The discount rate represents the effective interest rate (“EIR”) for the financial instrument or an approximation thereof.

Expected credit losses are modelled over instrument’s lifetime *period.* The lifetime *period* is equal to the remaining contractual period to maturity of debt instruments, adjusted for expected prepayments, if any. For loan commitments and financial guarantee contracts, it is the contractual period over which an entity has a present contractual obligation to extend credit. As a matter of exception from determining the lifetime exposure based on contractual maturity, for credit cards issued to individuals, the lifetime exposure is measured over a period that is based on expected life of the credit card contracts, based on internal statistics.

26 Financial Risk Management (Continued)

Management models *Lifetime ECL,* that is, losses that result from all possible default events over the remaining lifetime period of the financial instrument. The *12-month ECL,* represents a portion of lifetime ECLs that result from default events on a financial instrument that are possible within 12 months after the reporting period, or remaining *lifetime period* of the financial instrument if it is less than a year.

The ECLs that are estimated by management for the purposes of these financial statements are point-in-time estimates, rather than through-the-cycle estimates that are commonly used for regulatory purposes. The estimates consider *forward looking information,* that is, ECLs reflect probability weighted development of key macroeconomic variables that have an impact on credit risk.

The ECL modelling does not differ for POCI financial assets, except that (a) gross carrying value and discount rate are based on cash flows that were recoverable at initial recognition of the asset, rather than based on contractual cash flows, and (b) the ECL is always a lifetime ECL. POCI assets are financial assets that are credit-impaired upon initial recognition, such as impaired loans acquired in a past business combination.

For purposes of measuring PD, the Bank defines default as a situation when the exposure meets one or more of the following criteria:

- Deterioration in the financial condition or outlook of the borrower such that its ability to repay is considered doubtful;
- Known cash flow difficulties experienced by the borrower;
- Contractual payments of either principal or interest being past due for more than 90 days;
- The probability that the borrower will enter bankruptcy or other forms of creditor protection;
- A significant concession granted to the borrower for economic or legal reasons relating to the borrower's
- The Bank has sold the borrower's debt or its portion at a loss due to credit deterioration;
- The borrower meets the unlikeliness-to-pay criteria listed below:
  - the bank was forced to restructure the debt;
  - the borrower is deceased;
  - the borrower is insolvent;
  - the borrower is in breach of financial covenant(s);

For purposes of disclosure, the Bank fully aligned the definition of default with the definition of credit-impaired assets. The default definition stated above is applied to all types of financial assets of the Bank.

An instrument is considered to no longer be in default (i.e. to have cured) when it no longer meets any of the default criteria for a consecutive period of twelve months. This period of twelve months has been determined based on an analysis that considers the likelihood of a financial instrument returning to default status after curing by using different possible definitions of cures.

Financial instruments are allocated into appropriate stages before ECL calculations are performed. Stage allocation reflects whether the instrument constitutes part of the 'Good', 'Deteriorated' or 'Credit-Impaired' book based on Global Wholesale Credit Risk's approved stage allocation/transfer criteria. Stage allocation comprises a series of quantitative and qualitative criteria that are applied to identify significant increase in credit risk since initial recognition, and determine whether an instrument is to be allocated to Stage 1 or Stage 2 for up to 12 months or lifetime ECL calculation respectively.

The below listed indicators are considered to determine whether an instrument is allocated to Stage 1 or Stage 2.

- Residual average forward looking point in time PD (primary indicator)
- Watch/Worry list (backstop/secondary indicator)
- 30+ days past due (backstop/secondary indicator)

26 Financial Risk Management (Continued)

For loans to Individuals:

Stage allocation is determined for all accounts, particularly,

- Exposures 90+ Days Past Due are assigned to Stage 3
- Exposures 1+ Days Past Due are assigned to Stage 2
- Up-to-Date exposures are assigned to Stage 1

The Bank has two approaches for ECL measurement: (i) assessment on an individual basis; (ii) assessment on a portfolio basis: internal ratings are estimated on an individual basis but the same credit risk parameters (e.g. PD, LGD) will be applied during the process of ECL calculations for the same credit risk ratings and homogeneous segments of the loan portfolio. The Bank performs an assessment on an individual basis for defaulted corporate portfolio/accounts only.

ECL assessment on an individual basis is measured on a lifetime ECL basis using a Discounted Cash Flow ("DCF") methodology. For Stage 3 credit-impaired financial instruments, an event must have occurred for an instrument to be identified as being in default/impaired (i.e. CRR 9 or 10). Under IFRS 9, a financial instrument or group of financial instruments are credit-impaired and Stage 3 individual ECL allowances are to be determined if there is evidence of impairment as a result of one or more events that occurred after initial recognition of the instrument, and this event(s) has a detrimental effect on the estimated future cash flows of that instrument and the contractual cash flows are not anticipated to be collected as originally expected. Expert judgements are regularly tested in order to decrease the difference between estimates and actual losses.

When assessment is performed on a portfolio basis, the Bank determines the staging of the exposures and measures the loss allowance on a collective basis. The Bank analyses its exposures by segments determined on the basis of shared credit risk characteristics, such that exposures within a group have homogeneous or similar risks. The key shared credit characteristics considered are: type of customer (such as wholesale or retail), product type, credit risk rating, term to maturity. The different segments also reflect differences in credit risk parameters such as PD and LGD. The appropriateness of groupings is monitored and reviewed on a periodic basis by the Risk Management Department and Regional Model team.

In general, ECL is the sum of the multiplications of the following credit risk parameters: EAD, PD and LGD, that are defined as explained above, and discounted to present value using the instrument's effective interest rate. The ECL is determined by predicting credit risk parameters (EAD, PD and LGD) for each future year during the lifetime period for each individual exposure or collective segment. These three components are multiplied together and adjusted for the likelihood of survival (i.e. the exposure has been repaid or defaulted in an earlier month). This effectively calculates an ECL for each future period, that is then discounted back to the reporting date and summed up.

The key principles of calculating the credit risk parameters. The EADs are determined based on the expected payment profile, that varies by product type. EAD is based on the contractual repayments owed by the borrower over a 12-month or lifetime basis for amortising products and bullet repayment loans. This will also be adjusted for any expected overpayments made by a borrower. For revolving products, the EAD is predicted by taking the current drawn balance and adding a CCF that accounts for the expected drawdown of the remaining limit by the time of default. These assumptions vary by product type, current limit utilisation and other borrower-specific behavioural characteristics.

26 Financial Risk Management (Continued)

Two types of PDs are used for calculating ECLs: 12-month and lifetime PD. An assessment of a 12-month PD is based on the latest available historic default data and adjusted for supportable forward-looking information when appropriate. Lifetime PDs represent the estimated probability of a default occurring over the remaining life of the financial instrument and it is a sum of the 12 months PDs over the life of the instrument. The Bank uses different statistical approaches depending on the segment and product type to calculated lifetime PDs, such as the extrapolation of 12-month PDs based on migration matrixes, developing lifetime PD curves based on the historical default data, hazard rate approach or other.

Simplified approach is used to calculate ECL for Stage 1 and Stage 2. Under this approach the risk drivers – PDs and LGDs are derived by shifting the main site PDs and LGDs by the scalar reflecting the relationship of the site with one of the main HSBC Europe sites (UK and France). Scalar denotes the magnitude of the relationship existing between the risk parameters of the target portfolio and proxy country.

The scalar is used to shift the main site cumulative probability of default (“CPD”) curve and derive the international site CPD and is typically around 1. The PD term structure of the main site is available for each CRR grade, therefore each of the customers will have the CRR at reporting date linked to the CDP curve for that particular CRR.

The proxy country to be used for Armenia Portfolio is France.

ECL measurement for financial guarantees and loan commitments. The ECL measurement for these instruments includes the same steps as described above for on-balance sheet exposures and differs with respect to EAD calculation. The EAD is a product of credit conversion factor (“CCF”) and amount of the commitment. CCF for undrawn credit lines of corporate customers, credit cards issued to individuals and for financial guarantees is defined based on statistical analysis of past exposures at default. CCF for overdrafts is defined as 100% since the limits can be used by the customers at any time.

Forward-looking information incorporated in the ECL models. The Bank in general applies three forward-looking global economic scenarios determined with reference to external forecast distributions representative of the Bank’s view of forecast economic conditions, the consensus economic scenario approach. This approach is considered sufficient to calculate unbiased expected loss in most economic environments. They represent a most likely outcome (the Central scenario) and two, less likely, outer scenarios referred to as the Upside and Downside scenarios. The Central scenario is the basis for the annual operating planning process and, with regulatory modifications, will also be used in enterprise-wide stress tests. The Upside and Downside scenarios are constructed following a standard process supported by a scenario narrative reflecting the Bank’s current top and emerging risks and by consulting external and internal subject matter experts. The relationship between the outer scenarios and Central scenario will generally be fixed with the Central scenario being assigned a weighting of 80% and the Upside and Downside scenarios 10% each, with the difference between the Central and outer scenarios in terms of economic severity being informed by the spread of external forecast distributions among professional industry forecasts. The outer scenarios are economically plausible, internally consistent states of the world and will not necessarily be as severe as scenarios used in stress testing. The period of forecasts is five years for the Central scenario. Upside and Downside scenarios use distributional forecasts for the first two years, after which they converge to the Central forecasts. The spread between the Central and outer scenarios is grounded on consensus distributions of projected gross domestic product of the following economies: UK, France, Hong Kong, mainland China, US and Canada. The economic factors include, but are not limited to, gross domestic product, unemployment, interest rates, inflation and commercial property prices across all the countries and territories in which HSBC operates.

26 Financial Risk Management (Continued)

In general, the consequences of the assessment of credit risk and the resulting ECL outputs will be probability-weighted using the standard probability weights. This probability weighting may be applied directly or the effect of the probability weighting determined on a periodic basis, at least annually, and then applied as an adjustment to the outcomes resulting from the central economic forecast. The central economic forecast is updated quarterly.

The Bank recognises that the consensus economic scenario approach using three scenarios will be insufficient in certain economic environments. Additional analysis may be requested at management's discretion, including the production of extra scenarios. If conditions warrant, this could result in alternative scenarios and probability weightings being applied in arriving at the ECL.

The Bank regularly reviews its methodology and assumptions to reduce any difference between the estimates and the actual loss of credit. Such backtesting is performed at least once a year.

The results of backtesting the ECL measurement methodology are communicated to Bank's Management and further steps for tuning models and assumptions are defined after discussions between authorised persons.

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.

In thousands of Armenian Drams	**Stage 1 (12-months ECL)**	**Stage 2 (lifetime ECL for SICR)**	**Stage 3 (lifetime ECL for credit impaired)**	**Total**
Cash and cash equivalents, excluding cash on hand	**38,958,813**	**-**	**-**	**38,958,813**
Debt securities at FVOCI	**18,051,818**	**-**	**-**	**18,051,818**
Debt securities at AC	**5,008,517**	**-**	**-**	**5,008,517**
Loans and advances to banks	**17,359,992**	**-**	**-**	**17,359,992**
Loans and advances to customers				
- Strong	27,514,148	-	-	27,514,148
- Good	2,008,257	2,904	-	2,011,161
- Satisfactory	45,728,177	116,423	-	45,844,600
- Sub-standard	631,410	8,271,741	-	8,903,442
- Credit impaired	-	-	19,506,962	19,506,671
Other financial assets	**1,779,201**	**-**	**-**	**1,779,201**
Credit related commitments and guarantees	**30,322,018**	**2,425,597**	**174**	**32,747,789**
Debt securities at FVTPL	**723,437**	**-**	**-**	**723,437**
Derivative financial assets	**148,291**	**-**	**-**	**148,291**
Total maximum exposure	**188,234,079**	**10,816,665**	**19,507,136**	**218,557,880**

The maximum exposure to credit risk from financial assets as at 31 December 2017 is as follows:

In thousands of Armenian Drams	**2017**
ASSETS	
Cash and cash equivalents, excluding cash on hand	65,989,561
Financial instruments at fair value through profit or loss	1,314,070
Available-for-sale debt assets	23,267,614
Loans and advances to banks	10,566,868
Loans and advances to customers	95,431,247
Other financial assets	2,813,698
Credit related commitments and guarantees	27,634,355
Total maximum exposure	**227,017,413**

26 Financial Risk Management (Continued)

Market risk. The Bank takes on exposure to market risks. Market risks arise from open positions in (a) currency, (b) interest rates and (c) equity products, all of which are exposed to general and specific market movements. 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.

Currency risk. In respect of currency risk, management sets limits on the level of exposure by currency and in total for both overnight and intra-day positions, which are monitored daily.

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

In thousands of Armenian Drams	**AMD**	**USD**	**EUR**	**Other currencies**	**Total**
ASSETS					
Cash and cash equivalents	23,885,346	8,839,865	5,228,644	5,132,060	43,085,915
Investments in debt securities	23,783,772	-	-	-	23,783,772
Investments in equity securities	31,283	-	810	-	32,093
Loans and advances to banks	4,402,506	12,108,789	838,816	9,881	17,359,992
Loans and advances to customers	36,165,504	61,663,929	5,922,597	27,992	103,780,022
Other financial assets	627,445	722,788	566,374	10,885	1,927,492
Total financial assets	**88,895,856**	**83,335,371**	**12,557,241**	**5,180,818**	**189,969,286**
LIABILITIES					
Due to other banks	421,388	-	-	-	421,388
Current accounts and deposits from customers	45,733,876	89,092,731	16,156,134	1,969,614	152,952,355
Other financial liabilities	491,989	573,096	561,724	553,964	2,180,773
Total financial liabilities	**46,647,253**	**89,665,827**	**16,717,858**	**2,523,578**	**155,554,516**
Net position as at 31 December 2018	**42,248,603**	**(6,330,456)**	**(4,160,617)**	**2,657,240**	**34,414,770**
The effect of derivatives held for risk management and regular way currency contracts	**(8,153,014)**	**6,280,584**	**4,152,375**	**(2,279,945)**	**-**

26 Financial Risk Management (Continued)

The table below summarises the Bank's exposure to foreign currency exchange rate risk as at 31 December 2017:

In thousands of Armenian Drams	AMD	USD	EUR	Other currencies	Total
ASSETS					
Cash and cash equivalents	31,627,408	30,333,957	5,621,852	1,882,193	69,465,410
Financial instruments at fair value through profit or loss	1,118,124	195,562	384	-	1,314,070
Available-for-sale financial assets	23,298,898	-	848	-	23,299,746
Loans and advances to banks	3,285,315	7,266,319	8,685	6,549	10,566,868
Loans and advances to customers	26,795,911	56,770,231	11,865,105	-	95,431,247
Other financial assets	410,539	1,527,128	876,031	-	2,813,698
Total financial assets	**86,536,195**	**96,093,197**	**18,372,905**	**1,888,742**	**202,891,039**
LIABILITIES					
Due to other banks	1,067,791	-	5,816,459	-	6,884,250
Current accounts and deposits from customers	42,918,181	102,414,762	11,739,391	1,507,157	158,579,491
Other financial liabilities	803,081	1,054,642	909,962	236,409	3,004,094
Total financial liabilities	**44,789,053**	**103,469,404**	**18,465,812**	**1,743,566**	**168,467,835**
Net position as at 31 December 2017	**41,747,142**	**(7,376,207)**	**(92,907)**	**145,176**	**34,423,204**
The effect of derivatives held for risk management and regular way currency contracts	**(7,884,390)**	**7,922,350**	**5**	**(37,965)**	**-**

Derivatives presented above are monetary financial assets or monetary financial liabilities, but are presented separately in order to show the Bank's gross exposure.

Amounts disclosed in respect of derivatives represent the fair value, at the end of the reporting period, of the respective currency that the Bank agreed to buy (positive amount) or sell (negative amount) before netting of positions and payments with the counterparty. The amounts by currency are presented gross as stated in Note 30. The net total represents the fair value of the currency derivatives. The above analysis includes only monetary assets and liabilities. Investments in equities and non-monetary assets are not considered to give rise to any material currency risk.

The following table presents sensitivities of profit or loss and equity to reasonably possible changes in exchange rates applied at the end of the reporting period relative to the functional currency of the Bank, with all other variables held constant:

	At 31 December 2018		At 31 December 2017	
In thousands of Armenian Drams	**Impact on profit or loss**	**Impact on equity**	**Impact on profit or loss**	**Impact on equity**
US Dollar strengthening by 10% (2017: strengthening by 10%)	4,987	4,987	(54,614)	(54,614)
Euro strengthening by 10% (2017: strengthening by 10%)	824	824	9,290	9,290

26 Financial Risk Management (Continued)

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

The tables below summarise the Bank's exposure to interest rate risks. The tables present the aggregated amounts of the Bank's financial assets and liabilities at carrying amounts, categorised by the earlier of contractual interest repricing or maturity dates.

The Bank's exposure to interest rate risk as at 31 December 2018 is set out below:

In thousands of Armenian Drams	**Less than 3 months**	**3-12 months**	**1-5 years**	**More than 5 years**	**Non-interest bearing**	**Carrying amount**
ASSETS						
Cash and cash equivalents	7,081,312	-	-	-	36,004,603	43,085,915
Investments in debt securities	7,417,058	14,187,622	2,179,092	-	-	23,783,772
Investments in equity securities	-	-	-	-	32,093	32,093
Loans and advances to banks	17,359,992	-	-	-	-	17,359,992
Loans and advances to customers	91,055,945	3,469,160	7,427,594	1,827,323	-	103,780,022
Other financial assets	-	-	-	-	1,927,492	1,927,492
Total financial assets	**122,914,307**	**17,656,782**	**9,606,686**	**1,827,323**	**37,964,188**	**189,969,286**
LIABILITIES						
Due to other banks	39,960	-	-	-	381,428	421,388
Current accounts and deposits from customers	42,280,913	34,180,322	1,175,522	-	75,315,598	152,952,355
Other financial liabilities	-	-	-	-	2,180,773	2,180,773
Total financial liabilities	**42,320,873**	**34,180,322**	**1,175,522**	**-**	**77,877,799**	**155,554,516**
Net interest sensitivity gap at 31 December 2018	**80,593,434**	**(16,523,540)**	**8,431,164**	**1,827,323**	**(39,913,611)**	**34,414,770**

26 Financial Risk Management (Continued)

The Bank's exposure to interest rate risk as at 31 December 2017 is set out below:

In thousands of Armenian Drams	Less than 3 months	3-12 months	1-5 years	More than 5 years	Non-interest bearing	Carrying amount
ASSETS						
Cash and cash equivalents	3,001,110	-	-	-	66,464,300	69,465,410
Financial instruments at fair value through profit or loss	1,117,957	-	-	-	196,113	1,314,070
Available-for-sale financial assets	7,548,987	11,640,825	3,974,280	103,522	32,132	23,299,746
Loans and advances to banks	10,566,868	-	-	-	-	10,566,868
Loans and advances to customers	83,353,021	3,299,382	8,775,940	2,904	-	95,431,247
Other financial assets	-	-	-	-	2,813,698	2,813,698
Total financial assets	**105,587,943**	**14,940,207**	**12,750,220**	**106,426**	**69,506,243**	**202,891,039**
LIABILITIES						
Due to other banks	5,889,731	95,937	279,651	-	618,931	6,884,250
Current accounts and deposits from customers	41,442,723	41,339,375	2,049,345	-	73,748,048	158,579,491
Other financial liabilities	-	-	-	-	3,004,094	3,004,094
Total financial liabilities	**47,332,454**	**41,435,312**	**2,328,996**	**-**	**77,371,073**	**168,467,835**
Net interest sensitivity gap at 31 December 2017	**58,255,489**	**(26,495,105)**	**10,421,224**	**106,426**	**(7,864,830)**	**34,423,204**

The management of interest rate risk based on interest rate gap analysis supplemented 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 positions of interest-bearing assets and liabilities, excluding financial instruments at fair value though profit or loss and financial assets available-for-sale, existing as at 31 December 2018 and 2017 is as follows:

	2018		**2017**	
In thousands of Armenian Drams	**Profit or loss**	**Equity**	**Profit or loss**	**Equity**
100 bp parallel rise	628,214	628,214	421,526	421,526
100 bp parallel fall	(628,234)	(628,234)	(421,692)	(421,692)

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 2018 and 2017 and a simplified scenario of a 100 bp symmetrical fall or rise in all yield curves is as follows:

	2018		**2017**	
In thousands of Armenian Drams	**Profit or loss**	**Equity**	**Profit or loss**	**Equity**
100 bp parallel rise	(20,468)	(92,460)	(30,549)	(115,834)
100 bp parallel fall	21,556	94,537	32,968	119,518

26 Financial Risk Management (Continued)

The Bank monitors interest rates for its financial instruments. The table below summarises interest rates at the respective reporting date based on reports reviewed by key management personnel. For securities, the interest rates represent yields to maturity based on market quotations at the reporting date:

	2018			2017		
In % p.a.	**AMD**	**USD**	**Other**	**AMD**	**USD**	**Other**
Assets						
Cash and cash equivalents	-	2.4	2.7	4.6	-	-
Financial assets designated at fair value through profit or loss	-	-	-	10.6	-	-
Investments in debt securities	6.8	-	-	-	-	-
Loans and advances to banks	6.3	2.5	0.8	6.4	1.3	-
Loans and advances to customers	11.0	6.9	6.4	12.3	8.0	7.3
Debt investment securities available for sale	-	-	-	7.9	-	-
Liabilities						
Due to other banks	10.6	-	-	9.3	-	1.6
Current accounts and deposits from accounts						
- current accounts and demand deposits	2.0	0.8	1.5	2.3	0.9	0.6
- term deposits	7.9	2.9	1.0	9.0	4.0	1.3

The sign "-" in the table above means that the Bank does not have the respective assets or liabilities in the corresponding currency.

Other price risk. The Bank is exposed to prepayment risk through providing fixed or variable rate loans, including mortgages, which give the borrower the right to repay the loans early. The Bank's current year profit and equity at the end of the current reporting period would not have been significantly impacted by changes in prepayment rates because such loans are carried at amortised cost and the prepayment right is at, or close to, the amortised cost of the loans and advances to customers (2017: no material impact).

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

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 and the Board.

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.

26 Financial Risk Management (Continued)

Long-term, or structural, liquidity and funding risk management is the collective responsibility of ALCO. Main objectives of ALCO include managing the balance sheet with a view to enhance profitability and promote efficiency in the use of capital and funding by enhancing return on risk assets, reviewing all risks and ensuring their prudent management.

Global Markets department is responsible for the short-term or operational liquidity risk management of the Bank. Global Markets department should maintain adequate portfolio of short-term liquid assets, largely made up of: short-term liquid securities, loans and advances to banks and other inter-bank facilities. All significant transactions which can impact the Bank's liquidity position are pre-agreed with Global Markets department by Businesses.

The key measures used by the Bank for managing liquidity risk and funding risk are liquidity coverage ratio, liquid asset buffer ratio, net stable funding ratio, depositor and term funding maturity concentrations, which are monitored and managed on daily basis. Liquidity and funding risk appetite is defined by the Bank in a Risk Appetite Statement approved by the Board. The CBA sets and monitors liquidity requirements for the Bank. Under the current requirements set by the CBA, banks have to maintain the ratios of liquid assets to total assets and liquid assets to on demand liabilities above the prescribed minimum level. For this purpose liquid assets include cash and cash equivalents and Government treasury bills, which are not pledged or the use of which is not restricted in any way. As at 31 December 2018, this minimum level was 15% and 60% respectively. The Bank was in compliance with the statutory liquidity ratios as at 31 December 2018 and 2017 and over the periods.

The following table shows the liquidity ratios calculated in accordance with the requirements of the CBA, as at 31 December:

In thousands of Armenian Drams	**2018**	**2017**
At 31 December		
Ratio of liquid assets to total assets	37%	45%
Ratio of liquid assets to on demand liabilities	84%	125%

Regular liquidity stress testing under a variety of scenarios covering both normal and more severe market conditions is performed and reviewed by ALCO quarterly. There is also a Contingency Funding Plan in place, which defines early warning indicators, crises management team, responsibilities, urgent liquidity sources, as well as crisis scenarios and Bank's mitigating actions.

The table below shows liabilities at 31 December 2018 by their remaining contractual maturity. The amounts of liabilities disclosed in the maturity table are the contractual undiscounted cash flows, including gross loan commitments and financial guarantees. Such undiscounted cash flows differ from the amount included in the statement of financial position because the amount in the statement of financial position is based on discounted cash flows. Financial derivatives are included at the contractual amounts to be paid or received, unless the Bank expects to close the derivative position before its maturity date in which case the derivatives are included based on the expected cash flows.

26 Financial Risk Management (Continued)

The maturity analysis for financial liabilities as at 31 December 2018 is as follows:

In thousands of Armenian Drams	**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**
Non-derivative liabilities						
Due to other banks	415,996	30	2,142	3,873	-	422,041
Current accounts and deposits from customers	89,428,132	10,281,954	44,830,560	9,335,305	2,187,902	156,063,853
Other financial liabilities	1,415,979	217,384	519,902	27,508	-	2,180,773
Total liabilities	**91,260,107**	**10,499,368**	**45,352,604**	**9,366,686**	**2,187,902**	**158,666,667**
Credit related commitments and letters of credit	**30,862,668**	**-**	**-**	**-**	**-**	**30,862,668**
Performance guarantees	**1,499,464**	**-**	**-**	**-**	**-**	**1,499,464**
Financial guarantees	**372,243**	**-**	**-**	**-**	**-**	**372,243**
Other commitments	**86,357**	**-**	**-**	**-**	**-**	**86,357**

The maturity analysis for financial liabilities as at 31 December 2017 is as follows:

In thousands of Armenian Drams	**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**
Non-derivative liabilities						
Due to other banks	662,351	19,833	5,975,866	341,661	-	6,999,711
Current accounts and deposits from customers	84,021,977	10,112,505	45,264,045	22,007,959	1,525,937	162,932,423
Other financial liabilities	1,240,497	345,479	1,159,974	258,145	-	3,004,095
Total liabilities	**85,924,825**	**10,477,817**	**52,399,885**	**22,607,765**	**1,525,937**	**172,936,229**
Credit related commitments and letters of credit	**24,805,743**	**-**	**-**	**-**	**-**	**24,805,743**
Performance guarantees	**2,090,964**	**-**	**-**	**-**	**-**	**2,090,964**
Financial guarantees	**234,205**	**-**	**-**	**-**	**-**	**234,205**
Other commitments	**503,443**	**-**	**-**	**-**	**-**	**503,443**

The table below shows the maturity analysis of non-derivative financial assets at their carrying amounts and based on their contractual maturities, except for assets that are readily saleable if it should be necessary to meet cash outflows on financial liabilities. Such financial assets are included in the maturity analysis based on their expected date of disposal. Impaired loans are included at their carrying amounts net of impairment provisions, and based on the expected timing of cash inflows. Derivatives are presented based on their contractual maturities.

26 Financial Risk Management (Continued)

When the amount payable is not fixed, the amount disclosed is determined by reference to the conditions existing at the end of the reporting period. Foreign currency payments are translated using the spot exchange rate at the end of the reporting period.

The maturity analysis of financial instruments at 31 December 2018 is as follows:

In thousands of Armenian Drams	**Demand and less than 1 month**	**From 1 to 3 months**	**From 3 to 12 months**	**From 1 to 5 years**	**Over 5 years**	**No maturity**	**Overdue**	**Total**
Assets								
Cash and cash equivalents	43,085,915	-	-	-	-	-	-	43,085,915
Investments in debt securities	3,075,508	4,341,549	14,187,623	2,179,092	-	-	-	23,783,772
Investments in equity securities	-	-	-	-	-	32,093	-	32,093
Loans and advances to banks	17,359,992	-	-	-	-	-	-	17,359,992
Loans and advances to customers	6,801,689	7,942,312	26,576,308	42,818,281	10,023,172	-	9,618,260	103,780,022
Deferred tax assets	-	-	-	-	-	1,059,593	-	1,059,593
Property, equipment and intangible assets	-	-	-	-	-	2,718,200	-	2,718,200
Other assets	1,162,678	233,901	3,039,610	55,495	8,746	349,464	-	4,849,894
Total	**71,485,782**	**12,517,762**	**43,803,541**	**45,052,868**	**10,031,918**	**4,159,350**	**9,618,260**	**196,669,481**
Liabilities								
Due to other banks	415,823	30	2,036	3,499	-	-	-	421,388
Current accounts and deposits from customers	89,405,348	10,230,021	43,694,053	8,361,607	1,261,326	-	-	152,952,355
Other liabilities	2,004,560	1,059,500	604,678	71,293	-	-	-	3,740,031
Total potential future payments for financial obligations	**91,825,731**	**11,289,551**	**44,300,767**	**8,436,399**	**1,261,326**	**-**	**-**	**157,113,774**
Liquidity gap arising from financial instruments	**(20,339,949)**	**1,228,211**	**(497,226)**	**36,616,469**	**8,770,592**	**4,159,350**	**9,618,260**	**39,555,707**

26 Financial Risk Management (Continued)

Liquidity requirements to support calls under guarantees and standby letters of credit are considerably less than the amount of the commitment disclosed in the above maturity analysis, because the Bank does not generally expect the third party to draw funds under the agreement. The total outstanding contractual amount of commitments to extend credit as included in the above maturity table does not necessarily represent future cash requirements, since many of these commitments will expire or terminate without being funded.

The maturity analysis of financial instruments at 31 December 2017 is as follows:

In thousands of Armenian Drams	**Demand and less than 1 month**	**From 1 to 3 months**	**From 3 to 12 months**	**From 1 to 5 years**	**Over 5 years**	**No maturity**	**Overdue**	**Total**
Assets								
Cash and cash equivalents	69,465,410	-	-	-	-	-	-	69,465,410
Financial assets at fair value through profit or loss	1,128,052	25,834	160,184	-	-	-	-	1,314,070
Loans and advances to banks	10,566,868	-	-	-	-	-	-	10,566,868
Loans and advances to customers	5,587,465	6,290,499	25,193,822	39,032,345	6,168,705	-	13,158,411	95,431,247
Investment securities available for sale	3,015,455	4,533,532	11,640,825	3,974,280	103,522	32,132	-	23,299,746
Current tax assets	-	-	16,325	-	-	-	-	16,325
Deferred tax assets	-	-	-	-	-	1,152,217	-	1,152,217
Property, equipment and intangible assets	-	-	-	-	-	3,135,984	-	3,135,984
Other assets	681,554	356,332	2,543,146	258,145		49,038	379,140	4,267,355
Total	**90,444,804**	**11,206,197**	**39,554,302**	**43,264,770**	**6,272,227**	**4,369,371**	**13,537,551**	**208,649,222**
Liabilities								
Due to other banks	662,125	19,773	5,913,322	289,030	-	-	-	6,884,250
Current accounts and deposits from customers	84,001,795	10,057,447	43,962,546	19,717,326	840,377	-	-	158,579,491
Other liabilities	1,331,542	394,273	2,129,926	343,404	-	-	-	4,199,145
Total potential future payments for financial obligations	**85,995,462**	**10,471,493**	**52,005,794**	**20,349,760**	**840,377**	**-**	**-**	**169,662,886**
Liquidity gap arising from financial instruments	**4,449,342**	**734,704**	**(12,451,492)**	**22,915,010**	**5,431,850**	**4,369,371**	**13,537,551**	**38,986,336**

Payments in respect of gross settled forwards will be accompanied by related cash inflows. Current accounts and deposits from customers are classified in the above analysis based on contractual maturities. However, in accordance with Armenian legislation, individuals have a right to withdraw their deposits prior to maturity if they forfeit their right to 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:

26 Financial Risk Management (Continued)

- less than 1 month: AMD 9,081,593 thousand (2017: AMD 7,610,122 thousand);
- from 1 to 3 months: AMD 8,503,109 thousand (2017: AMD 9,261,651 thousand);
- from 3 to 12 months: AMD 36,113,364 thousand (2017: AMD 35,931,555 thousand);
- from 1 to 5 years: AMD 8,262,718 thousand (2017: AMD 18,363,768 thousand);
- more than 5 years: AMD 1,258,041 thousand (2017: AMD 836,966 thousand).

The matching and/or controlled mismatching of the maturities and interest rates of assets and liabilities is fundamental to the management of the Bank. It is unusual for banks 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 maturities of assets and liabilities and the ability to replace, at an acceptable cost, interest-bearing liabilities as they mature, are important factors in assessing the liquidity of the Bank and its exposure to changes in interest and exchange rates.

Management believes that in spite of a substantial portion of customer accounts being on demand, diversification of these deposits by number and type of depositors, and the past experience of the Bank would indicate that these customer accounts provide a long-term and stable source of funding for the Bank.

27 Management of Capital

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 2018, this minimum level was 12%. The Bank was in compliance with the statutory capital ratio as at 31 December 2018 and 2017 and over the periods.

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 calculated based on reports provided to the CBA, as at 31 December:

In thousands of Armenian Drams	**2018**	**2017**	**2016**
Tier 1 capital			
Share capital	18,434,350	18,434,350	18,434,350
Retained earnings	18,793,323	18,088,360	26,028,383
General Reserve (CBA)	1,958,838	1,958,838	1,958,838
Adjustment to CBA accounting principles	(3,232,133)	(3,413,480)	(10,504,088)
Other deductions	(3,161,953)	(3,018,638)	(3,059,590)
Total tier 1 capital	**32,792,425**	**32,049,430**	**32,857,893**
Tier 2 capital			
Revaluation reserve for available-for-sale financial assets, gross of tax	56,323	218,862	321,364
Revaluation reserve for land and buildings	292,215	292,215	292,215
Share-based payment reserve	83,371	95,927	94,788
Total tier 2 capital	**431,909**	**607,004**	**708,367**
Total capital	**33,224,334**	**32,656,434**	**33,566,260**
Risk weighted assets, combining credit, market and operational risks	**171,311,916**	**173,438,234**	**202,361,504**
Total capital ratio	**19.39%**	**18.83%**	**16.6%**

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.

28 Contingencies and Commitments

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

Tax contingencies. The taxation system in the Republic of Armenia continues to evolve and is characterised 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, might be material but is unlikely to be significant.

Operating lease commitments. Where the Bank is the lessee, the future minimum lease payments under non-cancellable operating leases are as follows:

In thousands of Armenian Drams	**2018**	**2017**
Not later than 1 year	456,937	442,325
Later than 1 year and not later than 5 years	1,008,144	1,356,820
Later than 5 years	-	27
Total operating lease commitments	**1,465,081**	**1,799,172**

Credit related commitments. The primary purpose of these instruments is to ensure that funds are available to a customer as required. Guarantees and standby letters of credit, which represent irrevocable assurances that the Bank will make payments in the event that a customer cannot meet its obligations to third parties, carry the same credit risk as loans. Documentary and commercial letters of credit, which are written undertakings by the Bank on behalf of a customer authorising a third party to draw drafts on the Bank up to a stipulated amount under specific terms and conditions, are collateralised by the underlying shipments of goods to which they relate or cash deposits and, therefore, carry less risk than a direct borrowing.

Commitments to extend credit represent unused portions of authorisations to extend credit in the form of loans, guarantees or letters of credit. With respect to credit risk on commitments to extend credit, the Bank is potentially exposed to loss in an amount equal to the total unused commitments, if the unused amounts were to be drawn down. However, the likely amount of loss is less than the total unused commitments since most commitments to extend credit are contingent upon customers maintaining specific credit standards.

The Bank monitors the term to maturity of credit related commitments, because longer-term commitments generally have a greater degree of credit risk than shorter-term commitments.

28 Contingencies and Commitments (Continued)

Outstanding credit related commitments are as follows:

In thousands of Armenian Drams	Note	2018	2017
Loan and credit line commitments		15,095,479	13,602,520
Credit card commitments		4,736,316	4,580,498
Performance guarantees		1,499,464	2,090,964
Undrawn overdraft facilities		8,752,100	6,574,914
Letters of credit		2,278,773	47,811
Financial guarantees issued		372,243	234,205
Other commitments		86,357	503,443
Less: Provision for guarantees and other commitments	18	(11,406)	-
Less: Provision for loan commitments	18	(61,537)	-
Total credit related commitments, net of provision and cash covered exposures		**32,747,789**	**27,634,355**

Refer to Note 26 for the description of credit risk grading system used by the Bank and the approach to ECL measurement, including the definition of default and SICR as applicable to credit related commitments.

The total outstanding contractual amount of undrawn credit lines, letters of credit, and guarantees does not necessarily represent future cash requirements, as these financial instruments may expire or terminate without being funded. The fair value of credit related commitments was AMD 362,817 thousand at 31 December 2018 (2017: AMD 447,125 thousand).

Of these commitments, AMD 17,819,396 thousand are top 10 customers as at 31 December 2018 (31 December 2017: AMD 13,618,839 thousand are to 10 customers).

29 Offsetting Financial Assets and Financial Liabilities

Financial instruments subject to offsetting, enforceable master netting and similar arrangements are as follows at 31 December 2018:

	Gross amounts before offsetting in the statement of financial position (a)	**Gross amounts set off in the statement of financial position (b)**	**Net amount after offsetting in the statement of financial position (c) = (a) – (b)**	**Amounts subject to master netting and similar arrangements not set off in the statement of financial position**		**Net amount of exposure (c) – (d) – (e)**
In thousands of Armenian Drams				**Financial instruments (d)**	**Cash collateral received (e)**	
ASSETS						
Loans and advances to customers						
- Reverse sale and repurchase agreements	3,035,176	-	3,035,176	(3,035,176)	-	-
TOTAL ASSETS SUBJECT TO OFFSETTING, MASTER NETTING AND SIMILAR ARRANGEMENT	**3,035,176**	**-**	**3,035,176**	**(3,035,176)**	**-**	**-**

29 Offsetting Financial Assets and Financial Liabilities (Continued)

Financial instruments subject to offsetting, enforceable master netting and similar arrangements are as follows at 31 December 2017:

In thousands of Armenian Drams	Gross amounts before offsetting in the statement of financial position (a)	Gross amounts set off in the statement of financial position (b)	Net amount after offsetting in the statement of financial position (c) = (a) – (b)	Amounts subject to master netting and similar arrangements not set off in the statement of financial position		Net amount of exposure (c) – (d) – (e)
				Financial instruments (d)	Cash collateral received (e)	
ASSETS						
Loans and advances to banks						
- Reverse sale and repurchase agreements	1,882,510	-	1,882,510	(1,882,510)	-	-
Loans and advances to customers						
- Reverse sale and repurchase agreements	2,089,823	-	2,089,823	(2,089,823)	-	-
TOTAL ASSETS SUBJECT TO OFFSETTING, MASTER NETTING AND SIMILAR ARRANGEMENT	**3,972,333**	**-**	**3,972,333**	**(3,972,333)**	**-**	**-**

The disclosure does not apply to loans and advances to customers and related customer deposits unless they are set off in the statement of financial position.

30 Derivative Financial Instruments

The table below sets out fair values, at the end of the reporting period, of currencies receivable or payable under foreign exchange forward contracts entered into by the Bank. The table reflects gross positions before the netting of any counterparty positions (and payments) and covers the contracts with settlement dates after the end of the respective reporting period. The contracts are short term in nature:

		2018		2017	
In thousands of Armenian Drams	Notes	Contracts with positive fair value	Contracts with negative fair value	Contracts with positive fair value	Contracts with negative fair value
Foreign exchange forwards: fair values, at the end of the reporting period, of					
- USD receivable on settlement (+)		141,545	(1,436)	195,729	(943)
- USD payable on settlement (-)		3,453	(1,848)	384	(5,546)
- EUR receivable on settlement (+)		3,293	(30,731)	-	-
Net fair value of foreign exchange forwards	**8,14, 18**	**148,291**	**(34,015)**	**196,113**	**(6,489)**

30 Derivative Financial Instruments (Continued)

Foreign exchange derivative financial instruments entered into by the Bank are generally traded in an over-the-counter market with professional market counterparties on standardised contractual terms and conditions. Derivatives have potentially favourable (assets) or unfavourable (liabilities) conditions as a result of fluctuations in market interest rates, foreign exchange rates or other variables relative to their terms. The aggregate fair values of derivative financial assets and liabilities can fluctuate significantly from time to time.

The table below summarises, by major currencies, the contractual amounts of forward currency contracts outstanding at 31 December 2018 and 2017 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**	
In thousands of Armenian Drams	**31 December 2018**	**31 December 2017**	**31 December 2018**	**31 December 2017**
Buy USD sell AMD				
Less than 3 months	3,311,932	3,869,787	485.2	480.2
Between 3 and 12 months	5,718,875	5,092,540	480.4	472.0
Buy USD sell EUR				
Less than 3 months	-	58,005	-	1.2
Buy EUR sell JPY				
Less than 3 months	2,214,600	-	95.9	-
Buy USD sell AUD				
Less than 3 months	34,810	-	1.4	-
Buy USD sell RUB				
Less than 3 months	129,849	-	68.3	-
Buy USD sell CAD				
Less than 3 months	28,481	37,965	1.4	1.3
Buy RUB sell USD				
Less than 3 months	127,795	-	68.6	-
Buy EUR sell USD				
Less than 3 months	1,937,775	58,010	1.1	1.2
Buy AMD sell USD				
Less than 3 months	606,423	1,077,937	485.8	482.9
Between 3 and 12 months	271,370	-	493.4	-

31 Fair Value Disclosures

Fair value measurements are analysed by level in the fair value hierarchy as follows: (i) level one are measurements at quoted prices (unadjusted) in active markets for identical assets or liabilities, (ii) level two measurements are valuations techniques with all material inputs observable for the asset or liability, either directly (that is, as prices) or indirectly (that is, derived from prices), and (iii) level three measurements are valuations not based on observable market data (that is, unobservable inputs). Management applies judgement in categorising financial instruments using the fair value hierarchy. If a fair value measurement uses observable inputs that require significant adjustment, that measurement is a Level 3 measurement. The significance of a valuation input is assessed against the fair value measurement in its entirety.

(a) Recurring fair value measurements

Recurring fair value measurements are those that the accounting standards require or permit in the statement of financial position at the end of each reporting period. The level in the fair value hierarchy into which the recurring fair value measurements are categorised are as follows:

	31 December 2018		**31 December 2017**	
In thousands of Armenian Drams	**Level 2**	**Total**	**Level 2**	**Total**
ASSETS AT FAIR VALUE				
FINANCIAL ASSETS				
Securities at FVTPL				
- Armenian government bonds	-	-	1,117,957	1,117,957
Investments in debt securities				
- Armenian government bonds	23,783,772	23,783,772	-	-
Investments in equity securities				
- Corporate shares	32,093	32,093	-	-
Investment securities AFS				
- Armenian government bonds	-	-	23,267,614	23,267,614
Other financial assets				
- Foreign exchange forward contracts	148,291	148,291	196,113	196,113
TOTAL ASSETS WITH FAIR VALUE MEASUREMENTS	**23,964,156**	**23,964,156**	**24,581,684**	**24,581,684**
LIABILITIES AT FAIR VALUE				
FINANCIAL LIABILITIES				
Other financial liabilities				
- Foreign exchange forward contracts	(34,015)	(34,015)	(6,489)	(6,489)
TOTAL LIABILITIES WITH FAIR VALUE MEASUREMENTS	**(34,015)**	**(34,015)**	**(6,489)**	**(6,489)**

31 Fair Value Disclosures (Continued)

(b) Assets and liabilities not measured at fair value but for which fair value is disclosed

Fair values analysed by level in the fair value hierarchy and carrying value of assets not measured at fair value are as follows:

In thousands of Armenian Drams	**31 December 2018** Level 2 fair value	Level 3 fair value	Total	Carrying value
FINANCIAL ASSETS				
Cash and cash equivalents	43,085,915	-	43,085,915	43,085,915
Loans and advances to banks	17,359,992	-	17,359,992	17,359,992
Loans and advances to customers at AC	-	103,780,022	103,780,022	103,780,022
Other financial assets	-	1,779,201	1,779,201	1,779,201
TOTAL	**60,445,907**	**105,559,223**	**166,005,130**	**166,005,130**
FINANCIAL LIABILITIES				
Due to other banks	421,388	-	421,388	421,388
Current accounts and deposits from customers	79,120,652	73,831,703	152,952,355	152,952,355
Other financial liabilities	-	2,146,758	2,146,758	2,146,758
TOTAL	**79,542,040**	**75,978,461**	**155,520,501**	**155,520,501**

In thousands of Armenian Drams	**31 December 2017** Level 2 fair value	Level 3 fair value	Total	Carrying value
FINANCIAL ASSETS				
Cash and cash equivalents	69,465,410	-	69,465,410	69,465,410
Loans and advances to banks	10,566,868	-	10,566,868	10,566,868
Loans and advances to customers at AC	-	95,431,247	95,431,247	95,431,247
Other financial assets	-	2,813,698	2,813,698	2,813,698
TOTAL	**80,032,278**	**98,244,945**	**178,277,223**	**178,277,223**
FINANCIAL LIABILITIES				
Due to other banks	6,884,250	-	6,884,250	6,884,250
Current accounts and deposits from customers	75,427,465	83,152,026	158,579,491	158,579,491
Other financial liabilities	-	3,004,094	3,004,094	3,004,094
TOTAL	**82,311,715**	**86,156,120**	**168,467,835**	**168,467,835**

31 Fair Value Disclosures (Continued)

The fair values in level 2 and level 3 of fair value hierarchy were estimated using the discounted cash flows valuation technique. The fair value of floating rate instruments that are not quoted in an active market was estimated to be equal to their carrying amount. The fair value of unquoted fixed interest rate instruments was estimated based on estimated future cash flows expected to be received discounted at current interest rates for new instruments with similar credit risk and remaining maturity.

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

- discount rates of 0.8%-6.3% (31 December 2017: 1.3%-6.4%) and 6.4%-11.0% (31 December 2017: 7.3%-12.3%) are used for discounting future cash flows from loans and advances to banks and loans to customers, respectively; discount rates of 0.8% - 10.6% (31 December 2017: 0.6% - 9.0%) are used for discounting future cash flows for liabilities;
- the fair value of variable rate instruments is not materially different from carrying amount;
- the fair value of government bonds is estimated based on government bonds yield curve.

32 Presentation of Financial Instruments by Measurement Category

For the purposes of measurement, IFRS 9 “Financial Instruments” classifies financial assets into the following categories: (a) financial assets at FVTPL; (b) debt instruments at FVOCI, (c) equity instruments at FVOCI and (d) financial assets at AC. Financial assets at FVTPL have two sub-categories: (i) assets mandatorily measured at FVTPL, and (ii) assets designated as such upon initial recognition or subsequently. In addition, finance lease receivables form a separate category.

For the purposes of measurement at 31 December 2017, IAS 39 “Financial Instruments: Recognition and Measurement”, classified financial assets into the following categories: (a) L&R; (b) AFS financial assets; (c) HTM financial assets and (d) financial assets at FVTPL (“FVTPL”). Financial assets at FVTPL had two sub-categories: (i) assets designated as such upon initial recognition, and (ii) those classified as held for trading. In addition, finance lease receivables formed a separate category. All of the Bank’s financial assets at 31 December 2017 fell in the L&R category except for financial derivatives. All of the Bank’s financial liabilities except for derivatives were carried at AC. Derivatives belonged to the FVTPL measurement category and were held for trading.

The following table provides a reconciliation of financial assets with these measurement categories as of 31 December 2018:

In thousands of Armenian Drams	**FVTPL (mandatory)**	**Debt instru-ments at FVOCI**	**Equity instru-ments at FVOCI**	**AC**	**Total**
ASSETS					
Cash and cash equivalents	-	-	-	43,085,915	43,085,915
Loans and advances to banks	-	-	-	17,359,992	17,359,992
Investments in debt securities	723,437	18,051,818	-	5,008,517	23,783,772
Investments in equity securities	-	-	32,093	-	32,093
Loans and advances to customers	-	-	-	103,780,022	103,780,022
Other financial assets	148,291	-	-	1,779,201	1,927,492
TOTAL FINANCIAL ASSETS	**871,728**	**18,051,818**	**32,093**	**171,013,647**	**189,969,286**
LIABILITIES					
Due to other banks	-	-	-	421,388	421,388
Current accounts and deposits from customers	-	-	-	152,952,355	152,952,355
Other financial liabilities	34,015	-	-	2,146,758	2,180,773
TOTAL FINANCIAL LIABILITIES	**34,015**	**-**	**-**	**155,520,501**	**155,554,516**

32 Presentation of Financial Instruments by Measurement Category (Continued)

The following table provides a reconciliation of financial assets with measurement categories at 31 December 2017:

In thousands of Armenian Drams	**L&R**	**AFS**	**Trading assets**	**Other amortised cost**	**Total**
ASSETS					
Cash and cash equivalents	69,465,410	-	-	-	69,465,410
Securities at FVTPL	-	-	1,314,070	-	1,314,070
Loans and advances to banks	10,566,868	-	-	-	10,566,868
Loans and advances to customers	95,431,247	-	-	-	95,431,247
Investment securities AFS	-	23,299,746	-	-	23,299,746
Other financial assets	2,813,698	-	-	-	2,813,698
TOTAL FINANCIAL ASSETS	**178,277,223**	**23,299,746**	**1,314,070**	**-**	**202,891,039**
LIABILITIES					
Due to other banks	-	-	-	6,884,250	6,884,250
Current accounts and deposits from customers	-	-	-	158,579,491	158,579,491
Other financial liabilities	-	-	6,489	2,997,605	3,004,094
TOTAL FINANCIAL LIABILITIES	**-**	**-**	**6,489**	**168,461,346**	**168,467,835**

As of 31 December 2018 and 31 December 2017, all of the Bank's financial liabilities except for derivatives were carried at AC.

33 Related Party Transactions

Parties are generally considered to be related if the parties are under common control, or one party has the ability to control the other party or can exercise significant influence over the other party in making financial or operational decisions. In considering each possible related party relationship, attention is directed to the substance of the relationship, not merely the legal form.

At 31 December 2018, the outstanding balances with related parties were as follows:

In thousands of Armenian Drams	**Entities under common control**	**Key management personnel**	**Other related parties**
Cash and cash equivalents (contractual interest rate: 0.0%-6.6%)	17,357,684	-	-
Loans and advances to banks (contractual interest rate:0.0% - 2.41 %)	12,126,731	-	-
Loans and advances to customers (contractual interest rate: 4.0 - 18.0%)	-	586,198	13,227
Credit loss allowance at 31 December 2018	-	(4,857)	(158)
Other assets	228,295	-	-
Due to other banks (contractual interest rate: 0%)	381,428	-	-
Current accounts and deposits from customers (contractual interest rate: 0-7.5 %)	-	412,329	502,440
Provisions for liabilities and charges	-	3	-
Other liabilities	1,897,226	-	-

33 Related Party Transactions (Continued)

The income and expense items with related parties for 2018 were as follows:

In thousands of Armenian Drams	**Entities under common control**	**Key management personnel**	**Other related parties**
Interest income	498,490	29,070	5,958
Interest expense	(56,985)	(16,839)	(207)
Credit loss allowance	-	(3,477)	9,344
Gains less losses from trading in foreign currencies	88,737	-	-
Foreign exchange translation gains less losses	(134,212)	954	1,646
Fee and commission expense	(63,066)	-	(5,141)
Other operating income	39,124	447	2,871
Other general administrative expenses	(1,593,225)	-	-

At 31 December 2018, other rights and obligations with related parties were as follows:

In thousands of Armenian Drams	**Entities under common control**	**Key management personnel**	**Other related parties**
Guarantees received by the Bank at the year end	2,000,000	-	-
Other commitments	-	22,790	360,463
Other contingent obligations	13,980,692	-	-

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

In thousands of Armenian Drams	**Entities under common control**	**Key management personnel**	**Other related parties**
Cash and cash equivalents (contractual interest rate: 0.0%-6.6%)	31,092,993	-	-
Loans and advances to banks (contractual interest rate: 1.3 %)	7,262,811	-	-
Loans and advances to customers (contractual interest rate: 4.0 – 18.0%)	-	567,426	208,872
Credit loss allowance	-	(1,380)	(9,502)
Other assets	18,743	-	-
Due to other banks (contractual interest rate: 0 – 1.6 %)	6,435,971	-	-
Current accounts and deposits from customers (contractual interest rate: 0 - 8.5%)	-	498,920	317,492
Other liabilities	2,466,736	-	-

The income and expense items with related parties for 2017 were as follows:

In thousands of Armenian Drams	**Entities under common control**	**Key management personnel**	**Other related parties**
Interest income	155,336	32,766	19,014
Interest expense	(124,195)	(8,570)	(6,959)
Credit loss allowance	-	(34)	(9,405)
Gains less losses from trading in foreign currencies	119,408	-	-
Foreign exchange translation gains less losses	31,459	742	572
Fee and commission expense	(79,573)	-	(2,161)
Other operating income	34,998	669	3,935
Other general administrative expenses	(1,552,834)	-	-

33 Related Party Transactions (Continued)

At 31 December 2017, other rights and obligations with related parties were as follows:

In thousands of Armenian Drams	**Entities under common control**	**Key management personnel**	**Other related parties**
Guarantees received by the Bank at the year end	870,150	-	-
Other commitments	-	20,230	4,231
Other contingent obligations	10,136,239	-	-

Key management compensation is presented below:

	2018		**2017**	
In thousands of Armenian Drams	**Expense**	**Accrued liability**	**Expense**	**Accrued liability**
Short-term benefits:				
- Salaries	714,472	-	628,965	-
- Short-term bonuses	134,206	202,449	127,947	195,720
- Benefits in-kind	84,843	-	76,397	-
Share-based compensation:				
- Cash-settled share-based compensation	6,608	7,551	-	-
- Equity-settled share-based compensation	26,552	30,341	13,067	-
Total	**966,681**	**240,341**	**846,376**	**195,720**

Short-term bonuses fall due wholly within twelve months after the end of the period in which management rendered the related services.

34 Events after the End of the Reporting Period

There were no events after the reporting period that may require adjustment of or disclosure in the Bank's financial statements for the year ended 31 December 2018.

35 Accounting Policies Applicable before 1 January 2018

Accounting policies applicable to the comparative period ended 31 December 2017 that were amended by IFRS 9, are as follows.

Financial instruments – key measurement terms. Depending on their classification financial instruments are carried at fair value, cost, or AC as described below. Refer to Note 3 for the definition of fair value and AC as well as for description of valuation techniques.

Cost is the amount of cash or cash equivalents paid or the fair value of the other consideration given to acquire an asset at the time of its acquisition and includes transaction costs. Measurement at cost is only applicable to investments in equity instruments that do not have a quoted market price and whose fair value cannot be reliably measured and derivatives that are linked to, and must be settled by, delivery of such unquoted equity instruments.

Other securities at FVTPL. Other securities at FVTPL are financial assets designated irrevocably, at initial recognition, into this category. Management designates securities into this category only if (a) such classification eliminates or significantly reduces an accounting mismatch that would otherwise arise from measuring assets or liabilities or recognising the gains and losses on them on different bases; or (b) a group of financial assets, financial liabilities or both is managed and its performance is evaluated on a fair value basis, in accordance with a documented risk management or investment strategy, and information on that basis is regularly provided to and reviewed by the Bank's management. Recognition and measurement of this category of financial assets is consistent with the above policy for trading securities.

Loans and advances to customers. Loans and advances to customers were carried at AC and impairment losses were recognised in profit or loss for the year when incurred as a result of one or more events ("loss events") that occurred after the initial recognition of the financial asset and which had an impact on the amount or timing of the estimated future cash flows of the financial asset or group of financial assets that could be reliably estimated. If the Bank determined that no objective evidence exists that impairment was incurred for an individually assessed financial asset, whether significant or not, it included the asset in a group of financial assets with similar credit risk characteristics, and collectively assessed them for impairment.

The primary factors that the Bank considered in determining whether a financial asset was impaired were its overdue status and realisability of related collateral, if any. The following other principal criteria were also used to determine whether there was objective evidence that a credit loss has occurred:

- any instalment was overdue and the late payment could not be attributed to a delay caused by the settlement systems;
- the borrower experienced a significant financial difficulty as evidenced by the borrower's financial information that the Bank obtained;
- the borrower considered bankruptcy or a financial reorganisation;
- there was an adverse change in the payment status of the borrower as a result of changes in the national or local economic conditions that impacted the borrower; or
- the value of collateral significantly decreased as a result of deteriorating market conditions.

35 Accounting Policies applicable before 1 January 2018 (Continued)

For the purposes of a collective evaluation of credit loss, financial assets were grouped on the basis of similar credit risk characteristics. Those characteristics were relevant to the estimation of future cash flows for groups of such assets by being indicative of the debtors' ability to pay all amounts due according to the contractual terms of the assets being evaluated.

Future cash flows in a group of financial assets that were collectively evaluated for credit loss, were estimated on the basis of the contractual cash flows of the assets and the experience of management in respect of the extent to which amounts would become overdue as a result of past loss events and the success of recovery of overdue amounts. Past experience was adjusted on the basis of current observable data to reflect the effects of current conditions that did not affect past periods, and to remove the effects of past conditions that do not exist currently.

Credit loss was always recognised through an allowance account to write down the asset's carrying amount to the present value of expected cash flows (which excluded future credit losses that have not been incurred) discounted at the original effective interest rate of the asset. The calculation of the present value of the estimated future cash flows of a collateralised financial asset reflected the cash flows that might result from foreclosure less costs for obtaining and selling the collateral, whether or not foreclosure was probable.

If the terms of an impaired financial asset held at AC were renegotiated or otherwise modified because of financial difficulties of the borrower or issuer, impairment were measured using the original effective interest rate before the modification of terms. The renegotiated asset were then derecognised and a new asset were recognised at its fair value only if the risks and rewards of the asset substantially changed. This were normally evidenced by a substantial difference between the present values of the original cash flows and the new expected cash flows.

If, in a subsequent period, the amount of the credit loss decreases and the decrease could be related objectively to an event occurring after the impairment was recognised (such as an improvement in the debtor's credit rating), the previously recognised impairment loss was reversed by adjusting the allowance account through profit or loss for the year.

Uncollectible assets were written off against the related credit loss allowance after all the necessary procedures to recover the asset had been completed and the amount of the loss had been determined. Subsequent recoveries of amounts previously written off were credited to credit loss account in profit or loss for the year.

Investments carried at cost. Management could not reliably estimate fair value of the Bank's AFS investments in equity instruments that do not have a quoted market price and whose fair value cannot be reliably measured. The investments are carried at a cost of AMD 32,132 thousand.

Credit related commitments. Financial guarantees and commitments to provide a loan are initially recognised at fair value and subsequently measured at the higher of (i) the remaining unamortised balance of the amount at initial recognition and (ii) the best estimate of expenditure required to settle the commitment at the end of each reporting period.

35 Accounting Policies applicable before 1 January 2018 (Continued)

Investment securities AFS. This classification included investment securities which the Bank intended to hold for an indefinite period of time and which might be sold in response to needs for liquidity or changes in interest rates, exchange rates or equity prices.

Investment securities AFS were carried at fair value. Interest income on AFS debt securities was calculated using the effective interest method, and recognised in profit or loss for the year.

Dividends on AFS equity instruments were recognised in profit or loss for the year when the Bank's right to receive payment was established and it was probable that the dividends would be collected. All other elements of changes in the fair value were recognised in other comprehensive income until the investment was derecognised or impaired, at which time the cumulative gain or loss was reclassified from other comprehensive income to profit or loss for the year. Impairment losses were recognised in profit or loss for the year when incurred as a result of one or more events ("loss events") that occurred after the initial recognition of investment securities AFS. A significant or prolonged decline in the fair value of an equity security below its cost was an indicator that it was impaired. The cumulative impairment loss – measured as the difference between the acquisition cost and the current fair value, less any impairment loss on that asset previously recognised in profit or loss – was reclassified from other comprehensive income to profit or loss for the year. Impairment losses on equity instruments were not reversed and any subsequent gains were recognised in other comprehensive income. If, in a subsequent period, the fair value of a debt instrument classified as AFS increases and the increase could be objectively related to an event occurring after the impairment loss was recognised in profit or loss, the impairment loss was reversed through profit or loss for the year.

Income and expense recognition. Interest income and expense are recorded for all debt instruments on an accrual basis using the effective interest method. This method defers, as part of interest income or expense, all fees paid or received between the parties to the contract that are an integral part of the effective interest rate, transaction costs and all other premiums or discounts.

Fees integral to the effective interest rate include origination fees received or paid by the entity relating to the creation or acquisition of a financial asset or issuance of a financial liability, for example fees for evaluating creditworthiness, evaluating and recording guarantees or collateral, negotiating the terms of the instrument and for processing transaction documents.

Commitment fees received by the Bank to originate loans at market interest rates are integral to the effective interest rate if it is probable that the Bank will enter into a specific lending arrangement and does not expect to sell the resulting loan shortly after origination. The Bank does not designate loan commitments as financial liabilities at fair value through profit or loss.

When loans and other debt instruments become doubtful of collection, they are written down to the present value of expected cash inflows and interest income is thereafter recorded for the unwinding of the present value discount based on the asset's effective interest rate which was used to measure the impairment loss.

All other fees, commissions and other income and expense items are generally recorded on an accrual basis by reference to completion of the specific transaction assessed on the basis of the actual service provided as a proportion of the total services to be provided.

Commissions and fees arising from negotiating, or participating in the negotiation of a transaction for a third party, such as the acquisition of loans, shares or other securities or the purchase or sale of businesses, and which are earned on execution of the underlying transaction, are recorded on its completion. Portfolio and other management advisory and service fees are recognised based on the applicable service contracts, usually on a time-proportion basis. Asset management fees relating to investment funds are recorded rateably over the period that the service is provided. The same principle is applied for wealth management, financial planning and custody services that are continually provided over an extended period of time.