# FINCA
# UNIVERSAL CREDIT ORGANIZATION
# CLOSED JOINT STOCK COMPANY

Financial Statements and
Independent Auditor’s Report
for the Year Ended 31 December, 2017

## Finca Universal Credit Organization Closed Joint Stock Company

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## Finca Universal Credit Organization Closed Joint Stock Company

### Statement of Management's Responsibilities for the Preparation and Approval of the Financial Statements for the Year Ended December 31, 2017

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

In preparing the financial statements, management is responsible for:

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

Management is also responsible for:

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

The financial statements of the Organization for the year ended December 31, 2017 were approved by management on March 21, 2018.

On behalf of the Management:

**Anush Petrosyan**
Acting General Director

21 March, 2018
Yerevan, Republic of Armenia

**Artak Miqayelyan**
Chief Accountant

21 March, 2018
Yerevan, Republic of Armenia

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# INDEPENDENT AUDITOR'S REPORT

To the Shareholders of FINCA Universal Credit Organization Closed Joint Stock Company:

We have audited the financial statements of FINCA Universal Credit Organization Closed Joint Stock Company (the "Organization"), which comprise the statement of financial position as at December 31, 2017, and the statement of comprehensive income, statement of changes in equity and statement of cash flows for the year then ended, and notes to the financial statements, including a summary of significant accounting policies.

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

## Basis for Opinion

We conducted our audit in accordance with International Standards on Auditing ("ISAs"). Our responsibilities under those standards are further described in the *Auditor's Responsibilities for the Audit of the Financial Statements* section of our report. We are independent of the Organization in accordance with the International Ethics Standards Board for Accountants' *Code of Ethics for Professional Accountants* (the "IESBA Code") together with the ethical requirements that are relevant to our audit of the financial statements in the Republic of Armenia, and we have fulfilled our other ethical responsibilities in accordance with these requirements and the IESBA Code. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

## Key Audit Matters

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

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| Why the matter was determined to be a key audit matter | How the matter was addressed in the audit |
|---|---|
| **Impairment of loans to customers**<br><br>Refer to Note 3 (Critical accounting judgements and key sources of estimation uncertainty)<br><br>The Organization's loans to customers disclosed in Note 8 amount to USD 50,599,651 as of December 31, 2017.<br><br>The Organization's loan portfolio consists of large number of customers with small loan balances. Impairment allowances are calculated on a collective basis for portfolios of loans with similar risk characteristics. To determine the expected future cash flows the management uses historical collection rates based on the information from migration models. The models are assessed bi-annually with the reference to historical collections experience and future expectations. Due to the materiality of the balances and the subjectivity of assumptions used in the models, this matter was determined as a key audit matter. | The following procedures were performed:<br>• We tested the design, implementation and operating effectiveness of key controls over the loan approval, administration and monitoring processes, as well as processes to identify, assess and record loan impairment provisions.<br>• Probability of defaults are estimated by the organization based on the data on migration of sums throughout delinquency buckets during the period from December 2014 to November 2017 as a weighted average of monthly roll rates (frequencies of loans at each bucket to shift to the bucket of more than 180 days past due) and sums at each bucket.<br>• We assessed the portfolio loan loss provisioning models employed by the Organization by reviewing migrations of loans within the buckets of overdue days. We also tested a sample of the model input data such as overdue days used in the migration.<br>• We assessed whether the modelling assumptions used considered all relevant risks, and whether the additional adjustments to reflect un-modelled risks were reasonable. Where we believed that a different value of assumption or input should be used, we recalculated the provision on that basis and compared the results with those of the management's for indications of management's bias.<br>• We have assessed the adequacy and completeness of disclosures. |

**Responsibilities of Management and Those Charged with Governance for the Financial Statements**

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

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

Those charged with governance are responsible for overseeing the Organization'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 Organization'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 Organization'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 Organization to cease to continue as a going concern.
- Evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation.

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

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

From the matters communicated with those charged with governance, we determine those matters that were of most significance in the audit of the financial statements of the current period, which constitute the key audit matters included herein.

Srbuhi Hakobyan
Executive Director

Arpine Ghevondyan
Audit Director

Deloitte Armenia cjsc
21 March, 2018

## Finca Universal Credit Organization Closed Joint Stock Company

### Statement of Financial Position as at December 31, 2017
***(In US Dollars, unless otherwise stated)***

| | Notes | December 31, 2017 | December 31, 2016 |
|---|---|---|---|
| **Assets** | | | |
| Cash and cash equivalents | 5 | 1,240,737 | 2,619,546 |
| Financial assets at fair value through profit or loss | 6 | 3,057 | - |
| Available-for-sale financial assets | | | |
| - pledged under repurchase agreements | 7 | 2,694,745 | 2,620,655 |
| Loans to customers | 8 | 50,599,651 | 53,757,631 |
| Current income tax assets | | - | 5,747 |
| Deferred income tax assets | 21 | 14,725 | 59,927 |
| Property and equipment | 9 | 572,128 | 745,588 |
| Intangible assets | 10 | 596,135 | 568,639 |
| Other assets | 11 | 251,324 | 120,079 |
| **Total assets** | | **55,972,502** | **60,497,812** |
| **Liabilities** | | | |
| Financial liabilities at fair value through profit or loss | 6 | 32,944 | 120,548 |
| Liabilities under repurchase agreements | 12 | 2,547,803 | 2,473,024 |
| Borrowed funds | 13 | 29,532,386 | 43,453,401 |
| Debt securities issued | 14 | 7,273,596 | - |
| Current tax liability | | 555,252 | - |
| Other liabilities | 15 | 915,301 | 907,257 |
| **Total liabilities** | | **40,857,282** | **46,954,230** |
| **Equity** | 16 | | |
| Share capital | | 11,815,575 | 11,815,575 |
| Available-for-sale revaluation reserve | | 142,514 | 88,483 |
| Retained earnings | | 5,698,017 | 4,179,633 |
| Foreign currency translation reserve | | (2,540,886) | (2,540,109) |
| **Total equity** | | **15,115,220** | **13,543,582** |
| **Total liabilities and equity** | | **55,972,502** | **60,497,812** |

The financial statements were authorized for issue on March 21, 2018 by the Board of Directors.

**Anush Petrosyan**
Acting General Director

21 March 2018
Yerevan

**Artak Miqayelyan**
Chief Accountant

21 March 2018
Yerevan

The notes on pages 9 - 48 form an integral part of these financial statements.

## Finca Universal Credit Organization Closed Joint Stock Company

**Statement of Profit or Loss and Other Comprehensive Income**
**for the Year Ended December 31, 2017**
***(In US Dollars, unless otherwise stated)***

| | Notes | 2017 | 2016 |
|---|---|---|---|
| Interest income | 17 | 15,766,281 | 17,589,913 |
| Interest expense | 17 | (3,520,052) | (5,749,724) |
| **Net interest income before impairment losses on interest bearing assets** | | **12,246,229** | **11,840,189** |
| Impairment losses on interest bearing assets | 8 | (1,347,451) | (2,705,291) |
| **Net interest income** | | **10,898,778** | **9,134,898** |
| Fee and commission expense | | (83,994) | (120,333) |
| Net gain/(loss) on financial assets and liabilities at fair value through profit or loss | | 15,168 | (21,773) |
| Net gain from foreign exchange operations | 18 | 212,420 | 234,291 |
| Other income | | 848,708 | 934,280 |
| **Net non-interest income** | | **992,302** | **1,026,465** |
| **Operating income** | | **11,891,080** | **10,161,363** |
| Staff costs | 19 | (4,313,079) | (4,415,654) |
| Depreciation and amortization | 9,10 | (389,275) | (400,712) |
| Other operating expenses | 20 | (3,814,617) | (3,786,844) |
| **Operating expenses** | | **(8,516,971)** | **(8,603,210)** |
| **Profit before income tax** | | **3,374,109** | **1,558,153** |
| Income tax expense | 21 | (680,416) | (325,790) |
| **Net profit for the year** | | **2,693,693** | **1,232,363** |
| **Other comprehensive income** | | | |
| **Items that may be reclassified subsequently to profit or loss:** | | | |
| Foreign currency translation difference | | (777) | (14,622) |
| Net change in fair value of available-for-sale financial assets, net of income tax of USD 13,508 (2016: USD 32,786) | | 54,031 | 131,142 |
| **Other comprehensive income for the year, net of income tax** | | **53,254** | **116,520** |
| **Total comprehensive income for the year** | | **2,746,947** | **1,348,883** |

The notes on pages 9 - 48 form an integral part of these financial statements.

## Finca Universal Credit Organization Closed Joint Stock Company

**Statement of Changes in Equity**
**for the Year Ended December 31, 2017**
***(In US Dollars, unless otherwise stated)***

| | Notes | Share capital | Available-for-sale revaluation reserve | Foreign currency translation reserve | Retained earnings | Total equity |
|---|---|---|---|---|---|---|
| **Balance at January 1, 2016** | | **11,815,575** | **(42,659)** | **(2,525,487)** | **2,947,270** | **12,194,699** |
| Profit for the year | | - | - | - | 1,232,363 | **1,232,363** |
| Other comprehensive loss for the year, net of income tax | | - | 131,142 | (14,622) | - | **116,520** |
| **Total comprehensive income for the year** | | **-** | **131,142** | **(14,622)** | **1,232,363** | **1,348,883** |
| **Balance at December 31, 2016** | | **11,815,575** | **88,483** | **(2,540,109)** | **4,179,633** | **13,543,582** |
| Profit for the year | | - | - | - | 2,693,693 | **2,693,693** |
| Other comprehensive income for the year, net of income tax | | - | 54,031 | (777) | - | **53,254** |
| **Total comprehensive income for the year** | | **-** | **54,031** | **(777)** | **2,693,693** | **2,746,947** |
| Dividends | 16 | - | - | - | (1,175,309) | **(1,175,309)** |
| **Balance at December 31, 2017** | | **11,815,575** | **142,514** | **(2,540,886)** | **5,698,017** | **15,115,220** |

The notes on pages 9 - 48 form an integral part of these financial statements.

## Statement of Cash Flows for the Year Ended December 31, 2017
***(In US Dollars, unless otherwise stated)***

| | Notes | 2017 | 2016 |
|---|---|---|---|
| **Cash flows from operating activities:** | | | |
| Profit before tax | | 3,374,109 | 1,558,153 |
| **Adjustments for:** | | | |
| Impairment losses on interest bearing assets | | 1,347,451 | 2,705,291 |
| Loss on disposal of property and equipment and intangible assets | | 3,315 | 7,678 |
| Net change in accrued interest | | (719,807) | (1,516,411) |
| Depreciation and amortization | | 389,275 | 400,712 |
| Net foreign exchange loss | | 8,568 | (3,536) |
| **Cash inflow from operating activities before changes in operating assets and liabilities** | | **4,402,911** | **3,151,887** |
| **Changes in operating assets and liabilities** | | | |
| Decrease in financial instruments at fair value through profit or loss | | (90,942) | (61,420) |
| Decrease in loans to customers | | 2,498,980 | 3,222,849 |
| Increase in other assets | | (48,100) | (26,329) |
| Increase in liabilities under repurchase agreements | | 75,928 | 577,910 |
| Increase /(Decrease) in other liabilities | | 6,401 | (32,471) |
| **Cash inflow from/(used in) operating activities before** | | **6,845,178** | **6,832,426** |
| Income tax paid | | (85,600) | (41,145) |
| **Net cash from operating activities** | | **6,759,578** | **6,791,281** |
| **Cash flows from investing activities:** | | | |
| Purchase of available-for-sale financial assets | | - | (496,768) |
| Purchase of property and equipment | | (202,633) | (133,180) |
| Purchase of intangible assets | | (127,260) | (179,915) |
| **Net cash used in investing activities** | | **(329,893)** | **(809,863)** |
| **Cash flows from financing activities:** | | | |
| Proceeds from borrowed funds | | 70,672,514 | 69,703,988 |
| Repayment of borrowed funds | | (84,463,825) | (73,017,584) |
| Proceeds from debentures | | 7,147,281 | - |
| Dividends paid | | (1,175,309) | - |
| Repayment of subordinated debt | | - | (2,481,163) |
| **Net cash used in financing activities** | | **(7,819,339)** | **(5,794,759)** |
| **Net (decrease)/increase in cash and cash equivalents** | | **(1,389,654)** | **186,659** |
| **Cash and cash equivalents, beginning of the year** | 5 | **2,619,546** | **2,460,564** |
| Effect of exchange rate changes on the balance of cash and cash equivalents held in foreign currencies | | 10,845 | (27,677) |
| **Cash and cash equivalents, end of the year** | 5 | **1,240,737** | **2,619,546** |

| **Supplementary information:** | | |
|---|---|---|
| Interest received | 15,990,400 | 17,077,069 |
| Interest paid | (3,293,169) | (5,567,587) |

The notes on pages 9 - 48 form an integral part of these financial statements.

## 1. Organization

FINCA Universal Credit Organization cjsc (the "Organization") is a closed joint stock company - 100% subsidiary of FINCA Microfinance Coöperatief U.A. (Netherlands). The Organization is regulated by the Central Bank of Armenia (the "CBA") and conducts its business under license number 13, granted on 28 March 2006.

The Organization is involved in microfinance and provides individual business, consumer and rural loans. The loans are disbursed both in local and foreign currencies.

The registered office of the Organization is located at 2a, Agatangeghos str., Yerevan, Republic of Armenia.

As at December 31, 2017 the Organization had 38 branches operating in Armenia (December 31, 2016: 37 branches).

The founder of FINCA UCO CJSC is FINCA International, Inc., a tax-exempt not-for-profit corporation incorporated and existing under the laws of the state of New York. In 2011 FINCA International, Inc. transferred 100% of issued shares (136,472 shares) of the Organization to FINCA Microfinance Coöperatief U.A. (a cooperative with exclusion on liability, having its official seat in Amsterdam, the Netherlands) as a member contribution to the Cooperative.

As of December 31, 2017, the members of the Cooperative were:

1. FINCA MICROFINANCE HOLDING COMPANY LLC, a limited liability company registered under the laws of the State of Delaware, United States of America and having its registered address at 2711 Centerville Road, Suite 400, Wilmington, Delaware 19808, United States of America. FINCA MICROFINANCE HOLDING COMPANY LLC holds 99 voting rights as a Member A and 1 voting right as a Member B of the Cooperative.
2. FINCA INTERNATIONAL LLC, a limited liability company registered under the laws of the State of Maryland, United States of America and having its registered address at 11 East Chase Street, Baltimore, Maryland 21202, United States of America. FINCA INTERNATIONAL LLC holds 1% voting right of the Cooperative.

As at December 31, 2017 and 2016 the following shareholders owned FINCA MICROFINANCE HOLDING COMPANY LLC:

| | **December 31,2017** | **December 31,2016** |
|---|---|---|
| **First level shareholders/ holders of the issued share capital:** | | |
| FINCA International LLC | 62.93% | 62.93% |
| International Finance Corporation | 14.27% | 14.27% |
| KfW | 8.87% | 8.87% |
| Nederlandse Financierings Maatschappij voor Ontwikkelingslanden N.V. | 7.25% | 7.25% |
| Credit Suisse Microfinance Fund Management Company | 2.96% | 2.96% |
| ASN-NOVIB FONDS | 1.67% | 1.67% |
| Triodos Custody B.V. | 1.03% | 1.03% |
| Triodos SICAV II | 1.03% | 1.03% |
| **Total** | **100.00%** | **100.00%** |

FINCA International Inc. is a not-for-profit corporation under the laws of the United State of America and as such, its Members hold no ownership in the Organization and have no economic rights. As at December 31, 2017 the Members of FINCA International, Inc. are as follows: Rupert Scofield, John Hatch, Robert Hatch and Richard Williamson. FINCA International Inc. produces publicly available financial statements.

The purpose of FINCA is to "Help the poor help themselves". FINCA believes that world hunger and poverty cannot be cured simply by food handouts and grants but can be permanently affected by self-help and self-sufficiency of the poor. FINCA provides low-income people around the world the tools they need to succeed, by offering responsible financial services, such as small loans or savings accounts; by reaching people in remote communities using technology like mobile phones and tablets; and by providing access to life-enhancing products. FINCA operates in communities through affiliated organizations ("affiliates").

The affiliates are typically separate legal entities that enter into affiliate agreements with FINCA. Small loans support investment in individual or community productive micro enterprises. Participants build self-reliance, self-esteem, and a savings fund that remains within the community as a permanent source of capital for continued investment.

## 2. Significant accounting policies

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

These financial statements have been prepared assuming that the Organization is a going concern and will continue in operation for the foreseeable future.

These financial statements are presented in United States Dollars ("USD"), unless otherwise indicated.

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

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

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

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

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

The Organization presents its statement of financial position broadly in order of liquidity. An analysis regarding recovery or settlement within 12 months after the statement of financial position date (current) and more than 12 months after the statement of financial position date (non-current) is presented in Note 27.

**Functional currency.** Items included in the financial statements are measured using the currency of the primary economic environment in which the Organization operates ("the functional currency"). The functional currency of the Organization is the Armenian Dram ("AMD"). The presentational currency of the financial statements of the Organization is the USD.

Translation of financial statements denominated in functional currency into presentation currency is performed as follow:

- Assets and liabilities are translated at the exchange rate at the reporting date,
- Income and expense are translated at the average annual rate
- Share capital and other reserve items of capital are translated at the historical rate
- The resulting differences are presented as a component of other comprehensive income and are recognized directly into equity referred as the "Foreign Currency Translation Reserve".

**Offsetting.** Financial assets and financial liabilities are offset and the net amount reported in the statement of financial position only when there is a legally enforceable right to offset the recognized

amounts and there is an intention to settle on a net basis, or to realize the assets and settle the liability simultaneously. Income and expense is not offset in the statement of profit or loss unless required or permitted by any accounting standard or interpretation, and as specifically disclosed in the accounting policies of the Organization.
The principal accounting policies are set out below.

**Revenue recognition**

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

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

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

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

**Recognition of fee and commission income.** Loan origination fees are deferred, together with the related direct costs, and recognized as an adjustment to the effective interest rate of the loan. Where it is probable that a loan commitment will lead to a specific lending arrangement, the loan commitment fees are deferred, together with the related direct costs, and recognized as an adjustment to the effective interest rate of the resulting loan. Where it is unlikely that a loan commitment will lead to a specific lending arrangement, the loan commitment fees are recognized in profit or loss over the remaining period of the loan commitment. Where a loan commitment expires without resulting in a loan, the loan commitment fee is recognized in profit or loss on expiry. Loan servicing fees are recognized as revenue as the services are provided. All other commissions are recognized when services are provided.

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

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

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

**a) Financial assets at FVTPL.** Financial assets are classified as at FVTPL when the financial asset is either held for trading or it is designated as at FVTPL.

A financial asset is classified as held for trading if:

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

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

Financial assets at FVTPL are stated at fair value, with any gains or losses arising on remeasurement recognized in profit or loss. The net gain or loss recognized in profit or loss incorporates any dividend and interest earned on the financial asset and is included in the 'other gains and losses' and 'interest income' line item, respectively, in the statement of profit or loss and other comprehensive income.

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

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

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

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

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

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

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

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

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

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

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

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

**Renegotiated loans.** The contractual terms of a loan may be modified for a number of reasons including changing market conditions, customer retention and other factors not related to the current or potential credit deterioration of a customer. When the contractual payment terms of a loan have been modified because management have significant concerns about the borrower's ability to meet contractual payments when due, these loans are classified as 'renegotiated loans'. For retail lending, when considering whether there is 'significant concern' regarding a customer's ability to meet contractual loan repayments when due, management assess the customer's delinquency status, account behavior, repayment history, current financial situation and continued ability to repay. Where the customer is not meeting contractual repayments or it is evident that they will be unable to do so without the renegotiation, there will be a significant concern regarding their ability to meet contractual payments, and the loan will be disclosed as impaired, unless the concession granted is insignificant and there are no other indicators of impairment.

Where the modification of contractual payment terms of a loan represents a concession for economic or legal reasons relating to the borrower's financial difficulty, and is a concession that management would not otherwise consider then the renegotiated loan is disclosed as impaired.

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

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

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

Renegotiated loans are classified as unimpaired where the renegotiation has resulted from significant concern about a borrower's ability to meet their contractual payment terms but the renegotiated terms are based on current market rates and contractual cash flows are expected to be collected in full following the renegotiation. Unimpaired renegotiated loans also include previously impaired renegotiated loans that have demonstrated satisfactory performance over a period of time or have been assessed based on all available evidence as having no remaining indicators of impairment. Renegotiated loans are segregated from other parts of the loan portfolio for collective impairment assessment to reflect the possible higher rates of losses for these segments.

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

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

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

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

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

On derecognition of a financial asset other than in its entirety (e.g. when the Organization retains an option to repurchase part of a transferred asset), the Organization allocates the previous carrying amount of the financial asset between the part it continues to recognize under continuing involvement, and the part it no longer recognizes on the basis of the relative fair values of those parts on the date of the transfer. The difference between the carrying amount allocated to the part that is no longer recognized and the sum of the consideration received for the part no longer recognized and any cumulative gain or loss allocated to it that had been recognized in other comprehensive income is recognized in profit or loss. A cumulative gain or loss that had been recognized in other comprehensive income is allocated between the part that continues to be recognized and the part that is no longer recognized on the basis of the relative fair values of those parts.

**Financial liabilities and equity instruments issued**

**Classification as debt or equity.** Debt and equity instruments are classified as either financial liabilities or as equity in accordance with the substance of the contractual arrangements and the definitions of a financial liability and an equity instrument.

**Equity instruments.** An equity instrument is any contract that evidences a residual interest in the assets of an entity after deducting all of its liabilities. Equity instruments are recognized at the proceeds received, net of direct issue costs.

Repurchase of the Organization’s own equity instruments is recognized and deducted directly in equity. No gain or loss is recognized in profit or loss on the purchase, sale, issue or cancellation of the Organization’s own equity instruments.

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

Financial liabilities are classified as at FVTPL when the financial liability is either held for trading or it is designated as at FVTPL.

A financial liability is classified as held for trading if:

- It has been incurred principally for the purpose of repurchasing it in the near term; or

- On initial recognition it is part of a portfolio of identified financial instruments that the Organization manages together and has a recent actual pattern of short-term profit-taking; or
- It is a derivative that is not designated and effective as a hedging instrument.

A financial liability other than a financial liability held for trading may be designated as at FVTPL upon initial recognition if:

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

**Other financial liabilities.** Other financial liabilities (including borrowed funds, subordinated debt and other financial liabilities) are initially measured at fair value, net of transaction costs.
Other financial liabilities are subsequently measured at amortized cost using the effective interest method, with interest expense recognized on an effective yield basis.

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

**Derecognition of financial liabilities.** The Organization derecognizes financial liabilities when, and only when, the Organization's obligations are discharged, cancelled or they expire. Where an existing financial liability is replaced by another from the same lender on substantially different terms, or the terms of an existing liability are substantially modified, such an exchange or modification is treated as a derecognition of the original liability and the recognition of a new liability. The difference between the carrying amount of the financial liability derecognized and the consideration paid and payable is recognized in profit and loss.

**Derivative financial instruments.** In the normal course of business the Organization enters into various derivative financial instruments including currency swaps and currency exchange contracts.

Swaps are contractual agreements between two parties to exchange streams of payments over time based on specified notional amounts, in relation to movements in a specified underlying index such as an interest rate, foreign currency rate or equity index. In a currency swap, the Organization pays a specified amount in one currency and receives a specified amount in another currency. Currency swaps are mostly gross-settled.

Such financial instruments are held for trading and are initially recognized in accordance with the policy for initial recognition of financial instruments and are subsequently measured at fair value. The fair values are estimated based on pricing models that take into account the current market and contractual prices of the underlying instruments and other factors. Derivatives are carried as assets when their fair value is positive and as liabilities when it is negative. Gains and losses from transactions in the above instruments are reported in the statement of profit or loss as gains less losses arising from transactions in financial assets (liabilities) at fair value through profit or loss. Changes in the fair value of derivative instruments are included in gain/loss.

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

**Cash and cash equivalents.** Cash and cash equivalents consist of cash on hand and amounts due from credit institutions with original maturity of less or equal to 90 days and are free from contractual encumbrances.

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

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

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

- Communication devices and computers — 3 years;
- Office equipment — 5 years;
- Vehicles — 5 years;
- Other — 5 years.

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

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

**Intangible assets**

**Intangible assets acquired separately.** Intangible assets consists mainly of software and licenses. Intangible assets with finite useful lives that are acquired separately are carried at cost less accumulated amortization and accumulated impairment losses. Amortization is recognized on a straight-line basis over their estimated useful lives, which is estimated at 5-10 years. The estimated useful life and amortization method are reviewed at the end of each reporting period, with the effect of any changes in estimate being accounted for on a prospective basis. Intangible assets with indefinite useful lives that are acquired separately are carried at cost less accumulated impairment losses.

**Derecognition of intangible assets.** An intangible asset is derecognised on disposal, or when no future economic benefits are expected from use or disposal. Gains or losses arising from derecognition of an intangible asset, measured as the difference between the net disposal proceeds and the carrying amount of the asset, are recognized in profit or loss when the asset is derecognized.

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

Intangible assets with indefinite useful lives and intangible assets not yet available for use are tested for impairment at least annually, and whenever there is an indication that the asset may be impaired. Recoverable amount is the higher of fair value less costs to sell and value in use. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset for which the estimates of future cash flows have not been adjusted.

If the recoverable amount of an asset (or cash-generating unit) is estimated to be less than its carrying amount, the carrying amount of the asset (or cash-generating unit) is reduced to its recoverable amount. An impairment loss is recognized immediately in profit or loss, unless the relevant asset is carried at a revalued amount, in which case the impairment loss is treated as a revaluation decrease.

Where an impairment loss subsequently reverses, the carrying amount of the asset (or a cash-generating unit) is increased to the revised estimate of its recoverable amount, but so that the increased carrying amount does not exceed the carrying amount that would have been determined had no impairment loss been recognized for the asset (or cash-generating unit) in prior years. A reversal of an impairment loss is recognized immediately in profit or loss, unless the relevant asset is carried at a revalued amount, in which case the reversal of the impairment loss is treated as a revaluation increase.

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

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

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

Deferred tax liabilities are recognized for taxable temporary differences associated with property and equipment and loans to customers. Deferred tax assets arising from deductible temporary differences associated with such investments and interests are only recognized to the extent that it is probable that there will be sufficient taxable profits against which to utilize the benefits of the temporary differences and they are expected to reverse in the foreseeable future.

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

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

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

**Current and deferred tax for the year.** Current and deferred tax are recognized in profit or loss, except when they relate to items that are recognized in other comprehensive income or directly in equity, in which case, the current and deferred tax are also recognized in other comprehensive income or directly in equity respectively.

**Operating taxes.** The Republic of Armenia also has various other taxes, which are assessed on the Organization’s activities. These taxes are included as a component of operating expenses in the statement of comprehensive income.

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

The amount recognized as a provision is the best estimate of the consideration required to settle the present obligation at the end of the reporting period, taking into account the risks and uncertainties surrounding the obligation. When a provision is measured using the cash flows estimated to settle the

present obligation, its carrying amount is the present value of those cash flows (where the effect of the time value of money is material).

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

**Contingencies.** Contingent liabilities are not recognized in the statement of financial position but are disclosed unless the possibility of any outflow in settlement is remote. A contingent asset is not recognized in the statement of financial position but disclosed when an inflow of economic benefits is probable.

**Foreign currencies.** In preparing the financial statements, transactions in currencies other than the Organization's functional currency (foreign currencies) are recognized at the rates of exchange prevailing at the dates of the transactions. At the end of each reporting period, monetary items denominated in foreign currencies are retranslated at the rates prevailing at that date. Non-monetary items carried at fair value that are denominated in foreign currencies are retranslated at the rates prevailing at the date when the fair value was determined. Non-monetary items that are measured in terms of historical cost in a foreign currency are not retranslated.
Exchange differences on monetary items are recognized in profit or loss in the period in which they arise.

For the purposes of presenting these financial statements, the assets and liabilities of the Organization's operations are translated into USD using exchange rates prevailing at the end of each reporting period. Income and expense items are translated at the average exchange rates for the period, unless exchange rates fluctuate significantly during that period, in which case the exchange rates at the dates of the transactions are used. Exchange differences arising, if any, are recognized in other comprehensive income and accumulated in equity.

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

| | Average Rate | | Spot Rate | |
|---|---|---|---|---|
| | **2017** | **2016** | **December 31, 2017** | **December 31, 2016** |
| AMD/1 US Dollar | 482.39 | 480.45 | 484.10 | 483.94 |

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

**Share capital.** Contributions to share capital are recognized at cost. Costs directly attributable to the issue of new shares, other than on a business combination, are deducted from equity net of any income taxes.

**Equity reserves.** The reserves recorded in equity (other comprehensive income) on the Organization's statement of financial position is 'Foreign currency translation reserve' which is used to record exchange differences arising from the translation of figures denominated in the functional currency into presentation currency.

**Segment reporting.** An operating segment is a component of the Organization that engages in business
activities from which it may earn revenues and incur expenses (including revenues and expenses relating to transactions with other components of the Bank); whose operating results are regularly reviewed by the chief operating decision maker to make decisions about resources to be allocated to the segment and assess its performance, and for which discrete financial information is available.

The Organization's operations are highly integrated and constitute a single business segment for the purposes of IFRS 8 Operating Segments. Management does not review separately the operating results of any of the components of the Bank. Assets are concentrated primarily in the Republic of Armenia, and the majority of revenues and profit is derived from operations in, and connected with, the Republic of Armenia. The Chief Operating Decision Maker, in the case of the Organization, the Board of Directors, only receives and reviews the information on the Organization as a whole.

## 3. Critical accounting judgments and key sources of estimation uncertainty

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

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

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

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

The Organization uses a combination of individual assessment and group assessment in determining the allowance for impairment required at any reporting date.

Loans and receivables with outstanding balance greater than 0.5% of outstanding amount of total portfolio as of date of measurement are considered individually significant, when such loans exist, individual assessment is performed on loans and receivables. The Organization uses management's judgment to estimate the amount of any impairment loss in cases where a borrower has financial difficulties and there are few available sources of historical data relating to similar borrowers.

Individually significant loans and receivables that are not impaired, as well as all other loans and receivables that have not been individually assessed are then included in the group of loans and receivables that are collectively assessed for impairment. The collectively assessed loans and receivables are grouped based on similar credit risk characteristics and on their past-due status and assessed accordingly. The Organization estimates changes in future cash flows based on past performance, past customer behavior, observable data indicating an adverse change in the payment status of borrowers in a group, and economic conditions that correlate with defaults on assets in the group. Management uses estimates based on historical loss experience for assets with credit risk characteristics and objective evidence of impairment similar to those in the group of loans. The Organization uses management's judgment to adjust observable data for a group of loans to reflect current circumstances not reflected in historical data. The collectively assessed methodology strives to ensure the allowance for impairment reflects the loss events that have occurred, but have not yet been identified on an individual basis.

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

As at December 31, 2017 and 2016 the gross loans totaled USD 51,497,026 and USD 54,980,905 respectively, and allowance for impairment losses amounted to USD 897,375 and USD 1,223,274 respectively. Included in loans at December 31, 2017 and 2016 are renegotiated loans in the amount of USD 1,843,693 and USD 2,841,639 and allowance for impairment of USD 261,964 and USD 406,254, respectively.

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

**Functional currency.** Despite the fact that the Organization receives its' financing in foreign currency mainly in USD, Organization's functional currency is AMD, which is the currency of the primary economic environment in which the Organization operates.

**Continued ability to raise financing.** As the Organization needs financing for its operations, as microfinance organization and as the borrowings are mainly from 1 to 3 years, the Organization assess continuality to raise finance every year.

Based on the normal ongoing business processes, the Organization is always in the ongoing negotiations and communications with the lenders, in order to renegotiate the existing loans as well as receiving new loan agreements.

## 4. Application of new and revised International Financial Reporting Standards (IFRSs)

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

In the current year, the following new and revised Standards and Interpretations have been adopted. The application of these amendments had no material impact on the disclosures or the amounts recognized in the Organization's financial statements.

- Amendments to IAS 7 *Disclosure Initiative*;
- Annual Improvements to IFRSs 2014-2016 Cycle – amendments to IFRS 12

### Amendments to IAS 7 Disclosure Initiative

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

The Organization's liabilities arising from financing activities consist of borrowings (Note 13) and certain other financial liabilities. A reconciliation between the opening and closing balances of these items is provided in note 25. Consistent with the transition provisions of the amendments, the Organization has not disclosed comparative information for the prior period. Apart from the additional disclosure in note 25, the application of these amendments has had no impact on the Organization's financial statements.

### Annual Improvements to IFRSs 2014-2016 Cycle – amendments to IFRS 12

The Group has applied the amendments to IFRS 12 included in the Annual Improvements to IFRSs 2014-2016 Cycle for the first time in the current year. The other amendments included in this package are not yet mandatorily effective and they have not been early adopted by the Organization (see the list of new and revised IFRSs in issue but not yet effective below).

IFRS 12 states that an entity need not provide summarised financial information for interests in subsidiaries, associates or joint ventures that are classified (or included in a disposal group that is classified) as held for sale. The amendments clarify that this is the only concession from the disclosure requirements of IFRS 12 for such interests.

The application of these amendments has had no effect on the Organization's financial statements.

The Organization did not early adopt any other standard, amendment or interpretation that has been issued and is not yet effective.

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

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

- IFRS 9 *Financial Instruments*[1];
- IFRS 15 *Revenue from Contracts with Customers (and the related Clarifications)*[1];
- IFRS 16 Leases[2];
- IFRIC 22 Foreign Currency Transactions and Advance Consideration[1];
- Annual Improvements to IFRSs 2015-2017 Cycle[2].

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

**IFRS 9 Financial Instruments**

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

The key requirements of IFRS 9 applicable for the Organization are:

- Classification and measurement of financial assets. All recognised financial assets that are within the scope of IFRS 9 are required to be subsequently measured at amortised cost or fair value. Specifically, debt investments that are held within a business model whose objective is to collect the contractual cash flows, and that have contractual cash flows that are solely payments of principal and interest on the principal outstanding are generally measured at amortised cost at the end of subsequent accounting periods. Debt instruments that are held within a business model whose objective is achieved both by collecting contractual cash flows and selling financial assets, and that have contractual terms that give rise on specified dates to cash flows that are solely payments of principal and interest on the principal amount outstanding, are generally measured at FVTOCI. All other debt investments and equity investments are measured at their fair value at the end of subsequent accounting periods. In addition, under IFRS 9, entities may make an irrevocable election to present subsequent changes in the fair value of an equity investment (that is not held for trading nor contingent consideration recognised by an acquirer in a business combination) in other comprehensive income, with only dividend income generally recognised in profit or loss.
- Impairment. In relation to the impairment of financial assets, IFRS 9 requires an expected credit loss model, as opposed to an incurred credit loss model under IAS 39. The expected credit loss model requires an entity to account for expected credit losses and changes in those expected credit losses at each reporting date to reflect changes in credit risk since initial recognition. In other words, it is no longer necessary for a credit event to have occurred before credit losses are recognised.

The Organization will adopt the IFRS 9 from the effective date of January 1, 2018; apply it retrospectively and recognize the cumulative effect of initially applying this standard as an adjustment to the opening balance of retained earnings as of January 1, 2018. We are continuing to evaluate the impact of this guidance on our financial statements. We expect that the application of the expected credit loss model of IFRS 9 will result in earlier recognition of credit losses for the respective items and will increase the amount of loss allowance recognised for these items.

**IFRS 15 Revenue from Contracts with Customers**

In May 2014, IFRS 15 was issued which establishes a single comprehensive model for entities to use in accounting for revenue arising from contracts with customers. IFRS 15 will supersede the current revenue recognition guidance including IAS 18 Revenue, IAS 11 Construction Contracts and the related interpretations when it becomes effective.

The core principle of IFRS 15 is that an entity should recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods and services. Specifically, the standard provides a single, principles based five-step model to be applied to all contracts with customers.

The five steps in the model are as follows:

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

Under IFRS 15, an entity recognizes revenue when or as a performance obligation is satisfied, i.e. when 'control' of the goods or services underlying the particular performance obligation is transferred to the customer. Far more prescriptive guidance has been added in IFRS 15 to deal with specific scenarios. Furthermore, extensive disclosures are required by IFRS 15.
In April 2016, the IASB issued Clarifications to IFRS 15 in relation to the identification of performance obligations, principal versus agent considerations, as well as licensing application guidance.

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

**IFRS 16 Leases**

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

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

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

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

As at 31 December 2017, the Organization has non-cancellable operating lease commitments of USD 109,280 thousand. IAS 17 does not require the recognition of any right-of-use asset or liability for future payments for these leases; instead, certain information is disclosed as operating lease commitments in Note 22. A preliminary assessment indicates that these arrangements will meet the definition of a lease under IFRS 16, and hence the Organization will recognise a right-of-use asset and a corresponding liability in respect of all these leases unless they qualify for low value or short-term leases upon the application of IFRS 16.

The new requirement to recognise a right-of-use asset and a related lease liability is expected to have a significant impact on the amounts recognised in the Organization's financial statements and the

management is currently assessing its potential impact. It is not practicable to provide a reasonable estimate of the financial effect until the management completes the review.

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

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

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

The Interpretation is effective for annual periods beginning on or after 1 January 2018 with earlier application permitted. Entities can apply the Interpretation either retrospectively or prospectively. Specific transition provisions apply to prospective application. The management of the Organization does not anticipate that the application of these amendments will have a significant effect on the financial statements.

**Annual improvements to IFRSs 2015 – 2017 Cycle**

Annual Improvements to IFRSs 2015-2017 Cycle makes amendments to several standards.
The amendments to IFRS 3 clarify that when an entity obtains control of a business that is a joint operation, it remeasures previously held interests in that business. The amendments to IFRS 11 clarify that when an entity obtains joint control of a business that is a joint operation, the entity does not remeasure previously held interests in that business.

The amendments to IAS 12 clarify that all income tax consequences of dividends (i.e. distribution of profits) should be recognised in profit or loss, regardless of how the tax arises.

The amendments to IAS 23 clarify that if any specific borrowing remains outstanding after the related asset is ready for its intended use or sale, that borrowing becomes part of the funds that an entity borrows generally when calculating the capitalisation rate on general borrowings.

All amendments are effective for annual periods beginning on or after 1 January 2019.

The management of the Organization does not anticipate that the application of these amendments will have a significant effect on the financial statements.

## 5. Cash and cash equivalents

| | December 31, 2017 | December 31, 2016 |
|---|---|---|
| Cash on hand | 660,818 | 882,983 |
| Correspondent accounts | 300,919 | 206,656 |
| Time deposits with original maturities up to 90 days | 279,000 | 1,529,907 |
| **Total cash and cash equivalents** | **1,240,737** | **2,619,546** |

As at December 31, 2017 correspondent accounts are held with resident commercial banks, with 67.60% of the balance held at two resident commercial banks. As at December 31, 2017 the Organization has not had any holdings in a single financial institution whose balance exceeded 10% of equity (December 31 2016: USD 1,534,567).

## 6. Financial instruments at fair value through profit or loss

The Organization has entered into various currency swaps. Such derivative financial instruments are subsequently measured at fair value. Derivatives are carried as assets when their fair value is positive and as liabilities when the fair value is negative.

At reporting date financial assets/liabilities at fair value through profit or loss comprise:

| | Fair value | | Notional amount | | Weighted average exchange rates | |
|---|---|---|---|---|---|---|
| **Assets** | **December 31, 2017** | **December 31, 2016** | **2017** | **2016** | **2017** | **2016** |
| *Buy AMD Sell USD* | | | | | | |
| - less than 1 month | 3,057 | - | 500,289 | - | 486.78 | - |
| - from 1 to 2 months | - | - | - | - | - | - |
| | **3,057** | **-** | **500,289** | **-** | | |
| **Liabilities** | | | | | | |
| *Buy USD Sell AMD* | | | | | | |
| - less than 1 month | (29,634) | - | 363,290 | - | 478.91 | - |
| *Buy AMD Sell USD* | | | | | | |
| - less than 1 month | (3,310) | - | 920,333 | - | 482.18 | - |
| - from 1 to 3 months | - | (28,291) | - | 1,985,287 | 481.2 | 480.38 |
| - from 1 to 2 years | - | (92,257) | - | 1,187,527 | - | 478.91 |
| | **(32,944)** | **(120,548)** | **1,283,623** | **3,172,814** | | |

None of these financial assets/liabilities are either past due or impaired.

## 7. Available-for-sale financial assets

As at December 31, 2017 available-for-sale financial assets of USD 2,694,745 were comprised of Eurobonds of the Ministry of Finance of the Republic of Armenia (December 31, 2016: USD 2,620,655). As at December 31, 2017 these assets were pledged against Organization's liabilities under repurchase agreements, see note 12. The Eurobonds bear 6.90% (1 Eurobond) nominal interest and mature in the year of 2020.

## 8. Loans to customers

| | December 31, 2017 | December 31, 2016 |
|---|---|---|
| Loans to customers | 51,497,026 | 54,980,905 |
| Less: allowance for impairment losses | (897,375) | (1,223,274) |
| **Total loans to customers** | **50,599,651** | **53,757,631** |

Loans to customers per products are presented below:

| | December 31, 2017 | December 31, 2016 |
|---|---|---|
| Individual business loans | 21,991,477 | 25,282,063 |
| Consumer loans | 3,005,017 | 439,003 |
| Individual rural loans | 26,493,550 | 28,424,568 |
| Group loans* | 2,110 | 453,441 |
| Rural group loans* | 4,872 | 381,830 |
| **Gross loans to customers** | **51,497,026** | **54,980,905** |
| Less: allowance for impairment losses | (897,375) | (1,223,274) |
| **Total loans to customers** | **50,599,651** | **53,757,631** |

*These represent Group and Rural group loans that the Organization does not provide any longer as a separate product line. The balances as at reporting date represent the remaining balances of the respective product portfolio.

Starting from January 2016, the Organization provides consumer loans to individuals in addition to business and entrepreneur purposes.

Loans to customers per industry groups are presented below:

| | December 31, 2017 | December 31, 2016 |
|---|---|---|
| Agriculture | 26,735,215 | 29,125,989 |
| Trade | 10,032,878 | 12,008,695 |
| Production | 2,733,646 | 3,157,278 |
| Transport | 1,939,338 | 2,399,595 |
| Construction | 1,005,383 | 1,407,404 |
| Other | 9,050,566 | 6,881,994 |
| **Gross loans to customers** | **51,497,026** | **54,980,905** |
| Less: allowance for impairment losses | (897,375) | (1,223,274) |
| **Total loans to customers** | **50,599,651** | **53,757,631** |

The analysis of changes for loan impairment is presented in the table below:

| | Agriculture | Trade | Production | Transport | Construction | Other | Total |
|---|---|---|---|---|---|---|---|
| **January 1, 2016** | **375,806** | **278,152** | **85,656** | **42,216** | **28,589** | **142,023** | **952,442** |
| Additional provisions recognized | 1,379,446 | 577,806 | 162,733 | 178,279 | 79,842 | 327,185 | 2,705,291 |
| Write off of assets | (1,309,574) | (749,514) | (243,572) | (163,216) | (92,638) | (438,678) | (2,997,192) |
| Recovery of assets previously written off | 142,437 | 195,517 | 77,484 | 20,385 | 18,668 | 110,586 | 565,077 |
| Effects of foreign currency exchange Difference | (1,679) | (281) | (10) | (272) | (54) | (48) | (2,344) |
| **December 31, 2016** | **586,436** | **301,680** | **82,291** | **77,392** | **34,407** | **141,068** | **1,223,274** |
| Additional provisions recognized | 854,881 | 174,134 | 66,258 | 59,957 | 56,590 | 135,631 | 1,347,451 |
| Write off of assets | (1,243,454) | (563,440) | (153,670) | (165,576) | (90,419) | (308,593) | (2,525,152) |
| Recovery of assets previously written off | 257,942 | 288,020 | 60,220 | 61,995 | 21,745 | 161,133 | 851,055 |
| Effects of foreign currency exchange Difference | 267 | 257 | 69 | 128 | 31 | (5) | 747 |
| **December 31, 2017** | **456,072** | **200,651** | **55,168** | **33,896** | **22,354** | **129,234** | **897,375** |

The table below summarizes carrying value of loans to customers analyzed by type of collateral obtained by the Organization.

| | **December 31, 2017** | | | | | | |
|---|---|---|---|---|---|---|---|
| | **Agriculture** | **Trade** | **Production** | **Transport** | **Construction** | **Other** | **Total** |
| Loans collateralized by pledge of real estate | 1,401,402 | 3,535,978 | 1,032,981 | 174,411 | 10,971 | 979,375 | 7,135,118 |
| Loans collateralized by movable property | 509,168 | 1,441,043 | 344,735 | 452,136 | 11,817 | 328,145 | 3,087,044 |
| Loans collateralized by gold | - | - | - | - | - | 53,035 | 53,035 |
| Loans collateralized by personal guarantees of individuals | 24,781,464 | 5,055,857 | 1,355,930 | 1,312,791 | 982,595 | 5,815,290 | 39,303,927 |
| Unsecured loans | 43,181 | - | - | - | - | 1,874,721 | 1,917,902 |
| | **26,735,215** | **10,032,878** | **2,733,646** | **1,939,338** | **1,005,383** | **9,050,566** | **51,497,026** |
| Less: allowance for impairment losses | (456,072) | (200,651) | (55,168) | (33,896) | (22,354) | (129,234) | (897,375) |
| **Total loans to customers at December 31, 2017** | **26,279,143** | **9,832,227** | **2,678,478** | **1,905,442** | **983,029** | **8,921,332** | **50,599,651** |

| | **December 31, 2016** | | | | | | |
|---|---|---|---|---|---|---|---|
| | **Agriculture** | **Trade** | **Production** | **Transport** | **Construction** | **Other** | **Total** |
| Loans collateralized by pledge of real estate | 1,178,431 | 3,938,275 | 918,639 | 192,266 | - | 492,904 | 6,720,515 |
| Loans collateralized by movable property | 513,760 | 5,689,714 | 1,763,739 | 1,866,820 | 1,397,107 | 5,899,248 | 17,130,388 |
| Loans collateralized by personal guarantees of individuals | 27,433,798 | 2,380,706 | 474,900 | 340,509 | 10,297 | 489,792 | 31,130,002 |
| | **29,125,989** | **12,008,695** | **3,157,278** | **2,399,595** | **1,407,404** | **6,881,944** | **54,980,905** |
| Less: allowance for impairment losses | (586,436) | (301,680) | (82,291) | (77,392) | (34,407) | (141,068) | **(1,223,274)** |
| **Total loans to customers at December 31, 2016** | **28,539,553** | **11,707,015** | **3,074,987** | **2,322,203** | **1,372,997** | **6,740,876** | **53,757,631** |

As at December 31, 2017 and 2016 all loans to customers (100% of total portfolio) are granted to individuals and companies operating in Republic of Armenia, which represents a significant geographical concentration in one region.

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

| | Gross loans | Provision for impairment | Net loans | Provision for impairment to gross loans |
|---|---|---|---|---|
| **Collectively assessed** | | | | |
| Not overdue | 50,486,652 | 349,101 | 50,137,551 | 0.69% |
| Overdue: | | | | |
| - 1 to 30 days overdue | 302,212 | 67,637 | 234,575 | 22.38% |
| - 31 to 60 days overdue | 216,323 | 103,989 | 112,334 | 48.07% |
| - 61 to 90 days overdue | 127,075 | 78,190 | 48,885 | 61.53% |
| - 91 to 180 days overdue | 364,764 | 298,458 | 66,306 | 81.82% |
| **Total loans to customers** | **51,497,026** | **897,375** | **50,599,651** | **1.74%** |

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

| | Gross loans | Provision for impairment | Net loans | Provision for impairment to gross loans |
|---|---|---|---|---|
| **Collectively assessed** | | | | |
| Not overdue | 53,369,423 | 509,559 | 52,859,864 | 0.95% |
| Overdue: | | | | |
| - 1 to 30 days overdue | 452,203 | 76,270 | 375,933 | 16.87% |
| - 31 to 60 days overdue | 341,148 | 120,071 | 221,077 | 35.20% |
| - 61 to 90 days overdue | 239,714 | 118,812 | 120,902 | 49.56% |
| - 91 to 180 days overdue | 578,417 | 398,562 | 179,855 | 68.91% |
| **Total loans to customers** | **54,980,905** | **1,223,274** | **53,757,631** | **2.22%** |

As at December 31, 2017 and 2016, the Organization did not have any individually significant borrowers.

The modification to contractual terms was a temporary modification to the contractual terms of a loan that resulted in the giving up of the right to contractual cash flows over a pre-defined period. During 2017 Organization’s Credit Risk Department performed assessment for loan restructuring applications received from customers, and 664 loans for a total amount of USD 1,779,600 were restructured (in 2016 1,133 loans for a total amount of USD 2,229,271). Total restructured loans have carrying value of USD 1,581,729 as at December 31, 2017 (December 31, 2016: USD 2,435,385).

## 9. Property and equipment

| | Leasehold improvements | Communication devices and computers | Office equipment | Vehicles | Other | Total |
|---|---|---|---|---|---|---|
| **At cost** | | | | | | |
| **January 1, 2016** | **659,955** | **511,305** | **607,328** | **158,235** | **441,996** | **2,378,819** |
| Additions | 27,366 | 54,553 | 32,001 | - | 19,260 | 133,180 |
| Disposals | (25,928) | (753) | (3,782) | - | (4,600) | (35,063) |
| Transfers | (258) | (42) | 747 | - | (447) | - |
| Foreign currency translation difference | (266) | (590) | (449) | (62) | (275) | (1,642) |
| **December 31, 2016** | **660,869** | **564,473** | **635,845** | **158,173** | **455,934** | **2,475,294** |
| Additions | 13,995 | 69,203 | 22,357 | - | 13,730 | 119,285 |
| Disposals | (1,119) | (35,878) | (12,722) | - | (32,043) | (81,762) |
| Transfer | 1,280 | (45) | (184) | - | (1,051) | - |
| Foreign currency translation difference | (264) | (296) | (241) | (53) | (88) | (942) |
| **December 31, 2017** | **674,761** | **597,457** | **645,055** | **158,120** | **436,482** | **2,511,875** |
| **Accumulated depreciation** | | | | | | |
| **January 1, 2016** | **272,004** | **427,132** | **357,019** | **130,741** | **246,590** | **1,433,486** |
| Depreciation charge | 70,769 | 62,529 | 96,528 | 20,980 | 75,517 | 326,323 |
| Disposals | (19,157) | (753) | (3,016) | - | (4,459) | (27,385) |
| Foreign currency translation difference | (502) | (205) | (756) | (202) | (1,053) | (2,718) |
| **December 31, 2016** | **323,114** | **488,703** | **449,775** | **151,519** | **316,595** | **1,729,706** |
| Depreciation charge | 72,039 | 57,607 | 87,715 | 6,675 | 65,770 | 289,806 |
| Transfers | 75 | 35 | 479 | - | (589) | - |
| Disposals | (549) | (35,764) | (11,254) | - | (30,880) | (78,447) |
| Foreign currency translation difference | (360) | (238) | (421) | (74) | (225) | (1,318) |
| **December 31, 2017** | **394,319** | **510,343** | **526,294** | **158,120** | **350,671** | **1,939,747** |
| **Net book value** | | | | | | |
| **As at December 31, 2017** | **280,442** | **87,114** | **118,761** | **-** | **85,811** | **572,128** |
| **As at December 31, 2016** | **337,755** | **75,770** | **186,070** | **6,654** | **139,339** | **745,588** |
| **As at January 1, 2016** | **387,951** | **84,173** | **250,309** | **27,494** | **195,406** | **945,333** |

As at December 31, 2017 and 2016, the cost of fully depreciated assets that are still in use comprised USD 1,020,280 and USD 724,018 respectively.
The Organization did not have any pledged property and equipment as at December 31, 2017 and 2016.

## 10. Intangible assets

| | Software | Total |
|---|---|---|
| **At cost** | | |
| **January 1, 2016** | **604,901** | **604,901** |
| Additions | 179,915 | 179,915 |
| Foreign currency translation difference | (1,535) | (1,535) |
| **December 31, 2016** | **783,281** | **783,281** |
| Additions | 127,260 | 127,260 |
| Foreign currency translation difference | (717) | (717) |
| **December 31, 2017** | **909,824** | **909,824** |
| **Accumulated amortization** | | |
| **January 1, 2016** | **140,845** | **140,845** |
| Amortization charge | 74,389 | 74,389 |
| Foreign currency translation difference | (592) | (592) |
| **December 31, 2016** | **214,642** | **214,642** |
| Amortization charge | 99,469 | 99,469 |
| Foreign currency translation difference | (422) | (422) |
| **December 31, 2017** | **313,689** | **313,689** |
| **Net book value** | | |
| **As at December 31, 2017** | **596,135** | **596,135** |
| **As at December 31, 2016** | **568,639** | **568,639** |
| **As at January 1, 2016** | **464,056** | **464,056** |

As at December 31, 2017 and 2016, the cost of fully depreciated intangible assets that are still in use comprised USD 50,524 and USD 30,130 respectively. The Organization did not have any pledged intangible assets as at 31 December, 2017 and 2016.

## 11. Other assets

| | December 31, 2017 | December 31, 2016 |
|---|---|---|
| Prepayment for the purchase of property and equipment | 83,348 | - |
| Prepayments for the goods and services | 77,546 | 75,826 |
| Receivables from payment transfer organizations | 37,872 | 12,582 |
| Inventory | 36,439 | 20,947 |
| Other | 16,119 | 10,724 |
| **Total other assets** | **251,324** | **120,079** |

## 12. Liabilities under repurchase agreements

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

At December 31, 2017 the Organization’s liabilities for repurchase agreements signed with entities in the financial services sector amounted to USD 2,547,803 (December 31, 2016: USD 2,473,024). As at December 31, 2017 the fair value of financial assets, which comprise of Eurobond of the Ministry of Finance of Republic of Armenia, given as collateral against these liabilities amounted to USD 2,694,745 (as of December 31, 2016: USD 2,620,655), see note 7.

## 13. Borrowed funds

| | Currency | Maturity | Nominal interest rate % | December 31, 2017 | Nominal interest rate % | December 31, 2016 |
|---|---|---|---|---|---|---|
| Loans from banks and financial institutions | USD | 1-4 years | 6.20-7.80% | 26,604,600 | 6.20-8.00% | 34,496,621 |
| Loans from banks and financial institutions | AMD | 2 years | 12.25% | 1,977,550 | 11.60%-22.22% | 7,501,820 |
| Loans from non-financial legal entities | USD | 1 year | 5.50% | 501,984 | 6.25% | 1,004,563 |
| The central bank loans obtained from international programs | AMD | 5 year | 6.25-6.75% | 448,252 | 6.75% | 450,397 |
| | | | | **29,532,386** | - | **43,453,401** |

As at December 31, 2017 the Organization has borrowings from seven financial institutions (December 31 2016: nine financial institutions) whose balances each exceed 10% of equity. The value of these balances as at December 31, 2017 is USD 26,076,126 (December 31 2016: USD 41,556,917). These liabilities are measured at amortized cost.

The Organization is obligated to comply with financial covenants in relation to borrowed funds. These covenants include stipulated ratios, debt to equity ratios and various other financial performance ratios.

As at December 31, 2017, the Organization has no breach of financial performance related ratios (as at December 31, 2016: one breach in respect of one lender agreement).

## 14. Debt securities issued

| | Currency | Maturity | Coupon rate % | December 31, 2017 | December 31, 2016 |
|---|---|---|---|---|---|
| Debt securities issued | USD | 2 years | 7.50% | 4,106,989 | - |
| Debt securities issued | AMD | 2 years | 12.75% | 3,166,607 | - |
| | | | | **7,273,596** | **-** |

## 15. Other liabilities

| | December 31, 2017 | December 31, 2016 |
|---|---|---|
| **Other financial liabilities** | | |
| Payables for services | 200,874 | 222,538 |
| Payables to employees | 17,994 | 74,241 |
| Payables for contractual obligations | - | 40,708 |
| | **218,868** | **337,487** |
| **Other non-financial liabilities** | | |
| Vacation reserve | 398,759 | 337,629 |
| Taxes payable, other than income tax | 226,205 | 226,443 |
| Other | 71,469 | 5,698 |
| | **696,433** | **569,770** |
| **Total other liabilities** | **915,301** | **907,257** |

## 16. Equity

As at December 31, 2017 and 2016 Organization's registered, issued, outstanding and fully paid share capital consisted of 490,596 ordinary shares respectively with par value of AMD 10,000 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 the annual and general meetings of the Organization.

The share capital of the Organization was contributed by the shareholders in AMD and they are entitled to dividends and any capital distribution in AMD.

The Organization's distributable reserves among shareholders are limited to the amount of its accumulated retained earnings as disclosed in its statutory accounts. Non-distributable reserves are represented by a reserve fund, which is created as required by the statutory regulations. The reserve fund of the Organization is formed by compulsory annual deductions in the amount of 5% from net profits of the Organization until the fund reaches 15% of its Share capital. The reserve fund may be used to cover losses of the Organization, as well as for the retirement of debentures and redemption of stock of the Organization in the event that no other funds are available. The reserve fund shall not be used for any other purposes.

In 2017 the Organization declared and paid dividends USD 1,175,309 (2016: None).

## 17. Net interest income

| | 2017 | 2016 |
|---|---|---|
| **Interest income:** | | |
| Interest income on financial assets recorded at amortized cost | | |
| - loans to customers | 15,519,422 | 17,240,320 |
| - cash and cash equivalents | 32,440 | 151,943 |
| | **15,551,862** | **17,392,263** |
| Interest income on financial instruments at fair value through profit or loss | 57,700 | 42,662 |
| Interest income on available-for-sale financial assets | 156,719 | 154,988 |
| **Total interest income** | **15,766,281** | **17,589,913** |
| **Interest expense:** | | |
| Interest expense on financial liabilities recorded at amortized cost | | |
| - borrowed funds | 2,723,843 | 4,653,470 |
| - subordinated debt | - | 286,409 |
| - debt securities issued | 527,060 | - |
| - repurchase agreements | 71,885 | 124,191 |
| | **3,322,788** | **5,064,070** |
| Interest expense on financial instruments at fair value through profit or loss | 197,264 | 685,654 |
| **Total interest expense** | **3,520,052** | **5,749,724** |
| **Net interest income before impairment losses on interest bearing assets** | **12,246,229** | **11,840,189** |

## 18. Net gain from foreign exchange operations

| | 2017 | 2016 |
|---|---|---|
| Gain from foreign exchange trading, net | 220,988 | 230,755 |
| Foreign exchange translation (loss)/gain, net | (8,568) | 3,536 |
| **Total net gain from foreign exchange operations** | **212,420** | **234,291** |

## 19. Staff costs

| | 2017 | 2016 |
|---|---|---|
| Salaries, bonuses and other employee benefits | 4,296,613 | 4,401,428 |
| Training costs | 16,466 | 14,226 |
| **Total staff cost** | **4,313,079** | **4,415,654** |

## 20. Other operating expenses

| | 2017 | 2016 |
|---|---|---|
| Royalty and management fee | 1,528,813 | 1,569,252 |
| Operating leases | 685,344 | 690,596 |
| Information technology expenses | 248,859 | 278,916 |
| Insurance | 173,729 | 197,105 |
| Taxes, other than income tax | 110,473 | 77,688 |
| Utilities | 95,058 | 134,882 |
| Communications | 92,299 | 88,144 |
| Office supplies | 88,753 | 108,151 |
| Professional services | 87,210 | 87,745 |
| Business trip expense | 83,270 | 50,176 |
| Loan collection expenses | 81,083 | 25,607 |
| Security expenses | 52,914 | 60,214 |
| Representative expenses | 44,524 | 33,202 |
| Property and equipment maintenance | 43,843 | 67,613 |
| Early redemption fees on borrowed funds | 34,621 | 670 |
| Advertising costs | 12,632 | 3,611 |
| Loss on disposal of property and equipment | 3,315 | 7,678 |
| Other expenses | 347,877 | 305,594 |
| | **3,814,617** | **3,786,844** |

## 21. Income tax

The Organization measures and records its current income tax payable and its tax bases in its assets and liabilities in accordance with the tax regulations of the Republic of Armenia, which differ from IFRS.

The Organization is subject to certain permanent tax differences due to the non-tax deductibility of certain expenses and certain income being treated as non-taxable for tax purposes.

Deferred taxes reflect the net tax effects of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for tax purposes. Temporary differences as at December 31, 2017 and 2016 relate mostly to different methods/timing of income and expense recognition as well as to temporary differences generated by tax – book bases' differences for certain assets.

The tax rate used for the reconciliations below is the corporate tax rate of 20% payable by corporate entities in the Republic of Armenia on taxable profits (as defined) under tax law of the Republic of Armenia.

Temporary differences as at December 31, 2017 and 2016 comprise:

| | December 31, 2017 | December 31, 2016 |
|---|---|---|
| *Deferred tax assets/ (liabilities) in relation to:* | | |
| Available-for-sale assets | (35,472) | (22,019) |
| Loans to customers | (78,244) | 1,668 |
| Property and equipment | 47,866 | 17,920 |
| Other assets | (3,146) | (3,598) |
| Borrowed funds | (11,601) | (21,230) |
| Other liabilities | 95,322 | 87,186 |
| **Net deferred tax asset** | **14,725** | **59,927** |

| | 2017 | 2016 |
|---|---|---|
| Profit before income tax | 3,374,109 | 1,558,153 |
| Tax at the statutory tax rate (20%) | 674,822 | 311,631 |
| Tax effect of permanent differences | 20,365 | 14,159 |
| Prior years related current tax expense | 3,221 | - |
| Recognition of previously unrecognized deferred tax on property | (17,992) | - |
| **Income tax expense** | **680,416** | **325,790** |
| | | |
| Current income tax expense | 645,359 | 114,501 |
| Current income tax expense – prior years | 3,221 | - |
| Deferred tax expense recognized in the current year profit or loss | 31,836 | 211,289 |
| **Income tax expense** | **680,416** | **325,790** |

| | 2017 | 2016 |
|---|---|---|
| **Deferred income tax assets** | | |
| As at January 1 – deferred tax assets | 59,927 | 302,359 |
| Changes in deferred tax balances recognized in profit or loss | (31,836) | (211,289) |
| Changes in deferred tax balances recognized in other comprehensive income | (13,508) | (32,786) |
| Effect of foreign currency exchange difference | 142 | 1,643 |
| **As at December 31- deferred tax assets** | **14,725** | **59,927** |

## 22. Commitments and contingencies

In the normal course of business, the Organization is a party to financial instruments with off-balance sheet risk in order to meet the needs of its customers. These instruments, involving varying degrees of credit risk, are not reflected in the statement of financial position. The Organization's uses the same credit control and management policies in undertaking off-balance sheet commitments as it does for on-balance operations.

The Organization has no provision for losses on contingent liabilities as at December 31, 2017 and 2016.

**Capital commitments.** As at December 31, 2017 the Organization had capital commitments of USD 194,478 with respect to acquisition of fixed and intangible assets (December 31, 2016: none).

**Operating lease commitments.** The Organization leases a number of offices under operating leases. The leases typically run for a period of 3-5 years. Lease payments are reviewed every 2-3 years to reflect market rentals. Some leases provide for additional rent payments that are based on changes in a local price index.

Where the Organization is the lessee, the future minimum lease payments under non-cancellable operating leases of rented offices are as follows:

| | December 31, 2017 | December 31, 2016 |
|---|---|---|
| Less than 1 year | 109,280 | 110,113 |
| **Total operating lease commitments** | **109,280** | **110,113** |

**Legal proceeding.** In the ordinary course of business, the Organization is subject to legal actions and complaints. Management believes that the ultimate liability arising from such actions or complaints will not have a material adverse effect on the financial condition or the results of future operations of the Organization and has adequately provisioned for in these financial statements.

**Taxation**. Commercial legislation of the Republic of Armenia, including tax legislation, may allow more than one interpretation. In addition, there is a risk of tax authorities making arbitrary judgments of business activities. If a particular treatment, based on management's judgment of the Organization's business activities, was to be challenged by the tax authorities, the Organization may be assessed additional taxes, penalties and interest. Generally, taxpayers are subject to tax audits with respect to three calendar years preceding the year of the audit.

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

Adverse changes arising from systemic risks in global financial systems, including any tightening of the credit environment could slow or disrupt the Republic of Armenia's economy, may adversely affect the

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

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

## 23. Transactions with related parties

| | As at December 31, 2017 | | As at December 31, 2016 | |
|---|---|---|---|---|
| | **Related party balances** | **Total category as per the financial statements caption** | **Related party balances** | **Total category as per the financial statements caption** |
| ***Statement of financial position*** | | | | |
| **Other liabilities (note 15)** | | | | |
| *Comprised of balances with:* | (86,228) | (915,301) | (111,175) | (907,257) |
| *- the parent* | (86,228) | - | (107,290) | - |
| *- other related parties* | - | - | (3,885) | - |

| | 2017 | | 2016 | |
|---|---|---|---|---|
| | **Related party transactions** | **Total category as per the financial statements caption** | **Related party transactions** | **Total category as per the financial statements caption** |
| ***Statement of profit or loss*** | | | | |
| **Other operating income** | - | - | 76,320 | 112,737 |
| **Interest expense (note 17)** | 85,370 | 3,520,052 | - | - |
| **Other operating expenses (note 20)** | 1,777,672 | 3,814,617 | 1,923,280 | 3,786,844 |
| *Comprised of transactions with:* | | | | |
| *- the parent (royalty and management fees)* | 1,528,813 | - | 1,569,252 | - |
| *- other related parties (IT and other services)* | 248,859 | - | 278,916 | - |

| | 2017 | | 2016 | |
|---|---|---|---|---|
| | **Related party balances** | **Total category as per the financial statements caption** | **Related party balances** | **Total category as per the financial statements caption** |
| **Key management personnel compensation(note 19)** | | | | |
| *- Short-term employee benefits* | 343,235 | 4,313,079 | 336,545 | 4,415,654 |

As at December 31, 2017 and 2016 the Organization's key management personnel consisted of 3 positions.

## 24. Fair value of financial instruments

IFRS defines fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. The estimates presented herein are not necessarily indicative of the amounts the Organization could realize in a market exchange from the sale of its full holdings of a particular instrument.

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

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

| Financial assets/ Liabilities | Fair value as at December 31, 2017 | Fair value as at December 31, 2016 | Fair value hierarchy | Valuation technique(s) and key input(s) | Significant unobservable input(s) | Relationship of unobservable inputs to fair value |
|---|---|---|---|---|---|---|
| Financial assets at fair value through profit or loss: - currency swaps | 3,057 | - | Level 3 | Discounted cash flows, Future cash flows are estimated based on forward exchange rates and contract forward rates, discounted at a rate that reflects the credit risk of various counterparties | Forward exchange rates, determined using a combination of purchasing power parity and interest rate parity | The higher the forward exchange rates the higher the fair value |
| Available for sale financial assets | 2,694,745 | 2,620,655 | Level 2 | Quoted bid prices in a market. | N/A | N/A |
| Financial liabilities at fair value through profit or loss: - currency swaps | (32,944) | (120,548) | Level 3 | Discounted cash flows, Future cash flows are estimated based on forward exchange rates and contract forward rates, discounted at a rate that reflects the credit risk of various counterparties | Forward exchange rates, determined using a combination of purchasing power parity and interest rate parity | The higher the forward exchange rates the higher the fair value |

The reconciliation of Level 3 fair value measurements of financial assets is presented as follows:

| | 2017 | | 2016 |
|---|---|---|---|
| | Financial liabilities at fair value through profit or loss | Financial assets at fair value through profit or loss | Financial liabilities at fair value through profit or loss |
| **At January 1** | **(120,548)** | **-** | **(181,596)** |
| Total gains or losses: | | | |
| - in profit or loss | (127,453) | 3,057 | (664,765) |
| Settlements | 215,340 | - | 726,185 |
| Foreign currency translation difference | (283) | - | (372) |
| **At December 31** | **(32,944)** | **3,057** | **(120,548)** |

**Fair value of financial assets and financial liabilities that are not measured at fair value on a recurring basis.** Because of the short-term nature of most financial assets and financial liabilities, management believes that their carrying amounts approximate their fair values. For certain other financial assets and financial liabilities, management uses discounted cash flows to estimate fair values. Interest rates used to discount these estimated cash flows are based on the government bond yield curve at the reporting date plus currency, maturity of the instrument and credit risk of the counterparty.

| | December 31, 2017 | | December 31, 2016 | |
|---|---|---|---|---|
| | Carrying amount | Fair value | Carrying amount | Fair value |
| **Financial assets** | | | | |
| *Loans and receivables:* | **50,599,651** | **53,965,152** | **53,757,631** | **54,980,905** |
| - Loans to customers, gross | 50,599,651 | 53,965,152 | 53,757,631 | 54,980,905 |
| **Financial liabilities** | | | | |
| *Financial liabilities held at amortised cost:* | **36,805,982** | **36,982,896** | **43,453,401** | **43,453,401** |
| - Borrowings received | 29,532,386 | 29,575,418 | 43,453,401 | 43,453,401 |
| - Debt securities issued | 7,273,596 | 7,407,478 | - | - |

| | Fair value hierarchy as at December 31, 2017 | | | |
|---|---|---|---|---|
| | Level 1 | Level 2 | Level 3 | Total |
| ***Financial assets*** | | | | |
| *Loans and receivables:* | | | | |
| - Loans to customers | - | - | 53,965,152 | 53,965,152 |
| **Total** | - | - | **53,965,152** | **53,965,152** |
| ***Financial liabilities*** | | | | |
| *Financial liabilities held at amortised cost:* | | | | |
| - Borrowings received | - | - | 29,575,418 | 29,575,418 |
| - Debt securities issued | - | 7,407,478 | - | 7,407,478 |
| **Total** | - | **7,407,478** | **29,575,418** | **36,982,896** |

| | Fair value hierarchy as at December 31, 2016 | | | |
|---|---|---|---|---|
| | Level 1 | Level 2 | Level 3 | Total |
| ***Financial assets*** | | | | |
| *Loans and receivables:* | | | | |
| - Loans to customers | - | - | 54,980,905 | 54,980,905 |
| **Total** | - | - | **54,980,905** | **54,980,905** |
| ***Financial liabilities*** | | | | |
| *Financial liabilities held at amortised cost:* | | | | |
| - Borrowings received | - | - | 43,453,401 | 43,453,401 |
| **Total** | - | - | **43,453,401** | **43,453,401** |

## 25. Reconciliation of liabilities arising from financing activities

| | January 1, 2017 | Proceeds /repayments - cash flows | Interest payment | Non-cash changes: Interest expense | Non-cash changes: Foreign currency revalua-tion | Origina-tion fees | December 31, 2017 |
|---|---|---|---|---|---|---|---|
| Borrowed funds | 43,453,401 | (13,791,311) | (2,860,106) | 2,723,843 | 66,535 | (59,976) | 29,532,386 |
| Debt securities issued | - | 7,147,281 | (346,995) | 527,060 | (50,100) | (3,650) | 7,273,596 |
| | **43,453,401** | **(6,644,030)** | **(3,207,101)** | **3,250,903** | **16,435** | **(63,626)** | **36,805,982** |

## 26. Capital risk management

The Organization manages its capital to ensure that the Organization will be able to continue as a going concern while maximizing the return to stakeholders through the optimization of the debt and equity balance.

The CBA sets and monitors capital requirements for the Organization. Under the current capital requirements set by the CBA, universal credit organizations as at December 31, 2017 have to maintain a minimum share capital of AMD 150,000 thousand, equivalent to USD 309,853 (December 31, 2016: USD 309,956).

As per CBA regulatory requirement, which became effective in 2011, credit organizations conducting foreign exchange transactions in cash other than for the purpose of accepting loan repayments; have to maintain a ratio of capital to risk weighted assets (statutory capital ratio) above the prescribed minimum level. In 2013 the Organization changed its charter so that it has the right to conduct foreign exchange cash transactions as a separate activity, thus the Organization has to measure and comply with this statutory capital requirements and capital ratio. As at December 31, 2017, total capital requirements was AMD 1,000,000 thousand, equivalent to USD 2,065,689 (December 31, 2016: USD 2,066,372) and minimum capital ratio level was 10% (December 31, 2016: 10%).

The calculation of statutory capital ratio based on requirements set by the Central Bank of Armenia is as follows:

| | December 31, 2017 Unaudited | December 31, 2016 Unaudited |
|---|---|---|
| Primary capital | 13,906,344 | 12,308,234 |
| Additional capital | 147,986 | 107,486 |
| **Total capital*** | **14,054,330** | **12,415,720** |
| **Risk weighted assets** | **53,841,973** | **55,628,346** |
| Statutory capital ratio (%) | 26% | 22% |
| Minimum required statutory capital ratios | 10% | 10% |
| **Compliance with the minimum share capital and total capital requirements** | **No breaches during the year** | **No breaches during the year** |

* Total regulatory capital has been translated to USD using the applicable rate as at 31 December 2017 and 31 December 2016 respectively.

The Management Board reviews the capital structure on a semi-annual basis. The adequacy of the Organization's capital is set and monitored using the ratios established by CBA. As a part of this review, the Board considers the cost of capital and the risks associated with each class of capital. Based on recommendations of the Board, the Organization balances its overall capital structure through payment of dividends, new share issues as well as the issue of new debt or the redemption of existing debt. In addition, the Organization manages its capital in order to meet covenant requirements.

## 27. Risk management

Management of risk is fundamental to the Organization's business and is an essential element of the Organization's operations. The main risks inherent to the Organization's operations are those related to:

- Credit exposures;
- Liquidity risk;
- Market risk.

The Organization recognizes that it is essential to have efficient and effective risk management processes in place. To enable this, the Organization has established a risk management framework, whose main purpose is to protect the Organization from risk and allow it to achieve its performance objectives.

The Board of Directors has overall responsibility for the determination of the Organization's risk management objectives, policies and oversight of the Organization's risk management framework. The overall objective of the Board of Directors is to set polices that seek to reduce risks as far as possible without unduly affecting the Organization's competitiveness and flexibility. Whilst retaining ultimate responsibility for them, it has delegated the authority for designing and operating processes that ensure the effective implementation of the objectives and policies to the Organization.
The Organization's risk management policies are established to identify and analyze the risks faced by the Organization, to set appropriate risk limits and controls, and to monitor risks and adherence to limits. Risk management policies and systems are reviewed regularly to reflect changes in market conditions, products and services offered. The Organization, through its training and management standards and procedures, aim to develop a disciplined and constructive control environment, in which all employees understand their roles and obligations.

Credit, market and liquidity risks both at the portfolio and transactional levels are managed and controlled through a system of Credit Committees and an Asset and Liability Management Committee (ALCO). Risk Committee is responsible for developing, monitoring risk management policies and exercising control over the risk in the legislation and regulatory arena and assesses its influence on the Organization's activity. This approach allows the Organization to minimize potential losses from the investment climate fluctuations in the Republic of Armenia.

### Credit risk

The Organization is exposed to credit risk which is the risk that one party to a financial instrument will fail to discharge an obligation and cause the other party to incur a financial loss.

The main business of the Organization is to provide micro-loans. Respectively credit risk is of crucial importance in the Micro Financing Organization risk management. To avoid significant financial damage caused by this the Organization uses various methods to identify and manage effectively the credit risks.

The Microfinance industry is generally exposed to credit risk through its loans to customers and bank deposits. With regard to the loans to customers this risk exposure is concentrated within the Republic of Armenia. The exposure is monitored on a regular basis to ensure that the credit limits and credit worthiness guidelines established by the Organization's risk management policy are not breached.

Risk management and monitoring is performed within set limits of authority. These processes are performed by the Credit Risk Department, Credit Committee and the Organization's Management Board. Before any application is approved by the Credit Committee, all recommendations on credit processes (borrower's limits approved, or amendments made to loan agreements, etc.) are reviewed and approved by the Credit Risk Department. Daily risk management is performed by the Head of Credit Risk Management Department.

The Organization's credit policy is determined by the number of internal policies and procedures, where all the related requirements, along with respective controls are clearly defined, including loan disbursement, monitoring of delinquent loans, etc.

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

Apart from individual customer analysis the credit portfolio is periodically assessed by the Internal Control department with regard to credit concentration and market risks.

The Credit Committee is the analytical body responsible for analyzing the information in the loan applications, assessing and reducing the credit risks as far as possible. The Credit Committee is the independent body within the Organization authorized to make the final decision about financing or rejecting the loan application.

Accuracy and correctness of information presented to the Credit Committee is the responsibility of the credit officer, who fills in the initial application after the due scrutiny of the applicant's business and its credit risks. Eventually the Credit Committee members assess the application against the established criteria (applicant's credit history, financial condition, competitive ability, etc.).
Each branch is required to implement Organization's credit policies and procedures, with credit approval authorities set by the internal regulations. Each branch manager reports on all credit related matters to Management. Each branch is responsible for the quality and performance of its credit portfolio and for monitoring and controlling all credit risks in its portfolio. Internal Audit and Internal Control Departments undertake regular audits of branches and Organization's credit processes.

The Organization's Credit Risk Department reviews ageing analysis of outstanding loans and follows up past due balances. Management therefore considers it to be appropriate to provide ageing and other information about credit risk.

The Organization structures the level 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 industry and geographical segments. Limits on the level of credit risk by a borrower and a product (by industry sector, by region) are approved periodically by the Management Board. The exposure to any one borrower is further restricted by sub-limits covering on and off-balance sheet exposures which are set by the Credit Committee. Actual exposures against limits are monitored daily to ensure that the credit limits and creditworthiness guidelines established by the Organization's risk management policy are not breached.

Where appropriate, and in the case of most loans, the Organization obtains collateral and personal guarantee. However, a significant portion of loans is personal lending, where no such facilities can be obtained. Such risks are monitored on a continuous basis and are subject to annual or more frequent reviews.

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

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

| | December 31, 2017 | December 31, 2016 |
|---|---|---|
| Loans to customers | 1,581,729 | 2,435,385 |

**Allowances for impairment.** The Organization establishes an allowance for impairment losses that represents its estimate of incurred losses in its loan portfolio. The main component of this allowance is a collective loan loss allowance established for the Organization; homogeneous assets in respect of losses that have been incurred but not been identified on loans.

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

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

| | December 31,2017 | December 31,2016 |
|---|---|---|
| Cash and cash equivalent | 579,919 | 1,736,563 |
| Financial assets at fair value through profit or loss | 3,057 | - |
| Loans to customers | 50,599,651 | 53,757,631 |
| Available-for-sale financial assets | 2,694,745 | 2,620,655 |
| Other financial assets | 37,872 | 12,582 |
| | **53,915,244** | **58,127,431** |

Above carrying amounts best represent the maximum exposure to credit risk also when taking into account of any collateral held or personal guarantees obtained. The impact of possible netting of assets and liabilities to reduce credit exposure is not significant. For the analysis of collateral held against loans to customers and concentration of credit risk in respect of loans to customers, refer to note 8.

**Off-balance sheet risk.** The Organization applies fundamentally the same risk management policies for off-balance sheet risks as it does for its on-balance sheet risks.
The geographical concentration of the Organization's assets and liabilities as at December 31, 2017 is set out below:

| | Republic of Armenia | OECD countries | Other | Total |
|---|---|---|---|---|
| **Non-derivative financial assets** | | | | |
| Cash and cash equivalents | 1,240,737 | - | - | 1,240,737 |
| Loans to customers | 50,599,651 | - | - | 50,599,651 |
| Available for sale financial assets | 2,694,745 | - | - | 2,694,745 |
| Other financial assets | 37,872 | - | - | 37,872 |
| **Total non-derivative financial assets** | **54,573,005** | **-** | **-** | **54,573,005** |
| | | | | |
| **Non-derivative financial liabilities** | | | | |
| Repurchased agreements | 2,547,803 | - | - | 2,547,803 |
| Borrowed funds | 3,363,322 | 20,210,477 | 5,958,587 | 29,532,386 |
| Debt securities issued | 7,273,596 | - | - | 7,273,596 |
| Other financial liabilities | 218,868 | - | - | 218,868 |
| **Total non-derivative financial liabilities** | **13,403,589** | **20,210,477** | **5,958,587** | **39,572,653** |
| **Net position on non-derivative financial instruments** | **41,169,416** | **(20,210,477)** | **(5,958,587)** | **15,000,352** |
| Gross settled - currency swaps | (253) | (29,634) | - | (29,887) |
| **Net position** | **41,169,163** | **(20,240,111)** | **(5,958,587)** | **14,970,465** |

**Geographical concentration.** The geographical concentration of the Organization's assets and liabilities as at December 31, 2016 is set out below:

| | Republic of Armenia | OECD countries | Total |
|---|---|---|---|
| **Non-derivative financial assets** | | | |
| Cash and cash equivalents | 2,619,546 | - | **2,619,546** |
| Loans to customers | 53,757,631 | - | **53,757,631** |
| Available-for-sale financial assets | 2,620,655 | - | **2,620,655** |
| Other financial assets | 12,582 | - | **12,582** |
| **Total non-derivative financial assets** | **59,010,414** | **-** | **59,010,414** |
| | | | |
| **Non-derivative financial liabilities** | | | |
| Repurchased agreements | 2,473,024 | - | **2,473,024** |
| Borrowed funds | 4,461,326 | 38,992,075 | **43,453,401** |
| Other financial liabilities | 337,487 | - | **337,487** |
| **Total non-derivative financial liabilities** | **7,271,837** | **38,992,075** | **46,263,912** |
| **Net position on non-derivative financial instruments** | **51,738,577** | **(38,992,075)** | **12,746,502** |
| Gross settled - currency swaps | - | (120,548) | **(120,548)** |
| **Net position** | **51,738,577** | **(39,112,623)** | **12,625,954** |

The Organization enters into numerous transactions where the counterparties that are not rated by international rating agencies. The Organization has developed internal models, which allow it to determine the creditability of counterparties.

**Liquidity risk**

**Liquidity risk management.** Liquidity risk refers to the availability of sufficient funds to meet borrowed funds withdrawals and other financial commitments associated with financial instruments as they actually fall due.

The Organization's approach to managing liquidity is to ensure, as far as possible, that it will always have sufficient liquidity to meet its liabilities when due, under both normal and stressed conditions, without incurring unacceptable losses or risking damage to the Organization's reputation.

The ALCO controls these types of risks by means of maturity analysis and determining the Organization's strategy for the next financial period. In order to manage liquidity risk, the Organization performs daily monitoring of future expected cash flows on clients' operations, which is a part of assets/liabilities management process. Current liquidity is managed by Treasurer, so Treasury maintains a portfolio of short-term liquid assets, largely made up of short-term deposits, to ensure that sufficient liquidity is maintained for current liquidity support and cash flow optimization.

An analysis of liquidity and interest rate risk is presented in the following table. The presentation below is based upon the information provided internally to key management personnel of the Organization.

| | December 31, 2017 | | | | | |
|---|---|---|---|---|---|---|
| | **Weighted average effective interest rate** | **Up to 1 month** | **1 month to 3 months** | **3 month to 1 year** | **1 year to 7 years** | **Total** |
| **Non-derivative financial assets** | | | | | | |
| *Fixed interest rate instruments* | | | | | | |
| Cash and cash equivalents | 5.52% | 366,313 | - | - | - | 366,313 |
| Loans to customers | 35.01% | 1,373,423 | 3,496,759 | 17,322,743 | 28,406,726 | 50,599,651 |
| Available for –sale financial assets | 6.43% | 2,694,745 | - | - | - | 2,694,745 |
| **Total fixed interest bearing financial assets** | | **4,434,481** | **3,496,759** | **17,322,743** | **28,406,726** | **53,660,709** |
| *Non-interest bearing financial assets* | | | | | | |
| Cash and cash equivalents | | 874,424 | - | - | - | 874,424 |
| Other financial assets | | 37,872 | - | - | - | 37,872 |
| **Total non-interest bearing financial assets** | | 912,296 | - | - | - | 912,296 |
| **Total non-derivative financial assets** | | **5,346,777** | **3,496,759** | **17,322,743** | **28,406,726** | **54,573,005** |
| **Non-derivative financial liabilities and commitments** | | | | | | |
| *Fixed interest rate instruments* | | | | | | |
| Borrowed funds | 7.41% | 38,168 | 3,702,840 | 11,392,890 | 6,049,608 | 21,183,506 |
| Debt securities issued | 10.14% | - | 107,501 | 70,233 | 7,095,862 | 7,273,596 |
| Repurchased agreements | 2.67% | 2,547,803 | - | - | - | 2,547,803 |
| **Total fixed interest bearing financial liabilities** | | **2,585,971** | **3,810,341** | **11,463,123** | **13,145,470** | **31,004,905** |
| *Variable interest rate instruments* | | | | | | |
| Borrowed funds | 9.57% | 409,097 | - | 1,012,702 | 6,927,081 | 8,348,880 |
| **Total variable interest bearing financial liabilities** | | **409,097** | **-** | **1,012,702** | **6,927,081** | **8,348,880** |
| *Non-interest bearing financial liabilities* | | | | | | |
| Other financial liabilities | | 203,995 | - | 14,873 | - | 218,868 |
| **Total non-interest bearing financial liabilities** | | **203,995** | **-** | **14,873** | **-** | **218,868** |
| **Total non-derivative financial liabilities** | | **3,199,063** | **3,810,341** | **12,490,698** | **20,072,551** | **39,572,653** |
| Interest sensitivity gap | | **1,439,413** | **(313,582)** | **4,846,918** | **8,334,175** | **14,306,924** |
| **Cumulative interest sensitivity gap** | | **1,439,413** | **1,125,831** | **5,972,749** | **14,306,924** | **28,613,848** |
| **Derivative financial instruments** | | | | | | |
| Gross settled - currency swaps | | (29,887) | - | - | - | (29,887) |
| Liquidity gap | | 2,147,714 | (313,582) | 4,832,045 | 8,334,175 | 15,000,352 |
| **Cumulative liquidity gap** | | **2,147,714** | **1,834,132** | **6,666,177** | **15,000,352** | **15,000,352** |

**Finca Universal Credit Organization Closed Joint Stock Company**



| | December 31, 2016 | | | | | |
|---|---|---|---|---|---|---|
| | **Weighted average effective interest rate** | **Up to 1 month** | **1 month to 3 months** | **3 month to 1 year** | **1 year to 7 years** | **Total** |
| **Non-derivative financial assets** | | | | | | |
| *Fixed interest rate instruments* | | | | | | |
| Cash and cash equivalents | 5.47% | 1,736,563 | - | - | - | 1,736,563 |
| Loans to customers | 35.93% | 681,192 | 4,915,946 | 21,897,785 | 26,262,708 | 53,757,631 |
| Available-for sale financial assets | 6.34% | 2,620,655 | - | - | - | 2,620,655 |
| **Total fixed interest bearing financial assets** | | **5,038,410** | **4,915,946** | **21,897,785** | **26,262,708** | **58,114,849** |
| *Non-interest bearing financial assets* | | | | | | |
| Cash and cash equivalents | | 882,983 | - | - | - | 882,983 |
| Other financial assets | | 12,582 | - | - | - | 12,582 |
| **Total non-interest bearing financial assets** | | **895,565** | **-** | **-** | **-** | **895,565** |
| **Total non-derivative financial assets** | | **5,933,975** | **4,915,946** | **21,897,785** | **26,262,708** | **59,010,414** |
| Borrowed funds | 8.72% | 2,082,484 | 2,730,148 | 8,960,867 | 22,727,836 | 36,501,335 |
| Liabilities under repurchased agreements | 3.56% | 2,473,024 | - | - | - | 2,473,024 |
| **Total fixed interest bearing financial liabilities** | | **4,555,508** | **2,730,148** | **8,960,867** | **22,727,836** | **38,974,359** |
| *Variable interest rate instruments* | | | | | | |
| Borrowed funds | 12.14% | 6,510,478 | 13,382 | 428,206 | - | 6,952,066 |
| **Total variable interest bearing financial liabilities** | | **6,510,478** | **13,382** | **428,206** | **-** | **6,952,066** |
| *Non-interest bearing financial liabilities* | | | | | | |
| Other financial liabilities | | 322,609 | - | 14,878 | - | **337,487** |
| **Total non-interest bearing financial liabilities** | | **322,609** | **-** | **14,878** | **-** | **337,487** |
| **Total non-derivative financial liabilities** | | **11,388,595** | **2,743,530** | **9,403,951** | **22,727,836** | **46,263,912** |
| Interest sensitivity gap | | ( 6,027,576) | 2,172,416 | 12,508,712 | 3,534,872 | 12,188,424 |
| **Cumulative interest sensitivity gap** | | **(6,027,576)** | **(3,855,160)** | **8,653,552** | **12,188,424** | **24,376,848** |
| **Derivative financial instruments** | | | | | | |
| Gross settled - currency swaps | | - | (28,291) | - | (92,257) | (120,548) |
| Liquidity gap | | (5,454,620) | 2,144,125 | 12,493,834 | 3,442,615 | 12,625,954 |
| **Cumulative liquidity gap** | | **(5,454,620)** | **(3,310,495)** | **9,183,339** | **12,625,954** | **12,625,954** |

**Cumulative liquidity gap**. The tables above show the expected maturity analysis of non-derivative financial assets and liabilities at their carrying amounts and based on their contractual maturities. The amounts included above for variable interest rate instruments for both non-derivative financial assets and liabilities is subject to change if changes in variable interest rates differ to those estimates of interest rates determined at the end of the reporting period. Impaired loans are included at their carrying amounts net of allowance for impairment and based on the expected timing of cash inflows. As discussed in Note 13, the Organization did not have any covenant breaches that would result in borrowed funds being classified as on demand (December 31, 2016: borrowed funds of USD 6,105,243 classified on demand).

As at December 21, 2017 the Organization has unused amount of credit lines of USD 4,565,000 (December 31, 2016: USD 4,000,000) with three local banks (December 31, 2016: two local banks). In light of the aforementioned agreements, the Organization is not expecting to experience any liquidity issues for the 2018 financial year.

The following tables detail the Organization's remaining contractual maturity for its non-derivative financial liabilities with agreed repayment periods. The tables have been drawn up based on the undiscounted cash flows of financial liabilities on the basis of their earliest possible contractual maturity. It is not expected that cash flows included in the table below could occur significantly earlier, or at significantly different amounts. The tables include both interest and principal cash flows. To the extent that interest flows are floating rate, the undiscounted amount is derived from interest rate curves at the end of the reporting period.

## Finca Universal Credit Organization Closed Joint Stock Company

### Notes to the Financial Statements for the Year Ended December 31, 2017 (continued)
***(In US Dollars, unless otherwise stated)***

| | December 31, 2017 | | | | | | |
|---|---|---|---|---|---|---|---|
| | **Weighted avrge effect. Int. rate** | **Up to 1 month** | **1 month to 3 months** | **3 months to 1 year** | **1 year to 5 years** | **Total** | **Carrying amount** |
| *Fixed interest rate instruments* | | | | | | | |
| Borrowed funds | 7.41% | 45,177 | 3,829,318 | 12,365,422 | 6,343,530 | 22,583,447 | 21,183,506 |
| Debt securities issued | 10.14% | - | 150,835 | 545,895 | 7,449,399 | 8,146,129 | 7,273,596 |
| Liabilities under repurchase agreements | 2.67% | 2,551,659 | - | - | - | 2,551,659 | 2,547,803 |
| **Total fixed interest bearing financial liabilities** | | **2,596,836** | **3,980,153** | **12,911,317** | **13,792,929** | **33,281,235** | **31,004,905** |
| *Variable interest rate instruments* | | | | | | | |
| Borrowed funds | 9.57% | 413,724 | - | 1,633,163 | 8,030,169 | 10,077,056 | 8,348,880 |
| **Total variable interest bearing financial liabilities** | | **413,724** | **-** | **1,633,163** | **8,030,169** | **10,077,056** | **8,348,880** |
| *Non-interest bearing financial liabilities* | | | | | | | |
| Other financial liabilities | | 203,995 | - | 14,873 | - | 218,868 | 218,868 |
| **Total non-interest bearing financial liabilities** | | 203,995 | - | 14,873 | - | 218,868 | 218,868 |
| **Total financial liabilities** | | **3,214,555** | **3,980,153** | **14,559,353** | **21,823,098** | **43,577,159** | **39,572,653** |

| | December 31, 2016 | | | | | | |
|---|---|---|---|---|---|---|---|
| | **Weighted avrge effect. Int. rate** | **Up to 1 month** | **1 month to 3 months** | **3 months to 1 year** | **1 year to 5 years** | **Total** | **Carrying amount** |
| *Fixed interest rate instruments* | | | | | | | |
| Borrowed funds | 8.72% | 272,189 | 6,684,151 | 14,379,603 | 15,898,109 | **37,234,052** | **36,501,335** |
| Liabilities under repurchase agreements | 3.56% | 2,473,024 | - | - | - | **2,473,024** | **2,473,024** |
| **Total fixed interest bearing financial liabilities** | | **2,745,213** | **6,684,151** | **14,379,603** | **15,898,109** | **39,707,076** | **38,974,359** |
| *Variable interest rate instruments* | | | | | | | |
| Borrowed funds | 12.14% | 10,305,602 | 31,587 | 4,162,814 | 1,886,955 | **16,386,958** | **6,952,066** |
| **Total variable interest bearing financial liabilities** | | **10,305,602** | **31,587** | **4,162,814** | **1,886,955** | **16,386,958** | **6,952,066** |
| *Non-interest bearing financial liabilities* | | | | | | | |
| Other financial liabilities | | 337,487 | - | - | - | **337,487** | **337,487** |
| **Total non-interest bearing financial liabilities** | | **337,487** | - | - | - | **337,487** | **337,487** |
| **Total financial liabilities** | | **13,388,302** | **6,715,738** | **18,542,417** | **17,785,064** | **56,431,521** | **46,263,912** |

**Market risk**

Market risk is the risk that the Organization's earnings or capital or its ability to meet business objectives will be adversely affected by changes in the level or volatility of market rates or prices. Market risk covers interest rate risk and currency risk that the Organization is exposed to. There have been no changes as to the way the Organization measures risk or to the risk it is exposed or the manner in which these risks are managed and measured.

**Interest rate risk.** The Organization's cash flow interest rate risk is the risk that the future cash flows of a financial instrument will fluctuate because of changes in the market interest rates, and the fair value interest rate risk is the risk that the value of financial instruments will fluctuate because of changes in the prevailing levels of market interest rates on both the value and cash flow risks.

**Interest rate sensitivity.** The Organization manages fair value interest rate risk through periodic estimation of potential losses that could arise from adverse changes in market conditions. The Organization's management conducts monitoring of the Organization's current financial performance, estimates the Organization's sensitivity to changes in fair value interest rates and its influence on the Organization's profitability.

The sensitivity analysis below has been determined based on the exposure to interest rates for non-derivative instruments at the end of the reporting period. For floating rate liabilities, the analysis is prepared assuming the amount of the liability outstanding at the end of the reporting period was outstanding for the whole year. A 200 basis point increase or decrease is used when reporting interest rate risk internally to key management personnel and represents management's assessment of the reasonably possible change in interest rates.

If interest rates had been 200 basis points higher/lower and all other variables were held constant, the Organization's profit for the year ended December 31, 2017 would increase /decrease by USD 84,770 and (December 31, 2016: increase/decrease by USD 102,864).

**Currency risk.** Currency risk is defined as the risk that the value of a financial instrument will fluctuate due to changes in foreign exchange rates. The Organization is exposed to the effects of fluctuations in the prevailing foreign currency exchange rates on its financial position and cash flows.

The ALCO controls currency risk by management of the open currency position on the estimated basis of USD devaluation and other macroeconomic indicators, which gives the Organization an opportunity to minimize losses from significant currency rates fluctuations toward its national currency. The Treasurer performs daily monitoring of the Organization's open currency position.
The Organization's exposure to foreign currency exchange rate risk as at December 31, 2017 is presented in the table below:

| | AMD | USD | Other | Total |
|---|---|---|---|---|
| **Non-derivative financial assets** | | | | |
| Cash and cash equivalents | 707,106 | 456,649 | 76,982 | 1,240,737 |
| Loans to customers | 17,700,552 | 32,899,099 | - | 50,599,651 |
| Available for sale financial assets | - | 2,694,745 | - | 2,694,745 |
| Other financial Assets | 37,872 | - | - | 37,872 |
| **Total non-derivative financial assets** | **18,445,530** | **36,050,493** | **76,982** | **54,573,005** |
| **Non-derivative financial liabilities** | | | | |
| Borrowed funds | 2,425,800 | 27,106,586 | - | 29,532,386 |
| Other financial liabilities | 130,349 | 88,519 | - | 218,868 |
| Debt securities issued | 3,166,608 | 4,106,988 | - | 7,273,596 |
| Repurchase agreements | - | 2,547,803 | - | 2,547,803 |
| **Total non-derivative financial liabilities** | 5,722,757 | 33,849,896 | - | 39,572,653 |
| **Open balance sheet position** | **12,722,773** | **2,200,597** | **76,982** | **15,000,352** |
| **Derivative financial instruments** | | | | |
| Gross settled - currency swaps | 987,319 | (1,017,206) | - | (29,887) |
| **Open position** | **13,710,092** | **1,183,391** | **76,982** | **14,970,465** |

The Organization's exposure to foreign currency exchange rate risk as at December 31, 2016 is presented in the table below:

| | AMD | USD | Other | Total |
|---|---|---|---|---|
| **Non-derivative financial assets** | | | | |
| Cash and cash equivalents | 1,910,650 | 621,387 | 87,509 | 2,619,546 |
| Loans to customers | 21,018,983 | 32,738,648 | - | 53,757,631 |
| Available-for-sale financial assets | - | 2,620,655 | - | 2,620,655 |
| Other financial assets | 12,582 | - | - | 12,582 |
| **Total non-derivative financial assets** | **22,942,215** | **35,980,690** | **87,509** | **59,010,414** |
| **Non-derivative financial liabilities** | | | | |
| Borrowed funds | 7,952,219 | 35,501,182 | - | 43,453,401 |
| Other financial liabilities | 185,135 | 111,644 | 40,708 | 337,487 |
| Liabilities under repurchase agreements | - | 2,473,024 | - | 2,473,024 |
| **Total non-derivative financial liabilities** | **8,137,354** | **38,085,850** | **40,708** | **46,263,912** |
| **Open balance sheet position** | **14,804,861** | **(2,105,160)** | **46,801** | **12,746,502** |
| **Derivative financial instruments** | | | | |
| Gross settled - currency swaps | (3,320,548) | 3,200,000 | - | (120,548) |
| **Open position** | **11,484,313** | **1,094,840** | **46,801** | **12,625,954** |

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

| | As at December 31, 2017 | As at December 31, 2016 |
|---|---|---|
| Impact on profit or loss | (236,678) | (218,968) |
| Impact on equity | (236,678) | (218,968) |

**Limitations of sensitivity analysis.** The above tables demonstrate the effect of a change in a key assumption while other assumptions remain unchanged. In reality, there is a correlation between the assumptions and other factors, It should also be noted that these sensitivities are non-linear, and larger or smaller impacts should not be interpolated or extrapolated from these results.

The sensitivity analyses do not take into consideration that the Organization's assets and liabilities are actively managed. Additionally, the financial position of the Organization may vary at the time that any actual market movement occurs. For example, the Organization's financial risk management strategy aims to manage the exposure to market fluctuations. As investment markets move past various trigger levels, management actions could include selling investments, changing investment portfolio allocation and taking other protective action. Consequently, the actual impact of a change in the assumptions may not have any impact on the liabilities, whereas assets are held at market value in the statement of financial position. In these circumstances, the different measurement bases for liabilities and assets may lead to volatility in shareholder equity.
Other limitations in the above sensitivity analyses include the use of hypothetical market movements to demonstrate potential risk that only represent the Organization's view of possible near-term market changes that cannot be predicted with any certainty; and the assumption that all interest rates move in an identical fashion.

**Price risks.** Price risk is the risk that the value of a financial instrument will fluctuate as a result of changes in market prices whether those changes are caused by factors specific to the individual security or its issuer or factors affecting all securities traded in the market. The Organization is exposed to price risks of its products, which are subject to general and specific market fluctuations.

The Organization manages price risk through periodic estimation of potential losses that could arise from adverse changes in market conditions and establishing and maintaining appropriate stop-loss limits and margin and collateral requirements. With respect to undrawn loan commitments, the Organization is potentially exposed to a loss of an amount equal to the total amount of such commitments. However, the likely amount of a loss is less than that, since most commitments are contingent upon certain conditions set out in the loan agreements.

**Operational risk.** Operational risk is the risk of loss arising from systems failure, human error, fraud or external events. When controls fail to perform, operational risks can cause damage to reputation, have legal or regulatory implications, or lead to financial loss. The Organization cannot expect to eliminate all operational risks, but it endeavors to manage these risks through a control framework and by monitoring and responding to potential risks. Controls include effective segregation of duties, access, authorization and reconciliation procedures, staff education and assessment processes.