

**NIKOIL OPEN JOINT
STOCK COMPANY
INVESTMENT
COMMERCIAL BANK**

Financial Statements
For the Year Ended December 31, 2014

NIKOIL OPEN JOINT STOCK COMPANY INVESTMENT COMMERCIAL BANK

TABLE OF CONTENTS

	Page
STATEMENT OF MANAGEMENT'S RESPONSIBILITIES FOR THE PREPARATION AND APPROVAL OF THE FINANCIAL STATEMENTS FOR THE YEAR ENDED DECEMBER 31, 2014	1
INDEPENDENT AUDITORS' REPORT	2
FINANCIAL STATEMENTS FOR THE YEAR ENDED DECEMBER 31, 2014:	
Statement of financial position	3
Statement of profit or loss and other comprehensive income	4
Statement of changes in equity	5
Statement of cash flows	6-7
Notes to the financial statements	
1. Organization	8
2. Significant accounting policies	8
3. Critical accounting judgements and key sources of estimation of uncertainty	17
4. Application of new and revised International Financial Reporting Standards (IFRSs)	19
5. Restatement	25
6. Cash and balances with the Central Bank of the Republic of Azerbaijan	25
7. Due from banks	26
8. Other debt securities	26
9. Loans to customers	26
10. Property and equipment	30
11. Intangible assets	31
12. Other assets	31
13. Repossessed assets	32
14. Due to banks and other financial institutions	32
15. Customer accounts	32
16. Other liabilities	33
17. Subordinated debt	33
18. Share capital	34
19. Net interest income	34
20. Allowance for impairment losses and other provisions	35
21. Net gain on foreign exchange operations	35
22. Fee and commission income and expense	36
23. Operating expenses	36
24. Income taxes	37
25. Earnings per share	37
26. Commitments and contingencies	38
27. Fair value of financial instruments	39
28. Capital risk management	40
29. Risk management policies	41
30. Transactions with related parties	53
31. Subsequent events	54

NIKOIL OPEN JOINT STOCK COMPANY INVESTMENT COMMERCIAL BANK

STATEMENT OF MANAGEMENT'S RESPONSIBILITIES FOR THE PREPARATION AND APPROVAL OF THE FINANCIAL STATEMENTS FOR THE YEAR ENDED DECEMBER 31, 2014

Management is responsible for the preparation of the financial statements that present fairly the financial position of Nikoil Open Joint Stock Company Investment Commercial Bank ("the Bank") as at December 31, 2014, and the results of its operations, cash flows and changes in 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 Bank's financial position and financial performance;
- Making an assessment of the Bank'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 Bank;
- Maintaining adequate accounting records that are sufficient to show and explain the Bank's transactions and disclose with reasonable accuracy at any time the financial position of the Bank, and which enable them to ensure that the financial statements of the Bank comply with IFRS;
- Maintaining statutory accounting records in compliance with legislation and accounting standards of the Republic of Azerbaijan;
- Taking such steps as are reasonably available to them to safeguard the assets of the Bank; and
- Preventing and detecting fraud and other irregularities.

The financial statements of the Bank for the year ended December 31, 2014 were approved by Management on May 13, 2015.

On behalf of the Management Board:

Mr. Vasiliy Khamaza
Chairman of the Management Board

May 13, 2015
Baku, the Republic of Azerbaijan



Ms. Elmira Aleskerova
Financial Director

May 13, 2015
Baku, the Republic of Azerbaijan

INDEPENDENT AUDITOR'S REPORT

To the Shareholders and Management Board of Nikoil Open Joint Stock Company Investment Commercial Bank:

We have audited the accompanying financial statements of Nikoil Open Joint Stock Company Investment Commercial Bank ("the Bank"), which comprise the statement of financial position as at December 31, 2014, and the statement of profit or loss and other comprehensive income, statement of changes in equity and statement of cash flows for the year then ended, and a summary of significant accounting policies and other explanatory information.

Management's Responsibility for the Financial Statements

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

Auditor's Responsibility

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

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

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

Opinion

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

Emphasis of matter

We draw attention to Note 5 to the financial statements which describes the restatement of corresponding figures for the year ended December 31, 2013. Our audit opinion is not qualified in that respect.



May 13, 2015
Baku, the Republic of Azerbaijan

NIKOIL OPEN JOINT STOCK COMPANY INVESTMENT COMMERCIAL BANK

STATEMENT OF FINANCIAL POSITION AS AT DECEMBER 31, 2014 (in thousands of Azerbaijan Manats)

	Notes	December 31, 2014	December 31, 2013 (restated)	December 31, 2012 (restated)
ASSETS:				
Cash and balances with the Central Bank of the Republic of Azerbaijan	6	23,013	10,745	10,581
Due from banks	7	16,700	14,234	4,470
Loans to customers	9, 30	298,141	224,256	178,752
Available-for-sale investments		304	304	304
Other debt securities	8	3,131	-	-
Deferred tax asset	24	-	1,100	1,306
Property and equipment	10	11,277	8,246	6,085
Intangible assets	11	1,764	1,534	1,170
Current income tax asset		257	507	-
Other assets	12	3,608	1,906	343
Reposessed collaterals	13	4,543	3,365	2,014
TOTAL ASSETS		362,738	266,197	205,025
LIABILITIES:				
Due to banks and other financial institutions	14, 30	64,320	36,965	40,840
Customer accounts	15, 30	240,218	172,670	131,995
Other liabilities	16	1,001	432	1,335
Deferred tax liability	24	314	-	-
Income tax payable		-	-	108
Subordinated debt	17, 30	11,888	11,897	-
TOTAL LIABILITIES		317,741	221,964	174,278
EQUITY:				
Share capital	18	34,500	34,500	22,500
Share premium		401	401	401
Retained earnings		10,096	9,332	7,846
TOTAL EQUITY		44,997	44,233	30,747
TOTAL LIABILITIES AND EQUITY		362,738	266,197	205,025

On behalf of the Management Board

Mr. Vasily Khamaza
Chairman of the Management Board

May 13, 2015
Baku, the Republic of Azerbaijan



Ms. Elmira Aleskerova
Financial Director

May 13, 2015
Baku, the Republic of Azerbaijan

The notes on pages 8-54 form an integral part of these financial statements.

NIKOIL OPEN JOINT STOCK COMPANY INVESTMENT COMMERCIAL BANK

STATEMENT OF PROFIT OR LOSS AND OTHER COMPREHENSIVE INCOME FOR THE YEAR ENDED DECEMBER 31, 2014

(in thousands of Azerbaijan Manats except for earnings per share which are in AZN)

	Notes	Year ended December 31, 2014	Year ended December 31, 2013 (restated)
Interest income	19, 30	44,235	33,974
Interest expense	19, 30	<u>(23,020)</u>	<u>(16,980)</u>
Net interest income before provision on interest bearing assets		21,215	16,994
Provision on interest bearing assets	20, 30	<u>(230)</u>	<u>(1,126)</u>
Net interest income		<u>20,985</u>	<u>15,868</u>
Net gain on foreign exchange operations	21	726	517
Fee and commission income	22	3,956	2,979
Fee and commission expense	22	(472)	(271)
Recovery of provision for impairment losses on other assets and transactions	20	95	216
Other income		<u>95</u>	<u>10</u>
Net non-interest income		<u>4,400</u>	<u>3,451</u>
Operating income		<u>25,385</u>	<u>19,319</u>
Operating expenses	23, 30	<u>(21,279)</u>	<u>(17,087)</u>
Profit before income tax		4,106	2,232
Income tax expense	24	<u>(1,856)</u>	<u>(746)</u>
Net profit for the year		2,250	1,486
Other comprehensive income		-	-
Total comprehensive income for the year		<u>2,250</u>	<u>1,486</u>
EARNINGS PER SHARE			
Basic and diluted (AZN)	25	0.13	0.11

On behalf of the Management Board:

Mr. Vasilij Khamaza
Chairman of the Management Board

May 13, 2015
Baku, the Republic of Azerbaijan



Ms. Elmira Aleskerova
Financial Director

May 13, 2015
Baku, the Republic of Azerbaijan

The notes on pages 8-54 form an integral part of these financial statements.

NIKOIL OPEN JOINT STOCK COMPANY INVESTMENT COMMERCIAL BANK

STATEMENT OF CHANGES IN EQUITY FOR THE YEAR ENDED DECEMBER 31, 2014 (in thousands of Azerbaijan Manats)

	Note	Share capital	Share premium	Retained earnings (restated)	Total equity (restated)
December 31, 2012		22,500	401	7,846	30,747
Issue of ordinary shares	18	12,000	-	-	12,000
Profit for the year		-	-	1,486	1,486
December 31, 2013		34,500	401	9,332	44,233
Dividend paid	18	-	-	(1,486)	(1,486)
Profit for the year		-	-	2,250	2,250
December 31, 2014		34,500	401	10,096	44,997

On behalf of the Management Board

Mr. Vasily Khamaza
Chairman of the Management Board

May 13, 2015
Baku, the Republic of Azerbaijan



Ms. Elmira Aleskerova
Financial Director

May 13, 2015
Baku, the Republic of Azerbaijan

The notes on pages 8-54 form an integral part of these financial statements.

NIKOIL OPEN JOINT STOCK COMPANY INVESTMENT COMMERCIAL BANK

STATEMENT OF CASH FLOWS FOR THE YEAR ENDED DECEMBER 31, 2014 *(in thousands of Azerbaijan Manats)*

	Notes	Year ended December 31, 2014	Year ended December 31, 2013 (restated)
CASH FLOWS FROM OPERATING ACTIVITIES:			
Profit before income tax		4,106	2,232
Adjustments for:			
Provision for impairment losses on interest bearing assets	20	230	1,126
Recovery of provision for impairment losses on other assets and transactions	20	(95)	(216)
Depreciation and amortization expense	23	2,098	1,473
Translation loss on foreign exchange operations	21	25	21
Change in interest accruals, net		<u>(9,413)</u>	<u>(4,303)</u>
Cash (outflow)/ inflow from operating activities before changes in operating assets and liabilities		(3,049)	333
Changes in operating assets and liabilities (Increase)/decrease in operating assets:			
Mandatory reserve deposit and other blocked accounts with the CBAR		(207)	396
Due from banks		(7,544)	(3,915)
Loans to customers		(65,166)	(43,123)
Other assets		(622)	(1,563)
Increase/(decrease) in operating liabilities:			
Due to banks and other financial institutions		27,084	(3,812)
Customer accounts		66,710	40,073
Other liabilities		<u>569</u>	<u>(648)</u>
Cash inflow/(outflow) from operating activities before taxation		17,775	(12,259)
Income tax paid		<u>(192)</u>	<u>(1,155)</u>
Net cash inflow/(outflow) from operating activities		<u>17,583</u>	<u>(13,414)</u>
CASH FLOWS FROM INVESTING ACTIVITIES:			
Payments for property, equipment and intangible assets		(6,356)	(4,027)
Payments for other debt securities		(11,016)	-
Proceeds on redemption of other debt securities		<u>7,941</u>	<u>-</u>
Net cash outflow from investing activities		<u>(9,431)</u>	<u>(4,027)</u>
CASH FLOWS FROM FINANCING ACTIVITIES:			
Proceeds from issue of ordinary shares	18	-	12,000
Dividends paid	18	(1,486)	-
Proceeds from subordinated debt	17	-	<u>11,768</u>
Net cash (outflow)/inflow from financing activities		<u>(1,486)</u>	<u>23,768</u>

NIKOIL OPEN JOINT STOCK COMPANY INVESTMENT COMMERCIAL BANK

STATEMENT OF CASH FLOWS (CONTINUED) FOR THE YEAR ENDED DECEMBER 31, 2014 *(in thousands of Azerbaijan Manats)*

	Notes	Year ended December 31, 2014	Year ended December 31, 2013 (restated)
Effect of exchange rate changes on the balance of cash held in foreign currencies		(2)	(1)
NET INCREASE IN CASH AND CASH EQUIVALENTS		6,664	6,326
CASH AND CASH EQUIVALENTS, beginning of the year	6	<u>16,941</u>	<u>10,615</u>
CASH AND CASH EQUIVALENTS, end of the year	6	<u><u>23,605</u></u>	<u><u>16,941</u></u>

Interest received and paid by the Bank during the year ended December 31, 2014 amounted to AZN 33,722 thousand and AZN 25,113 thousand, respectively.

Interest received and paid by the Bank during the year ended December 31, 2013 amounted to AZN 29,003 thousand and AZN 16,249 thousand, respectively.

On behalf of the Management Board

Mr. Vasiliy Khamaza
Chairman of the Management Board

May 13, 2015
Baku, the Republic of Azerbaijan



Ms. Elmira Aleskerova
Financial Director

May 13, 2015
Baku, the Republic of Azerbaijan

The notes on pages 8-54 form an integral part of these financial statements.

NIKOIL OPEN JOINT STOCK COMPANY INVESTMENT COMMERCIAL BANK

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED DECEMBER 31, 2014 *(in thousands of Azerbaijan Manats, unless otherwise indicated)*

1. ORGANIZATION

"Nikoil" Open Joint Stock Company Investment Commercial Bank (the "Bank") was incorporated and is domiciled in the Republic of Azerbaijan. The Bank is an open joint stock company and was set up in accordance with regulations of the Republic of Azerbaijan. The Bank's principal business activities are commercial and retail banking operations within the Republic of Azerbaijan. As at December 31, 2014 and 2013 the Bank had 20 and 17 branches, respectively, operating in the Republic of Azerbaijan.

Originally, "Ulpar" JSCB was founded in 1994 in the Republic of Azerbaijan and held general banking license No 203 issued in 1994. During 2002, "Nikoil" Closed Joint Stock Company and "Lukoil Azerbaijan" Closed Joint Stock Company acquired the controlling interest in the Bank and the Bank was renamed to "Nikoil" OJSC Investment Commercial Bank. The Bank has started operations under a full banking license No 203 issued by the Central Bank of the Republic of Azerbaijan ("CBAR") since May 2, 2002. On July 2, 2008, "Topaz Investments" LLC has acquired the controlling interest in the Bank.

The registered office of the Bank is located at 30, Pushkin Street, Baku AZ1010, Azerbaijan.

As at December 31, 2014 and 2013, the following shareholders owned the issued share capital of the Bank:

Shareholder	December 31, 2014, %	December 31, 2013, %
"Topaz Investments Limited" LLC	56.4	56.4
"Nikoil" CJSIC	42.6	33.6
"ISR Holding" LLC	1.0	1.0
"UralSib" Invest LLP	-	9.0
Total	100.0	100.0

Refer to Note 18 for the ultimate controlling party of the Bank.

These financial statements were authorized for issue on May 13, 2015 by the Management Board.

2. SIGNIFICANT ACCOUNTING POLICIES

Statement of Compliance

These financial statements have been prepared in accordance with International Financial Reporting Standards ("IFRS") issued by the International Accounting Standards Board ("IASB").

Other basis of presentation criteria

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

These financial statements are presented in thousands of Azerbaijan Manats ("AZN"), unless otherwise indicated. These financial statements have been prepared on the historical cost basis. 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 Group 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 consolidated 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 net realisable value in IAS 2 or value in use in IAS 36.

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

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

The Bank is registered in the Republic of Azerbaijan and maintains its accounting records in accordance with local accounting practice. These financial statements have been prepared from the statutory accounting records and have been adjusted to conform to IFRS.

The Bank 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 29.

Functional currency

Items included in the financial statements of Bank are measured using the currency of the primary economic environment in which the entity operates ("the functional currency"). The functional currency of the Bank is the Azerbaijani manat ("AZN"). The presentational currency of the financial statements of the Bank is the AZN. All values are rounded to the nearest thousand AZN, except when otherwise indicated.

Offsetting

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

The principal accounting policies are set out below.

Recognition of interest income

Interest income from a financial asset is recognized when it is probable that the economic benefits will flow to the Bank 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 revenue - other

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 Bank 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: 'available-for-sale' ("AFS") financial assets and 'loans and receivables'. The classification depends on the nature and purpose of the financial assets and is determined at the time of initial recognition.

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) loans and receivables, (2) held to maturity investments or (c) financial assets at fair value through profit or loss.

The fair value of AFS monetary assets denominated in a foreign currency is determined in that foreign currency and translated at the spot rate at the end of the reporting period. The foreign exchange gains and losses that are recognised in profit or loss are determined based on the amortised cost of the monetary asset. Other foreign exchange gains and losses are recognised in other comprehensive income.

AFS equity investments that do not have a quoted market price in an active market and whose fair value cannot be reliably measured are measured at cost less any identified impairment losses at the end of each reporting period.

Loans and receivables

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

Other debt securities

This classification includes unquoted non-derivative financial assets with fixed or determinable payments and fixed maturities. Management determines the classification of other debt securities at their initial recognition and reassesses the appropriateness of that classification at the end of each reporting period. Other debt securities are carried at amortised cost and are classified as loans and receivables category under IAS 39.

Impairment of financial assets

Financial assets 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 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
- It becoming probable that the borrower will enter bankruptcy or financial re-organisation; 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 Bank's past experience of collecting payments, an increase in the number of delayed payments in the portfolio, as well as observable changes in national or local economic conditions that correlate with default on receivables.

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

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

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

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

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

In respect of AFS equity securities, impairment losses previously recognized in profit or loss are not reversed through profit or loss. Any increase in fair value subsequent to an impairment loss is recognized in other comprehensive income and accumulated under the heading of available-for-sale revaluation reserve. In respect of AFS debt securities, impairment losses are subsequently reversed through profit or loss if an increase in the fair value of the investment can be objectively related to an event occurring after the recognition of the impairment loss.

Renegotiated loans

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

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 Bank and after the Bank 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. In accordance with the statutory legislation, loans may only be written off with the approval of the Supervisory Board and, in certain cases, with the respective decision of the Court.

Derecognition of financial assets

The Bank 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 Bank neither transfers nor retains substantially all the risks and rewards of ownership and continues to control the transferred asset, the Bank recognizes its retained interest in the asset and an associated liability for amounts it may have to pay. If the Bank retains substantially all the risks and rewards of ownership of a transferred financial asset, the Bank continues to recognise the financial asset and also recognises a collateralised borrowing for the proceeds received.

On derecognition of a financial asset in its entirety, the difference between the asset's carrying amount and the sum of the consideration received and receivable and the cumulative gain or 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 Bank retains an option to repurchase part of a transferred asset), the Bank 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 recognises 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 recognised and the sum of the consideration received for the part no longer recognised and any cumulative gain or loss allocated to it that had been recognised in other comprehensive income is recognized in profit or loss. A cumulative gain or loss that had been recognised in other comprehensive income is allocated between the part that continues to be recognised and the part that is no longer recognised 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 issued by an entity 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 issued by the Bank are recognised at the proceeds received, net of direct issue costs.

Repurchase of the Bank'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 Bank's own equity instruments.

Other financial liabilities

Other financial liabilities, including deposits by banks and customers, loans received from government agencies, subordinated debt and other financial liabilities, are initially measured at fair value, net of transaction costs.

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

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

Derecognition of financial liabilities

The Bank derecognises financial liabilities when, and only when, the Bank'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.

Financial guarantee contracts

A financial guarantee contract is a contract that requires the issuer to make specified payments to reimburse the holder for a loss it incurs because a specified debtor fails to make payments when due in accordance with the terms of a debt instrument.

Financial guarantee contracts issued by the Bank are initially measured at their fair values and, if not designated as at FVTPL, are subsequently measured at the higher of:

- The amount of the obligation under the contract, as determined in accordance with IAS 37 *Provisions, Contingent Liabilities and Contingent Assets*; and
- The amount initially recognized less, where appropriate, cumulative amortization recognized in accordance with the revenue recognition policies.

Derivative financial instruments

Forwards and futures. Forward and futures contracts are contractual agreements to buy or sell a specified financial instrument at a specific price and date in the future. Forwards are customised contracts transacted in the over-the-counter market. Futures contracts are transacted in standardised amounts on regulated exchanges and are subject to daily cash margin requirements. The main differences in the risk associated with forward and futures contracts are credit risk and liquidity risk.

The Bank has credit exposure to the counterparties of forward contracts. The credit risk related to future contracts is considered minimal because the cash margin requirements of the exchange help ensure that these contracts are always honoured. Forward contracts are settled gross and are, therefore, considered to bear a higher liquidity risk than the futures contracts which are settled on a net basis. Both types of contracts result in market risk exposure.

Derivatives are initially recognised at fair value at the date the derivative contracts are entered into and are subsequently remeasured to their fair value at the end of each reporting period. The resulting gain or loss is recognised in profit or loss immediately.

Leases

Leases are classified as finance leases whenever the terms of the lease transfer substantially all the risks and rewards of ownership to the lessee. All other leases are classified as operating leases.

The Bank as lessee

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

In the event that lease incentives are received to enter into operating leases, such incentives are recognised as a liability. The aggregate benefit of incentives is recognised as a reduction of rental expense on a straight-line basis, except where another systematic basis is more representative of the time pattern in which economic benefits from the leased asset are consumed.

Cash and cash equivalents

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

Mandatory cash balances with the CBAR

Minimum reserve deposits with the Central Bank of the Republic of Azerbaijan represent the amount of obligatory reserves deposited with the Central Bank of the Republic of Azerbaijan in accordance with requirements established by the Central Bank of the Republic of Azerbaijan, which subject to restrictions on their availability. In view of the above the amount of the minimum reserve deposit required by the Central Bank of the Republic of Azerbaijan is not included as a cash equivalent in statement of cash flows.

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 are stated at cost less accumulated depreciation and accumulated impairment losses.

Depreciation is recognised so as to write off the cost of assets less their residual values over their useful lives, using the straight-line method. The estimated useful lives, residual values and depreciation method are reviewed at the end of each reporting period, with the effect of any changes in estimate accounted for on a prospective basis at the following annual rates:

Buildings	5%
Furniture and equipment	20%
Computer equipments	25%
Other fixed assets	20%
Vehicles	25%
Leasehold improvements	10%

An item of property and equipment is derecognised 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 recognised in profit or loss.

Intangible assets

Intangible assets acquired separately. Intangible assets with finite useful lives that are acquired separately are carried at cost less accumulated amortisation and accumulated impairment losses. Amortisation is recognised on a straight-line basis over their estimated useful lives of 10 years. The estimated useful life and amortisation 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.

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 recognised in profit or loss when the asset is derecognised.

Impairment of tangible and intangible assets

At the end of each reporting period, the Bank 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). When it is not possible to estimate the recoverable amount of an individual asset, the Bank 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.

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 recognised immediately in profit or loss.

When 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 recognised for the asset (or cash-generating unit) in prior years. A reversal of an impairment loss is recognised immediately in profit or loss.

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 Bank's current tax is calculated using tax rates that have been enacted or substantively enacted by the end of the reporting period.

Deferred tax

Deferred tax is recognised on temporary differences between the carrying amounts of assets and liabilities in the financial statements and the corresponding tax bases used in the computation of taxable profit. Deferred tax liabilities are generally recognised for all taxable temporary differences. Deferred tax assets are generally recognised for all deductible temporary differences to the extent that it is probable that taxable profits will be available against which those deductible temporary differences can be utilised.

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

Deferred tax liabilities and assets are measured at the tax rates that are expected to apply in the period in which the liability is settled or the asset realised, based on tax rates (and tax laws) that have been enacted or substantively enacted by the end of the reporting period. The measurement of deferred tax liabilities and assets reflects the tax consequences that would follow from the manner in which the Bank expects, at the end of the reporting period, to recover or settle the carrying amount of its assets and liabilities.

Current and deferred tax for the year

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

Operating taxes

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

Provisions

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

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

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

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 Bank's functional currency (foreign currencies) are recognised 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 recognised in profit or loss in the period in which they arise.

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

	December 31, 2014	December 31, 2013
AZN/1 US Dollar	0.7844	0.7845
AZN/1 Euro	0.9522	1.0780

Collateral

The Bank 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 Bank a claim on these assets for both existing and future customer liabilities.

3. CRITICAL ACCOUNTING JUDGEMENTS AND KEY SOURCES OF ESTIMATION OF UNCERTAINTY

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

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

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 Bank regularly reviews its loans and receivables to assess for impairment. The Bank's loan impairment provisions are established to recognize incurred impairment losses in its portfolio of loans and receivables. The Bank 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 Bank's estimated losses and actual losses would require the Bank to record provisions which could have a material impact on its financial statements in future periods.

The Bank 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. Similarly, the Bank 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 national or local 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 Bank uses management's judgment to adjust observable data for a group of loans to reflect current circumstances not reflected in historical data.

The allowances for impairment of financial assets in the financial statements have been determined on the basis of existing economic and political conditions. The Bank is not in a position to predict what changes in conditions will take place in the Republic of Azerbaijan 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, 2014 and 2013, gross loans and receivables totalled AZN 323,491 thousand and AZN 253,753 thousand, respectively, and the allowance for impairment losses amounted to AZN 25,350 thousand and AZN 29,497 thousand, respectively.

Valuation of financial instruments

As described in Note 27, the Bank uses valuation techniques that include inputs that are not based on observable market data to estimate the fair value of certain types of financial instruments. Note 27 provides detailed information about the key assumptions used in the determination of the fair value of financial instruments, as well as the detailed sensitivity analysis for these assumptions. The Bank management believes that the chosen valuation techniques and assumptions used are appropriate in determining the fair value of financial instruments.

Useful lives of property and equipment

As described above, the Bank reviews the estimated useful lives of property and equipment at the end of each annual reporting period.

Tax legislation

Azerbaijani tax, currency and customs legislation is subject to varying interpretations. Refer to Note 24.

Initial recognition of related party transactions

In the normal course of business the Bank enters into transactions with its related parties. IAS 39 requires initial recognition of financial instruments based on their fair values. Judgement is applied in determining if transactions are priced at market or non-market interest rates, where there is no active market for such transactions. The basis for judgement is pricing for similar types of transactions with unrelated parties and effective interest rate analysis. The management concluded that interest rates for transactions with related parties do not significantly differ from those applied to transactions with third parties. The information on related party balances is disclosed in Note 30.

Capital adequacy ratio

Capital adequacy ratio is calculated in accordance with the International Convergence of Capital Measurement and Capital Standards (July 1988, updated in November 2005) or Basel Capital Accord requirements. Such requirements are subject to interpretation and accordingly the appropriateness of the inclusion, exclusion, and/or classification of amounts included in the calculation of the capital adequacy ratio requires management judgment, for example, whether the off-balance sheet commitments covered by blocked customer accounts would carry 0% risk for the purposes of calculating total risk-weighted assets. Currently, management believes that such off-balance sheet commitments carry 0% risk for the capital adequacy calculation purposes.

Liquidity mismatch

As set out in the contractual maturity table in Note 29, as at December 31, 2014 the Bank had a negative cumulative liquidity gap of AZN 16,722 thousand in the period up to twelve months (2013: AZN 3,709 thousand).

Management believes that although current accounts balance of AZN 44,311 thousand as of December 31, 2014 is included under on demand category in maturity table, apparently not all of these amounts will be withdrawn in period of one month. Past experience demonstrates that current account balances have not decreased below AZN 12,942 thousand for the period of last three years.

Shareholders have been providing a continuous support to the Bank in the periods of problems with liquidity. As a result of management's assessment and the actions being undertaken, the management believes that the Bank will be able to cover its liquidity needs over the next twelve months.

Term borrowings

Management has considered whether gains or losses should arise on initial recognition of loans from government financial institutions and related lending. The Bank obtains long term financing from government financial institutions at interest rates at which such institutions ordinarily lend in emerging markets and which may be lower than rates at which the Bank could source the funds from local lenders. As the transactions are with unrelated parties, management's judgement is that these funds and the related lending are at the market interest rates and no initial recognition gains or losses should arise. In making this judgment management also considered that these instruments are a separate market segment.

4. APPLICATION OF NEW AND REVISED INTERNATIONAL FINANCIAL REPORTING STANDARDS (IFRSs)

The Bank has adopted the following new or revised standards and interpretations issued by International Accounting Standards Board and the International Financial Reporting Interpretations Committee (the IFRIC) which became effective for the Bank's annual financial statements for the year ended December 31, 2014:

Standards affecting the financial statements

Amendments to IFRSs affecting amounts reported in the financial statements. In the current year, the following new and revised Standards and Interpretations have been adopted and have affected the amounts reported in these financial statements.

- Amendments to IFRS 10, IFRS 12 and IAS 27 – *Investment Entities*;
- Amendments to IAS 32 – *Offsetting Financial Assets and Financial Liabilities*;
- Amendments to IAS 36 – *Recoverable Amount Disclosures for Non-Financial Assets*;
- Amendments to IAS 39 – *Novation of Derivatives and Continuation of Hedge Accounting*;
- IFRIC 21 *Levies*.

Amendments to IFRS 10, IFRS 12 and IAS 27 – *Investment Entities*. The amendments to IFRS 10 introduce an exception from the requirement to consolidate subsidiaries for an investment entity. Instead, an investment entity is required to measure its interests in subsidiaries at fair value through profit or loss in its consolidated and separate financial statements. The exception does not apply to subsidiaries of investment entities that provide services that relate to the investment entity's investment activities.

To qualify as an investment entity, a reporting entity is required to:

- Obtain funds from one or more investors for the purpose of providing them with professional investment management services;
- Commit to its investor(s) that its business purpose is to invest funds solely for returns from capital appreciation, investment income, or both; and
- Measure and evaluate performance of substantially all of its investments on a fair value basis.

Consequential amendments have been made to IFRS 12 and IAS 27 to introduce new disclosure requirements for investment entities.

These amendments do not have any effect on the financial statements as the Bank is not an investment entity.

Amendments to IAS 32 – *Offsetting Financial Assets and Financial Liabilities*. The amendments to IAS 32 clarify the requirements relating to the offset of financial assets and financial liabilities. Specifically, the amendments clarify the meaning of 'currently has a legally enforceable right of set-off' and 'simultaneous realization and settlement'.

There is no effect of these amendments on the financial statements as the Bank does not have any financial assets and financial liabilities that qualify for offset.

Amendments to IAS 36 – *Recoverable Amount Disclosures for Non-Financial Assets*. The amendments to IAS 36 restrict the requirement to disclose the recoverable amount of an asset or a cash-generating unit to periods in which an impairment loss has been recognized or reversed. In addition, they expand and clarify the disclosure requirements applicable to when recoverable amount of an asset or a cash-generating unit has been determined on the basis of fair value less costs of disposal. The new disclosures include the fair value hierarchy, key assumptions and valuation techniques used which are in line with the disclosure required by IFRS 13 *Fair Value Measurements*.

Amendments to IAS 39 – *Novation of Derivatives and Continuation of Hedge Accounting*. These amendments allow the continuation of hedge accounting when a derivative is novated to a clearing counterparty and certain conditions are met. The amendments also clarify that any change to the fair value of the derivative designated as a hedging instrument arising from the novation should be included in the assessment and measurement of hedge effectiveness.

There is no effect of these amendments on these financial statements as the Bank does not apply hedge accounting.

IFRIC 21 Levies. The interpretation is applicable to all payments imposed by governments under legislation, other than income taxes that are within the scope of IAS 12 and fines and penalties for breaches of legislation. The interpretation clarifies that a liability to pay a levy should only be recognised when an obligating event has occurred and provides guidance on how to determine whether a liability should be recognized progressively over specific period or in full at a specific date. There was no effect of the interpretation on these financial statements except for the change in the Bank's policy.

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

- Amendments to IAS 19 - *Defined Benefit Plans: Employee contributions*¹;
- Annual Improvements to IFRSs 2010-2012 Cycle¹;
- Annual Improvements to IFRSs 2011-2013 Cycle¹;
- Annual Improvements to IFRSs 2012-2014 Cycle²;
- IFRS 14 *Regulatory Deferral Accounts*²;
- Amendments to IAS 16 and IAS 38 - *Clarification of Acceptable Methods of Depreciation and Amortisation*²;
- Amendments to IAS 27 - *Equity Method in Separate Financial Statements*²;
- Amendments to IAS 16 and IAS 41 - *Agriculture: Bearer Plants*²;
- Amendments to IFRS 11 - *Accounting for Acquisition of Interests in Joint Operations*²;
- Amendments to IFRS 10 and IAS 28 - *Sale or Contribution of Assets between an Investor and its Associate or Joint Venture*²;
- IFRS 15 *Revenue from Contracts with Customers*³;
- IFRS 9 *Financial Instruments*⁴.

¹ Effective for annual periods beginning on or after 1 July 2014, with earlier application permitted.

² Effective for annual periods beginning on or after 1 January 2016, with earlier application permitted.

³ Effective for annual periods beginning on or after 1 January 2017, with earlier application permitted.

⁴ Effective for annual periods beginning on or after 1 January 2018, with earlier application permitted.

Amendments to IAS 19 – *Defined Benefit Plans: Employee contributions.* The amendments to IAS 19 Employee Benefits clarify the requirements related to how contributions from employees or third parties that are linked to service should be attributed to periods of service. In addition, amendments permit a practical expedient if the amount of the contributions is independent of the number of years of service, such contributions, can, but are not required, to be recognised as a reduction in the service cost in the period in which the related service is rendered. The Bank's management does not expect any impact of these amendments on the financial statements as the Bank has no defined benefit plans.

IFRS 14 *Regulatory Deferral Accounts.* IFRS 14 permits an entity which is a first-time adopter of International Financial Reporting Standards to continue to account, with some limited changes, for 'regulatory deferral account balances' in accordance with its previous GAAP, both on initial adoption of IFRS and in subsequent financial statements.

The application of IFRS 14 will not have any impact on the Bank's financial statements in the future as the Bank is not an IFRS first-time adopter.

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 recognise revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods 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;
- Recognise revenue when (or as) the entity satisfies a performance obligation.

Under IFRS 15, an entity recognises revenue when or as a performance obligation is satisfied, i.e. when 'control' of the goods or services underlying the particular performance obligation is transferred to the customer. Far more prescriptive guidance has been added on topics such as the point in which revenue is recognised, accounting for variable consideration, costs of fulfilling and obtaining a contract and various related matters. New disclosures about revenue are also introduced.

The management of the Bank anticipates that the application of IFRS 15 in the future may have a significant impact on amount and timing of revenue recognition. However, it is not practicable to provide a reasonable estimate of the effect of IFRS 15 until a detailed review has been completed.

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. In July 2014 IASB issued a finalised version of IFRS 9 mainly introducing impairment requirements for financial assets and limited amendments to the classification and measurement requirements for financial assets. IFRS 9 is aiming at replacing IAS 39 Financial Instruments: Recognition and Measurement.

The key requirements of IFRS 9 are:

- **Classification and measurement of financial assets.** Financial assets are classified by reference to the business model within which they are held and their contractual cash flow characteristics. Specifically, debt instruments that are held within the 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 after initial recognition. The 2014 version of IFRS 9 introduces a 'fair value through other comprehensive income' category for debt instruments held within the business model whose objective is achieved both by collecting contractual cash flows and selling financial assets, and that have contractual terms of the financial asset giving rise on specified dates to cash flows that are solely payments of principal and interest on the principal amount outstanding which are measured at fair value through other comprehensive income after initial recognition. All other debt and equity investments are measured at their fair values. 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) in other comprehensive income, with only dividend income generally recognised in profit or loss.
- **Classification and measurement of financial liabilities.** Financial liabilities are classified in a similar manner to under IAS 39, however there are differences in the requirements applying to the measurement of an entity's own credit risk. IFRS 9 requires that the amount of change in the fair value of the financial liability that is attributable to changes in the credit risk of that liability is presented in other comprehensive income, unless the recognition of the effects of changes in the liability's credit risk in OCI would create or enlarge an accounting mismatch in profit or loss. Changes in fair value attributable to a financial liability's credit risk are not subsequently reclassified to profit or loss.
- **Impairment.** The 2014 version of IFRS 9 introduces an 'expected credit loss' model for the measurement of the impairment of financial assets, 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 a credit loss is recognized.

- **Hedge accounting.** Introduces a new hedge accounting model that is designed to be more closely aligned with how entities undertake risk management activities when hedging financial and non-financial risk exposures. Under IFRS 9, greater flexibility has been introduced to the types of transactions eligible for hedge accounting, specifically broadening the types of instruments that qualify for hedging instruments and the types of risk components of non-financial items that are eligible for hedge accounting. In addition, the effectiveness test has been overhauled and replaced with the principal of an 'economic relationship'. Retrospective assessment of hedge effectiveness is also no longer required. Enhanced disclosure requirements about an entity's risk management activities have also been introduced.
- **Derecognition.** The requirements for the derecognition of financial assets and liabilities are carried forward from IAS 39.

The standard is effective from 1 January 2018 with early application permitted. Depending on the chosen approach to applying IFRS 9, the transition can involve one or more than one date of initial application for different requirements.

The management of the Bank anticipates that the application of IFRS 9 in the future may have a significant impact on amounts reported in respect of the Bank's financial assets and financial liabilities. However, it is not practicable to provide a reasonable estimate of the effect of IFRS 9 until a detailed review has been completed.

Amendments to IFRS 11 – Accounting for Acquisitions of Interests in Joint Operations. The amendments to IFRS 11 provide guidance on how to account for the acquisition of a joint operation that constitutes a business as defined in IFRS 3 *Business Combinations*. Specifically, the amendments state that the relevant principles on accounting for business combinations in IFRS 3 and other standards should be applied. The same requirements should be applied to the formation of a joint operation if and only if an existing business is contributed to the joint operation by one of the parties that participate in the joint operation. A joint operator is also required to disclose the relevant information required by IFRS 3 and other standards for business combinations.

The management of the Bank does not anticipate that the application of these amendments will have a material impact of the Bank's financial statements.

Amendments to IAS 16 and IAS 38 – Clarification of Acceptable Methods of Depreciation and Amortisation. The amendments to IAS 16 prohibit entities from using a revenue-based depreciation method for items of property, plant and equipment. The amendments to IAS 38 introduce a rebuttable presumption that revenue is not an appropriate basis for amortization of an intangible asset. This presumption can only be rebutted when the intangible asset is expressed as a measure of revenue, or when it can be demonstrated that revenue and consumption of the economic benefits of the intangible asset are highly correlated.

The amendments apply prospectively for annual periods beginning on or after 1 January 2016. Currently, the Bank uses straight-line method for depreciation and amortization of its property, plant and equipment and intangible assets, respectively.

The management of the Bank does not anticipate that the application of these amendments will have a material impact on the Bank's financial statements.

Amendments to IAS 16 and IAS 41 – Agriculture: Bearer Plants. The amendments to IAS 16 and IAS 41 define a bearer plant and require biological assets that meet the definition of a bearer plant to be accounted for as a property, plant and equipment in accordance with IAS 16, instead of IAS 41. The produce growing on bearer plants continues to be accounted for as agricultural produce in accordance with IAS 41.

The management of the Bank does not expect any impact of adoption of these amendments on the financial statements as the Bank is not engaged in agricultural activities.

Amendments to IAS 27 – Equity Method in Separate Financial Statements. The amendments to IAS 27 allows entities to apply the equity method as one of the option for accounting for its investments in subsidiaries, joint ventures and associates in its separate financial statements. The amendments are effective from 1 January 2016 with earlier application permitted.

The management of the Bank does not expect any impact of these amendments on the financial statements as the Bank does not prepare its separate financial statements.

Amendments to IFRS 10 and IAS 28 – Sale or Contribution of Assets between an Investor and its Associate or Joint Venture. The amendments clarify that on a sale or contribution of assets to a joint venture or associate or on a loss of control when joint control or significant influence is retained in a transaction involving an associate or a joint venture, the extent of any gain or loss recognized depends on whether the assets or subsidiary constitute a business, as defined in IFRS 3. When the assets or subsidiary constitutes a business, any gain or loss is recognized in full; when the assets or subsidiary do not constitute a business, the entity's share of the gain or loss is eliminated.

The amendments apply prospectively to transactions occurring in annual periods beginning on or after 1 January 2016 with early application permitted. The management of the Bank does not anticipate that the application of these amendments will have a material impact on the Bank's financial statements.

Annual Improvements to IFRSs 2010-2012 Cycle. The Annual Improvements to IFRSs 2010-2012 Cycle include a number of amendments to various IFRSs, which are summarized below.

The amendments to IFRS 2 change the definition of 'vesting condition' and 'market condition' and add definitions for 'performance condition' and 'service condition' which were previously included within the definition of 'vesting condition'.

The amendments to IFRS 3 clarify that contingent consideration that is classified as an asset or liability should be measured at fair value at each reporting date, irrespective of whether the contingent consideration is a financial instrument within the scope of IAS 39 or IFRS 9 or a non-financial asset or liability.

The amendments to IFRS 8 require an entity to disclose the judgements made by management in applying the aggregation criteria to operating segments and clarify that a reconciliation of the total of the reportable segments' assets to the entity's assets should only be provided if the segment assets are regularly provided to the chief operating decision-maker.

The amendments to the basis for conclusions of IFRS 13 clarify that the issue of IFRS 13 and consequential amendments to IAS 39 and IFRS 9 did not remove the ability to measure short-term receivables and payables with no stated interest rate at their invoice amounts without discounting, if the effect of discounting is immaterial. These amendments are considered to be effective immediately.

The amendments to IAS 16 and IAS 38 remove perceived inconsistencies in the accounting for accumulated depreciation/ amortisation when an item of property, plant and equipment or an intangible asset is revalued. The amended standards clarify that the gross carrying amount is adjusted in a manner consistent with the revaluation of the carrying amount of the asset and that accumulated depreciation/ amortisation is the difference between the gross carrying amount and the carrying amount after taking into account accumulated impairment losses.

The amendments to IAS 24 clarify that a management entity providing key management personnel services to a reporting entity is a related party of the reporting entity. Consequently, the reporting entity should disclose as related party transactions the amounts incurred for the service paid or payable to the management entity for the provision of key management personnel services. However, disclosure of the components of such compensation is not required.

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

Annual Improvements to IFRSs 2011-2013 Cycle. The Annual Improvements to IFRSs 2011-2013 Cycle include the following amendments to various IFRSs.

The amendments to IFRS 3 clarify that the standard does not apply to the accounting for the formation of all types of joint arrangement in the financial statements of the joint arrangement itself.

The amendments to IFRS 13 clarify that the scope of portfolio exception for measuring the fair value of a group of financial assets and financial liabilities on a net basis includes all contracts that are within the scope of, and accounted for in accordance with, IAS 39 or IFRS 9, even if those contracts do not meet the definitions of a financial assets or financial liabilities within IAS 32.

The amendments to IAS 40 clarify that IAS 40 and IFRS 3 are not mutually exclusive and application of both standards may be required. Consequently, an entity acquiring investment property must determine whether the property meets the definition of investment property in terms of IAS 40, and whether the transaction meets the definition of a business combination under IFRS 3.

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

Annual Improvements to IFRSs 2012-2014 Cycle. The Annual Improvements to IFRSs 2012-2014 Cycle include the following amendments to various IFRSs.

The amendments to IFRS 5 clarify that reclassification of an asset or a disposal group from held for sale to held to distribution to owners or vice versa should not be considered changes to a plan of sale or a plan of distribution to owners and that the classification, presentation and measurement requirements applicable to the new method of disposal should be applied. In addition, amendments clarify that assets that no longer meet the criteria for held for distribution to owners and do not meet the criteria for held for sale should be treated in the same way as assets that cease to be classified as held for sale. The amendments should be applied prospectively.

The amendments to IFRS 7 provide additional guidance to clarify whether a servicing contract is continuing involvement in a transferred asset for the purposes of the disclosures required in relation to transferred assets. In addition, amendments to IFRS 7 were made to clarify that the disclosure requirements on offsetting financial assets and financial liabilities are not explicitly required to be included in the condensed interim financial statements for all interim periods, however, the disclosures may need to be included in condensed interim financial statements to comply with IAS 34. The amendments should be applied retrospectively.

The amendments to IAS 19 clarify that the high quality corporate bonds used to estimate the discount rate for post-employment benefits should be issued in the same currency as the benefits to be paid. The amendments apply from the beginning of the earliest comparative period presented in the financial statements in which the amendments are first applied.

The amendments to IAS 34 clarify that information required by IAS 34 that is provided elsewhere within the interim financial report but outside the interim financial statements should be incorporated by way of a cross-reference from the interim financial statements to the other part of the interim financial report that is available to users on the same terms and at the same time as the interim financial statements.

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

5. RESTATEMENT

On February 1, 2014, the Central Bank of the Republic of Azerbaijan amended the rules on interest income recognition on loans with overdue interest over 90 days. Under the previous rules interest income on loans with overdue interest over 90 days was not accrued. According to the amendment, banks are now required to accrue interest income on such loans and simultaneously create an allowance on impairment losses. In accordance with IAS 8 "Accounting Policies, Changes in Accounting Estimates and Errors," these financial statements were restated as detailed in the following paragraph:

Financial statement line item	As previously reported	Adjustment	As restated
December 31, 2013			
Accrued interest income on loans to customers	28,004	1,208	29,212
Allowance for impairment losses	(28,289)	(1,208)	(29,497)
2013			
Interest income on loans to customers	32,766	1,208	33,974
Provision for impairment losses on interest bearing assets	82	(1,208)	(1,126)
December 31, 2012			
Accrued interest income on loans to customers	19,442	4,810	24,252
Allowance for impairment losses	(27,411)	(4,810)	(32,221)

6. CASH AND BALANCES WITH THE CENTRAL BANK OF THE REPUBLIC OF AZERBAIJAN

	December 31, 2014	December 31, 2013
Cash on hand	9,581	6,633
Balances with the Central Bank of the Republic of Azerbaijan	<u>13,432</u>	<u>4,112</u>
Total cash and balances with the Central Bank of the Republic of Azerbaijan	<u>23,013</u>	<u>10,745</u>

The obligatory minimum reserve deposits with the Central Bank of the Republic of Azerbaijan included in the balances with CBAR are restricted balances of AZN 4,319 thousand and AZN 3,985 thousand as at December 31, 2014 and 2013, respectively. The Bank is entitled to use all funds on its correspondent account provided that average daily balance for 30 days period will be eventually higher than required mandatory reserve.

Cash and cash equivalents for the purposes of the statement of cash flows comprise the following:

	December 31, 2014	December 31, 2013
Cash and balances with CBAR	23,013	10,745
Correspondent accounts with other banks	4,911	6,377
Due from banks with original maturity within 90 days	<u>-</u>	<u>3,931</u>
Less minimum reserve deposits with CBAR	(4,319)	(3,985)
Less other blocked accounts with CBAR	<u>-</u>	<u>(127)</u>
Total cash and cash equivalents	<u>23,605</u>	<u>16,941</u>

The Bank did not have blocked accounts with CBAR as at December 31, 2014 (December 31, 2013: AZN 127 thousand blocked accounts).

7. DUE FROM BANKS

Due from banks comprise:

	December 31, 2014	December 31, 2013
Term Placement with other banks	11,789	3,926
Correspondent accounts with other banks	4,911	6,377
Due from banks with original maturity less than 90 days	-	3,931
Total due from banks	16,700	14,234

Movements in the allowance for impairment losses on balances due from banks for the years ended December 31, 2014 and 2013 are disclosed in Note 20.

As at December 31, 2014 the Bank simultaneously placed with and received short term funds from one bank in different currency of AZN 160 thousand.

As at December 31, 2014 the Bank had no balance with individual exposure exceeding 10% of equity. (December 31, 2013: due from one bank with individual exposure exceeding 10% of the Bank's equity).

8. OTHER DEBT SECURITIES

As at December 31, 2014 the Bank held term debt securities of one local company totaling AZN 3,131 thousand with the nominal interest rate of 11% per annum (December 31, 2013: Nil).

9. LOANS TO CUSTOMERS

Loans to customers comprise:

	December 31, 2014	December 31, 2013 (restated)
Loans to legal entities		
Trade and services	33,571	21,456
Manufacturing	13,442	16,499
Construction	14,641	5,590
Transportation	2,104	2,379
Agriculture	3,416	342
Other	683	348
Total loans to legal entities	67,857	46,614
Loans to individuals		
Purchase of motor vehicles	64,708	88,161
Entrepreneurs	123,238	77,666
Consumer loans	30,987	19,189
Mortgage loans	30,541	17,576
Plastic cards	3,542	2,668
Other	2,618	1,879
Total loans to individuals	255,634	207,139
Less: allowance for impairment losses	(25,350)	(29,497)
Total loans to customers	298,141	224,256

As at December 31, 2014 and 2013 the Bank granted loans to one customer with total amount of AZN 5,688 thousand and AZN 5,184 thousand, respectively, which exceeded 10% of the Bank's equity.

As at December 31, 2014 and 2013 a significant amount of loans (100% of total loans to customers) is granted to companies operating in the Republic of Azerbaijan, which represents a significant geographical concentration in one region.

Analysis by credit quality of loans to customers outstanding as at December 31, 2014 was as follows:

As at December 31, 2014	Corporate	Purchase of motor vehicles	Entrepreneurs	Consumer loans	Mortgage loans	Plastic cards	Other purposes	Total
Unimpaired loans collateralized by								
- motor vehicles	5,726	50,636	706	3	55	3	3	57,132
- real estate	4,607	-	38,160	5	29,734	37	2,455	74,998
- guarantee	5,521	1,791	40,752	14,631	-	514	-	63,209
- equipment	7,212	-	1,959	2,147	-	-	-	11,318
- securities	12,428	-	205	-	-	-	-	12,633
- cash deposits	651	-	100	4,340	-	1,048	-	6,139
- goods and materials	4,147	-	4,764	1,496	-	-	-	10,407
- other collateral	-	-	70	141	-	-	-	211
- unsecured loans	2,158	-	187	3,205	-	1,363	-	6,913
Total unimpaired loans	42,450	52,427	86,903	25,968	29,789	2,965	2,458	242,960
Collectively assessed								
Overdue:								
up to 30 days	911	3,782	1,803	1,272	512	107	-	8,387
31 to 90 days	1,959	4,214	2,105	784	104	112	160	9,438
91 to 180 days	670	567	1,139	498	136	91	-	3,101
181 to 360 days	4,961	368	1,729	1,010	-	52	-	8,120
over 360 days	5,876	3,350	18,879	1,455	-	215	-	29,775
Total collectively assessed loans	14,377	12,281	25,655	5,019	752	577	160	58,821
Individually impaired								
Overdue:								
over 360 days	11,030	-	10,680	-	-	-	-	21,710
Total individually impaired loans	11,030	-	10,680	-	-	-	-	21,710
Less: allowance for impairment losses	(9,070)	(884)	(13,566)	(1,444)	(222)	(164)	-	(25,350)
Total loans to customers	58,787	63,824	109,672	29,543	30,319	3,378	2,618	298,141

Analysis by credit quality of loans to customers outstanding as at December 31, 2013 was as follows:

As at December 31, 2013 (resated)	Corporate	Purchase of motor vehicles	Entrepreneurs	Consumer loans	Mortgage loans	Plastic cards	Other purposes	Total
Unimpaired loans collateralized by								
- motor vehicles	-	76,898	779	1	-	-	6	77,684
- real estate	3,576	-	11,802	44	15,299	201	1,789	32,711
- guarantee	2,517	-	22,062	7,514	-	182	-	32,275
- equipment	8,665	-	1,428	2,411	-	12	84	12,600
- securities	5,173	-	451	-	-	-	-	5,624
- cash deposits	2,858	-	11	4,519	-	1,350	-	8,738
- goods and materials	287	-	1,819	5	-	-	-	2,111
- other collateral	-	-	218	68	-	-	-	286
- unsecured loans	80	-	846	2,574	-	646	-	4,146
Total unimpaired loans	23,156	76,898	39,416	17,136	15,299	2,391	1,879	176,175
Collectively assessed								
Overdue:								
up to 30 days	144	3,791	973	293	208	1	-	5,410
31 to 90 days	67	3,904	507	147	299	9	-	4,933
91 to 180 days	-	184	1,370	93	220	8	-	1,875
181 to 360 days	2,755	263	2,677	210	147	6	-	6,058
over 360 days	4,665	3,121	14,861	1,310	1,403	253	-	25,613
Total collectively assessed loans	7,631	11,263	20,388	2,053	2,277	277	-	43,889
Individually impaired								
Overdue:								
181 to 360 days	3,773	-	1,911	-	-	-	-	5,684
over 360 days	12,054	-	15,951	-	-	-	-	28,005
Total individually impaired loans	15,827	-	17,862	-	-	-	-	33,689
Less: allowance for impairment losses	(10,002)	(2,541)	(15,435)	(1,200)	(170)	(149)	-	(29,497)
Total loans to customers	36,612	85,620	62,231	17,989	17,406	2,519	1,879	224,256

The table below summarizes total amount of loans to customers before provision for loan impairment by type of collateral, rather than the fair value of collateral itself as at December 31, 2014 and December 31, 2013:

	Corporate	Purchase of motor vehicles	Entrepreneurs	Consumer loans	Mortgage loans	Plastic cards	Other purposes	Total
As at December 31, 2014								
Loans collateralized by								
- motor vehicles	5,726	62,740	935	20	55	22	3	69,501
- real estate	11,712	-	60,868	346	30,486	46	2,615	106,073
- guarantee	9,369	1,958	47,270	16,277	-	578	-	75,452
- equipment	14,837	10	5,631	3,113	-	-	-	23,591
- securities	14,514	-	468	-	-	-	-	14,982
- cash deposits	873	-	104	5,362	-	1,113	-	7,452
- goods and materials	8,668	-	5,172	1,515	-	3	-	15,358
- other collateral	-	-	148	162	-	-	-	310
- unsecured loans	2,158	-	2,642	4,192	-	1,780	-	10,772
	<u>67,857</u>	<u>64,708</u>	<u>123,238</u>	<u>30,987</u>	<u>30,541</u>	<u>3,542</u>	<u>2,618</u>	<u>323,491</u>
Less: allowance for impairment losses	<u>(9,070)</u>	<u>(884)</u>	<u>(13,566)</u>	<u>(1,444)</u>	<u>(222)</u>	<u>(164)</u>	<u>-</u>	<u>(25,350)</u>
Total loans to customers	<u>58,787</u>	<u>63,824</u>	<u>109,672</u>	<u>29,543</u>	<u>30,319</u>	<u>3,378</u>	<u>2,618</u>	<u>298,141</u>
As at December 31, 2013 (restated)								
Loans collateralized by								
- motor vehicles	-	88,161	866	62	-	19	6	89,114
- real estate	12,242	-	36,730	317	17,576	223	1,789	68,877
- guarantee	10,605	-	25,983	8,626	-	216	-	45,430
- equipment	10,185	-	6,337	2,537	-	12	84	19,155
- securities	10,357	-	758	-	-	-	-	11,115
- cash deposits	231	-	31	4,522	-	1,373	-	6,157
- goods and materials	2,914	-	2,088	9	-	-	-	5,011
- other collateral	-	-	315	74	-	-	-	389
- unsecured loans	80	-	4,558	3,042	-	825	-	8,505
	<u>46,614</u>	<u>88,161</u>	<u>77,666</u>	<u>19,189</u>	<u>17,576</u>	<u>2,668</u>	<u>1,879</u>	<u>253,753</u>
Less: allowance for impairment losses	<u>(10,002)</u>	<u>(2,541)</u>	<u>(15,435)</u>	<u>(1,200)</u>	<u>(170)</u>	<u>(149)</u>	<u>-</u>	<u>(29,497)</u>
Total loans to customers	<u>36,612</u>	<u>85,620</u>	<u>62,231</u>	<u>17,989</u>	<u>17,406</u>	<u>2,519</u>	<u>1,879</u>	<u>224,256</u>

The Bank applied the portfolio provisioning methodology prescribed by IAS 39: Financial Instruments: Recognition and Measurement, and created portfolio provisions for impairment losses that were incurred but have not been specifically identified with any individual loan by the end of the reporting period. The Bank's policy is to classify each loan as 'unimpaired' until a specific objective evidence of impairment of the loan is identified. The impairment provisions may exceed the total gross amount of individually impaired loans as a result of this policy and the portfolio impairment methodology. The Bank's internal loan grading policy is to classify each loan as follows:

- Standard loans – Loans with the payments of both principal and interest are up-to-date in accordance with the agreed terms and provisions up to 10% against gross carrying amount.
- Sub-standard loans – Fully secured or expected loss is less than 20% of the unsecured amount and 10%-20% provisions against gross carrying amount.
- Doubtful loans – Indeterminable security value but expected to be significant with expected loss is 20% to less than 100% of the loan and 20%-100% provision against gross carrying amount.
- Loss (bad) loans – Loan recovery is assessed to be insignificant with no security available as alternative resource and 100% provision against gross carrying amount.

For the purposes of above tables analysing credit quality of loans to customers, standard and sub-standard loans have been classified as 'unimpaired' loans. Doubtful and loss (bad) loans have been classified as either 'collectively assessed' or 'individually impaired' loans.

During the years ended December 31, 2014 and 2013 the Bank received non-financial assets by taking possession of collateral it held as security. As at December 31, 2014 and 2013 such assets in amount of AZN 4,543 thousand and AZN 3,365 thousand, respectively, are stated separately in the statement of financial position.

10. PROPERTY AND EQUIPMENT

Property and equipment comprise:

	Buildings	Furniture and fixture	Computer equipment	Vehicles	Other fixed assets	Leasehold improvements	Total
Cost							
January 1, 2013	3,101	1,907	2,358	808	183	1,596	9,953
Additions	-	695	692	80	152	1,847	3,466
Disposals	-	(24)	(47)	-	(68)	-	(139)
December 31, 2013	3,101	2,578	3,003	888	267	3,443	13,280
Additions	4	1,084	1,054	162	149	2,453	4,906
Disposals	-	(289)	(727)	(11)	(32)	(497)	(1,556)
December 31, 2014	3,105	3,373	3,330	1,039	384	5,399	16,630
Accumulated depreciation							
January 1, 2013	(74)	(1,120)	(1,264)	(491)	(114)	(805)	(3,868)
Depreciation charge	(155)	(396)	(489)	(128)	(26)	(111)	(1,305)
Eliminated on disposals	-	24	47	-	68	-	139
December 31, 2013	(229)	(1,492)	(1,706)	(619)	(72)	(916)	(5,034)
Depreciation charge	(155)	(425)	(678)	(145)	(63)	(409)	(1,875)
Eliminated on disposals	-	289	727	11	32	497	1,556
December 31, 2014	(384)	(1,628)	(1,657)	(753)	(103)	(828)	(5,353)
Net book value:							
December 31, 2014	2,721	1,745	1,673	286	281	4,571	11,277
December 31, 2013	2,872	1,086	1,297	269	195	2,527	8,246

As at December 31, 2014 and 2013 included in property and equipment were fully depreciated assets totaling AZN 1,786 thousand and AZN 2,674 thousand, respectively.

11. INTANGIBLE ASSETS

	Software	CIP	Total
Cost			
January 1, 2013	1,553	65	1,618
Additions	534	-	534
Transfers	65	(65)	-
Disposals	(70)	-	(70)
December 31, 2013	2,082	-	2,082
Additions	453	-	453
Disposals	(49)	-	(49)
December 31, 2014	2,486	-	2,486
Accumulated amortization			
January 1, 2013	(448)	-	(448)
Charge for the year	(168)	-	(168)
Eliminated on disposal	68	-	68
December 31, 2013	(548)	-	(548)
Charge for the year	(223)	-	(223)
Eliminated on disposal	49	-	49
December 31, 2014	(722)	-	(722)
Net book value			
December 31, 2014	<u>1,764</u>	<u>-</u>	<u>1,764</u>
December 31, 2013	<u>1,534</u>	<u>-</u>	<u>1,534</u>

12. OTHER ASSETS

Other assets comprise:

	December 31, 2014	December 31, 2013
Other financial assets		
Amounts in course of settlement	519	259
Settlements on money transfers	427	218
Other receivables	834	715
Less: provision for other financial assets	(632)	(715)
Total other financial assets	1,148	477
Other non-financial assets		
Prepayments for property, plant and intangible assets	1,150	153
Prepaid expenses	1,005	1,219
Other	305	57
Total other assets	3,608	1,906

The movements in allowance for impairment losses on other assets are stated in Note 20.

13. REPOSSESSED ASSETS

During the years ended December 31, 2014 and 2013 the Bank received non-financial assets by taking possession of collateral it held as security as assets held for sale at fair value. As at December 31, 2014 and 2013 such assets amounted to AZN 4,543 thousand and AZN 3,365 thousand, respectively. The assets have been subsequently measured at the lower of fair value less cost to dispose or the carrying value, as the appropriate level of management has committed to a plan to sell the assets and an active program to locate a buyer and complete the plan has been initiated. Repossessed collaterals are comprised of real estate. It was intended that the fair value of these assets would be recovered principally through a sale transaction within one year from the date of classification.

14. DUE TO BANKS AND OTHER FINANCIAL INSTITUTIONS

Due to banks and other financial institutions comprise:

	December 31, 2014	December 31, 2013
Loans from government organizations	33,230	18,655
Loans from banks and other financial institutions	27,532	17,073
Loans from Central Bank of the Republic of Azerbaijan	3,220	1,120
Correspondent accounts of other banks	338	117
Total due to banks and other financial institutions	64,320	36,965

As at December 31, 2014 and 2013, included in loans received from government agencies are loans from the National Fund for Support of Entrepreneurship amounting to AZN 6,949 thousand and AZN 7,245 thousand respectively. These loans have maturity periods from 1 year to 7 years and bear an annual interest rate of 1%. This rate is considered as a market rate as this is rate by which the National Fund for Support of Entrepreneurship lends to local banks in the Republic of Azerbaijan.

As at December 31, 2014 and 2013, included in loans received from government agencies are loans from the Azerbaijan Mortgage Fund amounting to AZN 26,280 thousand and AZN 11,410 thousand, respectively. These loans have maturity periods from 10 years to 30 years and bear an annual interest rate of 1-8%. This rate is considered as a market rate as this is rate by which the Azerbaijan Mortgage Fund lends to local banks in the Republic of Azerbaijan.

The Bank is not obligated to comply with any financial covenants in relation to due to banks and other financial institutions balances as at December 31, 2014 and 2013.

15. CUSTOMER ACCOUNTS

Customer accounts comprise:

	December 31, 2014	December 31, 2013
Time deposits	195,907	156,025
Current and settlement accounts	44,311	16,645
Total customer accounts	240,218	172,670

As at December 31, 2014 and 2013, deposits by customers totaling AZN 54 thousand and AZN 502 thousand, respectively, were held as security against guarantees issued by the Bank.

As at December 31, 2014 and 2013 deposits by customer totaling AZN 35,000 thousand and AZN 25,150 thousand (15% and 15% of total deposits by customers), respectively, were due to 10 customers, which represents a significant concentration.

	December 31, 2014	December 31, 2013
Analysis by economic sector/customer type:		
Individuals	176,765	141,514
Insurance	26,507	21,273
Trade	14,189	8,058
Construction and real estate	9,770	930
State organizations	10,335	-
Manufacturing	1,504	318
Transport and communication	243	138
Other	905	439
Total customer accounts	240,218	172,670

16. OTHER LIABILITIES

Other liabilities comprise:

	December 31, 2014	December 31, 2013
Other financial liabilities:		
Items in course of settlement	561	155
Accrued expenses	48	63
Provision on guarantees and other contingencies	-	-
	<u>609</u>	<u>218</u>
Other non-financial liabilities:		
Taxes payable, other than income tax	361	195
Other	31	19
Total other liabilities	1,001	432

The movements in provision for guarantees and other commitments are stated in Note 20.

17. SUBORDINATED DEBT

Subordinated debt comprises:

	Currency	Maturity year	Nominal interest rate %	December 31, 2014	December 31, 2013
Topaz Opportunities (BVI)	USD	2023	12%	6,703	6,708
Nikoil CJSC	USD	2023	12%	5,066	-
ISR Holding LLC	USD	2023	12%	119	119
OJSC Uralsib	USD	2023	12%	-	5,070
Total subordinated debt				11,888	11,897

In the event of bankruptcy or liquidation of the Bank, repayment of this debt is subordinate to the repayments of the Bank's liabilities to all other creditors.

The Bank is not obligated to comply with any financial covenants in relation to this subordinated debt.

18. SHARE CAPITAL

As at December 31, 2014 the Bank's authorized, issued and fully paid share capital comprised 17,250 thousand ordinary shares with par value of AZN 2 each (2013: 17,250 thousand ordinary shares with par value of AZN 2 each).

	Number of authorized, issued and fully paid in ordinary shares	Share capital
January 1, 2013	11,250,000	22,500
Issue of shares	<u>6,000,000</u>	<u>12,000</u>
December 31, 2013	17,250,000	34,500
Issue of shares	<u>-</u>	<u>-</u>
December 31, 2014	<u><u>17,250,000</u></u>	<u><u>34,500</u></u>

The ultimate controlling party of the Bank is Mr. V. Alekperov.

In 2014 the Bank declared and paid dividends of AZN 1,486 thousand on ordinary shares (2013: nil).

19. NET INTEREST INCOME

	Year ended December 31, 2014	Year ended December 31, 2013 (restated)
Interest income comprises:		
Interest income on financial assets recorded at amortized cost:		
- Interest income on unimpaired assets	36,569	28,726
- Interest income on impaired assets	<u>7,666</u>	<u>5,248</u>
Total interest income	<u><u>44,235</u></u>	<u><u>33,974</u></u>
Interest income on financial assets recorded at amortized cost comprises:		
Interest income on loans to customers	43,211	33,884
Interest income on due from banks	852	90
Interest income on debt securities	<u>172</u>	<u>-</u>
Total interest income on financial assets recorded at amortized cost	44,235	33,974
Interest expense comprises:		
Interest expense on liabilities recorded at amortized cost	<u>(23,020)</u>	<u>(16,980)</u>
Total interest expense	<u><u>(23,020)</u></u>	<u><u>(16,980)</u></u>
Interest expense on financial liabilities recorded at amortized cost comprises:		
Interest expense on customer accounts	(19,279)	(14,960)
Interest expense on subordinated debt	(1,431)	(129)
Interest expense on due to banks and other financial institutions	<u>(2,310)</u>	<u>(1,891)</u>
Total interest expense on financial liabilities recorded at amortized cost	<u><u>(23,020)</u></u>	<u><u>(16,980)</u></u>
Net interest income before provision on interest bearing financial assets	<u><u>21,215</u></u>	<u><u>16,994</u></u>

20. ALLOWANCE FOR IMPAIRMENT LOSSES AND OTHER PROVISIONS

The movements in allowance for impairment losses on interest bearing assets were as follows:

	Due from banks	Loans to customers	Total
December 31, 2012 (restated)	72	32,221	32,293
Write-off of loans	-	(3,922)	(3,922)
Provision charge	(72)	1,198	1,126
December 31, 2013 (restated)	-	29,497	29,497
Write-off of loans	-	(4,377)	(4,377)
Provision charge	-	230	230
December 31, 2014	-	25,350	25,350

The movements in other provisions were as follows:

	Other assets	Repossessed assets	Guarantees and other commitments	Total
December 31, 2012	688	379	255	1,322
Provision/(recovery of provision)	27	12	(255)	(216)
December 31, 2013	715	391	-	1,106
Recovery of provision	(83)	(12)	-	(95)
December 31, 2014	632	379	-	1,011

21. NET GAIN ON FOREIGN EXCHANGE OPERATIONS

Net gain on foreign exchange operations comprises:

	Year ended December 31, 2014	Year ended December 31, 2013
Dealing, net	751	538
Translation differences, net	(25)	(21)
Total net gain on foreign exchange operations	726	517

22. FEE AND COMMISSION INCOME AND EXPENSE

Fee and commission income and expense comprise:

	Year ended December 31, 2014	Year ended December 31, 2013
Fee and commission income:		
Settlements	2,047	1,408
Cash operations	976	855
Agency fees	373	286
Plastic card operations	325	277
Guarantees	218	135
Other	17	18
	<u>3,956</u>	<u>2,979</u>
Total fee and commission income	3,956	2,979
Fee and commission expense:		
Agency fees	(159)	(45)
Plastic card operations	(150)	(149)
Settlements	(92)	(61)
Cash operations	(71)	(16)
	<u>(472)</u>	<u>(271)</u>
Total fee and commission expense	(472)	(271)

23. OPERATING EXPENSES

Operating expenses comprise:

	Year ended December 31, 2014	Year ended December 31, 2013
Staff costs	9,747	8,308
Rent expenses	3,186	2,309
Depreciation and amortization	2,098	1,473
Professional services	1,519	1,334
Office cleaning expenses	831	20
Advertising and marketing expenses	769	675
Security expenses	607	612
Communication expenses	447	418
Payments to the Deposit Insurance Fund	321	294
Office supplies and printing expenses	303	253
Business trip expenses	264	222
Insurance expenses	168	318
Entertainment expenses	148	244
Repair and maintenance expenses	147	80
Transportation and travel expenses	128	89
Computer software cost	109	168
Taxes other than income tax	104	90
Legal and court expenses	89	74
Utilities expenses	89	60
Staff training	51	35
Other expenses	154	11
	<u>21,279</u>	<u>17,087</u>
Total operating expenses	21,279	17,087

24. INCOME TAXES

The Bank 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 Azerbaijan where the Bank operates, which may differ from IFRS.

The Bank 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, 2014 and 2013 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 Azerbaijan on taxable profits (as defined) under tax law in that jurisdiction.

Deferred tax (liabilities)/assets as at December 31, 2014 and 2013 comprise:

	December 31, 2014	December 31, 2013
Deferred tax (liabilities)/assets in relation to:		
Loans to customers	(301)	1,403
Property, equipment and intangible assets	<u>(13)</u>	<u>(303)</u>
Net deferred tax (liabilities)/assets	<u>(314)</u>	<u>1,100</u>

The effective tax rate reconciliation is as follows for the years ended December 31, 2014 and 2013:

	Year ended December 31, 2014	Year ended December 31, 2013
Profit before income tax	<u>4,106</u>	<u>2,232</u>
Theoretical tax at the statutory tax rate	(821)	(446)
Adjustment recognized in the current year in relation to the deferred tax of prior years	(524)	-
Tax effect of permanent differences	<u>(511)</u>	<u>(300)</u>
Income tax expense	<u>(1,856)</u>	<u>(746)</u>
Current income tax expense	(442)	(540)
Deferred tax expense recognized in the current year	<u>(1,414)</u>	<u>(206)</u>
Income tax expense	<u>(1,856)</u>	<u>(746)</u>

25. EARNINGS PER SHARE

The earnings and weighted average number of ordinary shares used in calculation of basic and diluted earnings per share are as follows:

	Year ended December 31, 2014	Year ended December 31, 2013
Net profit for the year attributable to owners of the Bank	2,250	1,486
Weighted average number of ordinary shares for the purpose of basic and diluted earnings per share (in thousands)	<u>17,250</u>	<u>13,206</u>
Earnings per share – basic and diluted (AZN)	<u>0.13</u>	<u>0.11</u>

26. COMMITMENTS AND CONTINGENCIES

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

The Bank's uses the same credit control and management policies in undertaking off-balance sheet commitments as it does for on-balance operations.

Provision for losses on contingent liabilities totaled Nil as at December 31, 2014 and 2013,

As at December 31, 2014 and 2013 contingent liabilities comprise:

	December 31, 2014	December 31, 2013
Contingent liabilities and credit commitments		
Guarantees issued and similar commitments	17,545	15,091
Forward contracts	11,258	13,724
Commitments on loans and unused credit lines	9,433	5,912
Total contingent liabilities and credit commitments	38,236	34,727

Extension of loans to customers within credit line limits is approved by the Bank on a case-by-case basis and depends on borrowers' financial performance, debt service and other conditions. As at December 31, 2014 and 2013 such unused credit lines come to AZN 9,433 thousand and AZN 5,912 thousand, respectively.

Operating lease commitments

As at December 31, 2014 and 2013, the Bank does not have material commitments under non-cancelable operating leases where the Bank is the lessee.

Legal proceedings

From time to time and in the normal course of business, claims against the Bank are received from customers and counterparties. Management is of the opinion that no material unaccrued losses will be incurred and accordingly no provision has been made in these financial statements.

Taxation

Commercial legislation of the Republic of Azerbaijan, 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 Bank's business activities, was to be challenged by the tax authorities, the Bank may be assessed additional taxes, penalties and interest.

Such uncertainty may relate to the valuation of financial instruments, valuation of provision for impairment losses and the market pricing of deals. Additionally such uncertainty may relate to the valuation of temporary differences on the provision and recovery of the provision for impairment losses on loans to customers and receivables, as an underestimation of the taxable profit. The management of the Bank believes that it has accrued all tax amounts due and therefore no allowance has been made in the financial statements.

Generally, taxpayers are subject to tax audits with respect to three calendar years preceding the year of the audit. However, completed audits do not exclude the possibility of subsequent additional tax audits performed by upper-level tax inspectorates reviewing the results of tax audits of their subordinate tax inspectorates. In the case of criminal investigation statute of limitation maybe extended up to seven years based on the court decision.

Operating environment

Emerging markets such as Azerbaijan 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 Azerbaijan continue to change rapidly, tax and regulatory frameworks are subject to varying interpretations. The future economic direction of Azerbaijan is heavily influenced by the fiscal and monetary policies adopted by the government, together with developments in the legal, regulatory, and political environment.

Because Azerbaijan produces and exports large volumes of oil and gas, its economy is particularly sensitive to the price of oil and gas on the world market, which decreased significantly during 2014. Management is unable to reliably estimate the effects of any further price fluctuations on the Bank's financial position.

27. 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.

Fair value of financial assets and financial liabilities that are not measured at fair value on a recurring basis (but fair value disclosures are required)

The directors consider that the carrying amounts of financial assets and financial liabilities recognised in the financial statements approximate their fair values as at December 31, 2014 and 2013.

	December 31, 2014		
	Level 1	Level 2	Total
Financial assets:			
Balances with CBAR	13,432	-	13,432
Due from banks		16,700	16,700
Loans to customers		298,141	298,141
Other debt securities		3,131	3,131
Other financial assets		1,148	1,148
Financial liabilities:			
Due to banks and other financial institutions		64,320	64,320
Customer accounts		240,218	240,218
Other financial liabilities		609	609
Subordinated debt		11,888	11,888

	December 31, 2013		
	Level 1	Level 2	Total
Financial assets:			
Balances with CBAR	4,112		4,112
Due from banks		14,234	14,234
Loans to customers		224,256	224,256
Other financial assets		477	477
Financial liabilities:			
Due to banks and other financial institutions		36,965	36,965
Customer accounts		172,670	172,670
Other financial liabilities		218	218
Subordinated debt		11,897	11,897

As at December 31, 2014 and 2013 available-for-sale financial assets include equity investments of AZN 304 thousand, which are carried at cost.

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

28. CAPITAL RISK MANAGEMENT

The Bank's objectives when managing capital is to comply with the capital requirements set by the Central Bank of the Republic of Azerbaijan, to safeguard the Bank's ability to continue as a going concern and to maintain a sufficient capital base to achieve a capital adequacy ratio of at least 12%. Compliance with capital adequacy ratios set by the Central Bank of the Republic of Azerbaijan is monitored monthly with reports outlining their calculation reviewed and signed by the Bank's Financial Director, Chief Accountant, Chief of Audit Department, Head of Audit Committee and the Head of Supervisory Board. Other objectives of capital management are evaluated annually.

Under the current capital requirements set by the Central Bank of the Republic of Azerbaijan, banks have to: (a) hold the minimum level of share capital of AZN 10,000,000 (2013: AZN 10,000,000); (b) maintain a ratio of regulatory capital to risk weighted assets ("statutory capital ratio") at or above a prescribed minimum of 12% (2013: 12%) and (c) maintain a ratio of tier-1 capital to the risk-weighted assets (the "tier-1 capital ratio") at or above the prescribed minimum of 6% (2013: 6%).

The Central Bank of Azerbaijan Republic has taken a decision to increase minimum level of capital to AZN 50,000 thousand at July 25, 2013. The requirement is effective from January 1, 2015. In order to keep the level of capital in compliance with the CBAR's requirement, the Bank has obtained subordinated debt (see Note 17).

The following table analyses the Bank's regulatory capital resources for capital adequacy purposes in accordance with the requirements of Basel Capital Accord, as defined in the International Convergence of Capital Measurement and Capital Standards (July 1988, updated in November 2005):

	Year ended December 31, 2014	Year ended December 31, 2013
Composition of regulatory capital:		
Tier 1 capital:		
Ordinary shares	34,500	34,500
Share premium	401	401
Retained earnings	10,096	9,332
Less: intangible assets	(1,764)	(1,534)
Less: deferred tax assets	-	(1,100)
Total qualifying tier 1 capital	43,233	41,599
Subordinated debt	11,888	11,897
Total qualifying Tier 2 capital limited to 100% of Tier 1 capital	11,888	11,897
Total regulatory capital	55,121	53,496
Capital Ratios:		
Tier 1 capital	12%	15%
Total capital	15%	20%

As at December 31, 2014 and 2013, the Bank included in the computation of Total capital for Capital adequacy purposes the subordinated debt received, limited to 50% of Tier 1 capital. In the event of bankruptcy or liquidation of the Bank, repayment of this debt is subordinate to the repayments of the Bank's liabilities to all other creditors.

29. RISK MANAGEMENT POLICIES

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

- Credit risk
- Liquidity risk
- Market risk

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

Credit risk

The Bank 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.

Risk management and monitoring is performed within set limits of authority. These processes are performed by the Credit Committees and the Bank's Management Board. Before any application is made 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 branch risk-manager or the Risk Management Department. Daily risk management is performed by the Head of Credit Departments and Branch Credit Divisions.

The Bank 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 segments. Limits on the level of credit risk by a borrower and a product (by industry sector) are approved quarterly by the Management Board. The exposure to any one borrower including banks and brokers 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.

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

Commitments to extend credit represent unused portions of credit in the form of loans, guarantees or letters of credit. The credit risk on off-balance sheet financial instruments is defined as a probability of losses due to the inability of counterparty to comply with the contractual terms and conditions. With respect to credit risk on commitments to extend credit, the Bank is potentially exposed to a loss in an amount equal to the total unused commitments. However, the likely amount of the loss is less than the total unused commitments since most commitments to extend credit are contingent upon customers maintaining specific credit standards. The Bank applies the same credit policy to the contingent liabilities as it does to the statement of financial position financial instruments, i.e. the one based on the procedures for approving the granting of loans, using limits to mitigate the risk, and current monitoring. The Bank monitors the term to maturity of off balance sheet contingencies because longer term commitments generally have a greater degree of credit risk than short-term commitments.

Maximum exposure of credit risk

The Bank's maximum exposure to credit risk varies significantly and is dependant on both individual risks and general market economy risks.

The following table presents the maximum exposure to credit risk of balance sheet and off balance sheet financial assets. For financial assets in the balance sheet, the maximum exposure is equal to the carrying amount of those assets prior to any offset or collateral. The Bank's maximum exposure to credit risk under contingent liabilities and commitments to extend credit, in the event of non-performance by the other party where all counterclaims, collateral or security prove valueless, is represented by the contractual amounts of those instruments.

	Maximum exposure	Offset	Net exposure after offset	Collateral pledged	Net exposure
December 31, 2014					
Balances with CBAR	13,432	-	13,432	-	13,432
Due from banks	16,700	(160)	16,540	-	16,540
Loans to customers	298,141	(7,452)	290,689	(280,635)	10,054
Other debt securities	3,131	-	3,131	-	3,131
Other financial assets	1,148	-	1,148	-	1,148
Guarantees issued and similar commitments	17,545	(54)	17,491	(143)	17,348
Commitments on loans and unused credit lines	9,433	(4,256)	5,177	(2,953)	2,224
December 31, 2013					
Balances with CBAR	4,112	-	4,112	-	4,112
Due from banks	14,234	(3,920)	10,314	-	10,314
Loans to customers	224,256	(6,157)	218,099	(211,361)	6,738
Other financial assets	477	-	477	-	477
Guarantees issued and similar commitments	15,091	(502)	14,589	(235)	14,354
Commitments on loans and unused credit lines	5,912	(4,170)	1,742	(1,155)	587

Off-balance sheet risk

The Bank applies fundamentally the same risk management policies for off-balance sheet risks as it does for its on-balance sheet risks. In the case of commitments to lend, customers and counterparties will be subject to the same credit management policies as for loans and advances. Collateral may be sought depending on the strength of the counterparty and the nature of the transaction.

Geographical concentration

The Assets and Liabilities Management Committee ("ALMC") exercises control over the risk in the legislation and regulatory arena and assesses its influence on the Bank's activity. This approach allows the Bank to minimize potential losses from the investment climate fluctuations in the Republic of Azerbaijan.

The geographical concentration of assets and liabilities is set out below:

	The Republic of Azerbaijan	OECD countries	Other non-OECD countries	December 31, 2014 Total
NON-DERIVATIVE FINANCIAL ASSETS				
Cash and balances with the CBAR	23,013	-	-	23,013
Due from banks	11,909	4,483	308	16,700
Loans to customers	297,179	37	925	298,141
Other debt securities	3,131	-	-	3,131
Available-for-sale investments	304	-	-	304
Other financial assets	1,148	-	-	1,148
Total non-derivative financial assets	336,684	4,520	1,233	342,437
NON-DERIVATIVE FINANCIAL LIABILITIES				
Due to banks and other financial institutions	46,217	1,620	16,483	64,320
Customer accounts	119	-	11,769	11,888
Other financial liabilities	213,066	2,840	24,312	240,218
Subordinated debt	609	-	-	609
Total non-derivative financial liabilities	260,011	4,460	52,564	317,035
NET POSITION ON NON-DERIVATIVE FINANCIAL INSTRUMENTS	76,673	60	(51,331)	
	The Republic of Azerbaijan	OECD countries	Other non-OECD countries	December 31, 2013 Total
NON-DERIVATIVE FINANCIAL ASSETS				
Cash and balances with CBAR	10,745	-	-	10,745
Due from banks	9,076	5,086	72	14,234
Loans to customers	223,604	-	652	224,256
Available-for-sale investments	304	-	-	304
Other financial assets	477	-	-	477
Total non-derivative financial assets	244,206	5,086	724	250,016
NON-DERIVATIVE FINANCIAL LIABILITIES				
Due to banks and other financial institutions	24,814	1,974	10,177	36,965
Customer accounts	156,923	2,211	13,536	172,670
Other financial liabilities	119	99	-	218
Subordinated debt	119	-	11,778	11,897
Total non-derivative financial liabilities	181,975	4,284	35,491	221,750
NET POSITION ON NON-DERIVATIVE FINANCIAL INSTRUMENTS	62,231	802	(34,767)	

Collateral

The amount and type of collateral required depends on an assessment of the credit risk of the counterparty. Guidelines are implemented regarding the acceptability of types of collateral and valuation parameters.

The main types of collateral obtained are as follows:

- For commercial lending, charges over real estate properties, inventory
- For retail lending, mortgages over residential properties.

At December 31, 2014 and 2013, the fair value of collateral that the Bank holds relating to loans individually determined to be impaired amounts to AZN 11,491 thousand and AZN 1,909 thousand, respectively. The collateral consists of real estate and equipment.

During the year, the Bank took possession of real estate with a carrying value of AZN 1,178 thousand at the statement of financial position date, which the Bank is in the process of selling.

Management monitors the market value of collateral, requests additional collateral in accordance with the underlying agreement, and monitors the market value of collateral obtained during its review of the adequacy of the allowance for impairment losses.

Credit quality by class of financial asset

The following table details credit ratings of financial assets held by the Bank:

December 31, 2014	A	BBB	<BBB	Not rated	Total
Due from banks	4,482	233	8,545	3,440	16,700
Loans to customers	-	-	-	298,141	298,141
Other debt securities	-	-	-	3,131	3,131
Available-for-sale investments	-	-	-	304	304
Other financial assets	-	-	-	1,148	1,148
December 31, 2013					
Due from banks	5,086	27	4,105	5,016	14,234
Loans to customers	-	-	-	224,256	224,256
Available-for-sale investments	-	-	-	304	304
Other financial assets	-	-	-	477	477

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

A model of the borrower's scoring assessment has been developed in the Bank to assess and decide on loans to corporate customers as well as small and medium-sized businesses. The scoring model is developed relating to standard loan products and includes key performance indicators of borrowers: financial situation, relations with the borrower, management quality, target use, location, credit history, collateral, etc.

The scoring assessment based on the borrower's parameters is one of the main factors for the decision-making process relating to loans.

A methodology of evaluation of borrowers-individuals is based on following criteria: education, occupancy, financial position, credit history, property owned by the borrower. Based on information obtained the maximum limit of a loan is calculated. The maximum limit of a loan is calculated using a ratio of debt pressure on a borrower.

The Bank applies internal methodologies to specific corporate loans and groups of retail loans. The scoring methodologies are tailor-made for specific products and are applied at various stages over the life of the loan. As a result, it is not possible to make a cross-product score comparison which would agree to the outstanding balance of loans to customers per the statement of financial position. As such, more detailed information is not being presented.

Financial assets other than loans to customers are graded according to the current credit rating they have been issued by an internationally regarded agency such as Fitch, Standard & Poor's and Moody's. The highest possible rating is AAA. Investment grade financial assets have ratings from AAA to BBB. Financial assets which have ratings lower than BBB are classed as speculative grade.

As at December 31, 2014 and 2013 the balances with the CBAR amounted to 13,432 thousand and AZN 4,112 thousand, respectively. The credit rating of the Republic of Azerbaijan according to the international rating agencies in 2014 corresponded to BBB- (2013: BBB-).

Liquidity risk

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

The ALMC controls these types of risks by means of maturity analysis, determining the Bank's strategy for the next financial period. Current liquidity is managed by the Treasury Department, which deals in the money markets for current liquidity support and cash flow optimization.

In order to manage liquidity risk, the Bank performs daily monitoring of future expected cash flows on clients' and banking operations, which is a part of the assets/liabilities management process. The Management Board sets limits on the minimum proportion of maturing funds available to meet deposit withdrawals and on the minimum level on interbank and other borrowing facilities that should be in place to cover withdrawals at unexpected levels of demand. An analysis of the liquidity risk is presented in the following table. The presentation below is based upon the information provided internally to key management personnel of the Bank.

	Weighted average effective interest rate	Up to 1 month	1 month to 3 months	3 months to 1 year	1 year to 5 years	Over 5 years	Maturity undefined	December 31, 2014 Total
NON-DERIVATIVE FINANCIAL ASSETS								
<i>Fixed interest rate instruments</i>								
Due from banks	7.15%	-	160	7,629	4,000	-	-	11,789
Loans to customers	18.83%	14,970	28,384	128,197	112,569	14,021	-	298,141
Other debt securities	11.00%	-	-	-	3,131	-	-	3,131
Total fixed interest bearing financial assets		<u>14,970</u>	<u>28,544</u>	<u>135,826</u>	<u>119,700</u>	<u>14,021</u>	<u>-</u>	<u>313,061</u>
<i>Non-interest bearing financial assets</i>								
Cash and balances with the CBAR		12,444	1,199	6,577	2,789	4	-	23,013
Due from banks		4,911	-	-	-	-	-	4,911
Available-for-sale investments		-	-	-	-	-	304	304
Other financial assets		<u>1,148</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>1,148</u>
Total non-interest bearing financial assets		<u>18,503</u>	<u>1,199</u>	<u>6,577</u>	<u>2,789</u>	<u>4</u>	<u>304</u>	<u>29,376</u>
Total non-derivative financial assets		<u>33,473</u>	<u>29,743</u>	<u>142,403</u>	<u>122,489</u>	<u>14,025</u>	<u>304</u>	<u>342,437</u>
NON-DERIVATIVE FINANCIAL LIABILITIES								
<i>Fixed interest rate instruments</i>								
Due to banks and other financial institutions	3.77%	10,904	6,058	14,053	6,944	26,023	-	63,982
Customer accounts	11.05%	6,881	21,443	117,630	49,884	69	-	195,907
Subordinated debts	12.00%	<u>114</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>11,774</u>	<u>-</u>	<u>11,888</u>
Total fixed interest bearing financial liabilities		<u>17,899</u>	<u>27,501</u>	<u>131,683</u>	<u>56,828</u>	<u>37,866</u>	<u>-</u>	<u>271,777</u>
<i>Non-interest bearing financial liabilities</i>								
Due to banks and other financial institutions		338	-	-	-	-	-	338
Customer accounts		44,311	-	-	-	-	-	44,311
Other financial liabilities		<u>609</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>609</u>
Total non-interest bearing financial liabilities		<u>45,258</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>45,258</u>
Total non-derivative financial liabilities		<u>63,157</u>	<u>27,501</u>	<u>131,683</u>	<u>56,828</u>	<u>37,866</u>	<u>-</u>	<u>317,035</u>
Interest sensitivity gap		<u>(2,929)</u>	<u>1,043</u>	<u>4,143</u>	<u>62,872</u>	<u>(23,845)</u>		
Cumulative interest sensitivity gap		<u>(2,929)</u>	<u>(1,886)</u>	<u>2,257</u>	<u>65,129</u>	<u>41,284</u>		
Liquidity gap		<u>(29,684)</u>	<u>2,242</u>	<u>10,720</u>	<u>65,661</u>	<u>(23,841)</u>		
Cumulative liquidity gap		<u>(29,684)</u>	<u>(27,442)</u>	<u>(16,722)</u>	<u>48,939</u>	<u>25,098</u>		

	Weighted average effective interest rate	Up to 1 month	1 month to 3 months	3 months to 1 year	1 year to 5 years	Over 5 years	Maturity undefined	December 31, 2013 Total
NON-DERIVATIVE FINANCIAL ASSETS								
<i>Fixed interest rate instruments</i>								
Due from banks	6.33%	-	3,931	-	3,926	-	-	7,857
Loans to customers	19.58%	9,847	19,759	97,945	87,517	9,188	-	224,256
Total fixed interest bearing financial assets		9,847	23,690	97,945	91,443	9,188	-	232,113
<i>Non-interest bearing financial assets</i>								
Cash and balances with the CBAR		7,178	413	2,222	930	2	-	10,745
Due from banks		6,377	-	-	-	-	-	6,377
Available-for-sale investments		-	-	-	-	-	304	304
Other financial assets		477	-	-	-	-	-	477
Total non-interest bearing financial assets		14,032	413	2,222	930	2	304	17,903
Total non-derivative financial assets		23,879	24,103	100,167	92,373	9,190	304	250,016
NON-DERIVATIVE FINANCIAL LIABILITIES								
<i>Fixed interest rate instruments</i>								
Due to banks and other financial institutions	4.50%	5,013	4,912	8,047	236	18,640	-	36,848
Customer accounts	10.62%	6,253	17,343	93,310	39,051	68	-	156,025
Subordinated debts	12.00%	-	-	-	-	11,897	-	11,897
Total fixed interest bearing financial liabilities		11,266	22,255	101,357	39,287	30,605	-	204,770
<i>Non-interest bearing financial liabilities</i>								
Due to banks and other financial institutions		117	-	-	-	-	-	117
Customer accounts		16,645	-	-	-	-	-	16,645
Other financial liabilities		218	-	-	-	-	-	218
Total non-interest bearing financial liabilities		16,980	-	-	-	-	-	16,980
Total non-derivative financial liabilities		28,246	22,255	101,357	39,287	30,605	-	221,750
Interest sensitivity gap		(1,419)	1,435	(3,412)	52,156	(21,417)		
Cumulative interest sensitivity gap		(1,419)	16	(3,396)	48,760	27,343		
Liquidity gap		(4,367)	1,848	(1,190)	53,086	(21,415)		
Cumulative liquidity gap		(4,367)	(2,519)	(3,709)	49,377	27,962		

In the tables above, maturity of mandatory reserves which are included to cash and balances with the CBAR are split based on contractual repayment periods of customer accounts as the calculation of mandatory reserves is linked to the daily balances of customer accounts deposited in the Bank.

In the tables above, the terms to maturity correspond to the contractual terms. However, individuals are entitled to terminate the deposit agreement ahead of schedule according to effective laws.

As set out in the contractual maturity table above, as at December 31, 2014 the Bank had a negative cumulative liquidity gap of AZN 16,722 thousand in the period up to twelve months (2013: AZN 3,709 thousand). Management believes that although current accounts balance of AZN 44,311 thousand as of December 31, 2014 is included under on demand category in maturity table, apparently not all of these amounts will be withdrawn in period of one month. Past experience demonstrates that current account balances have not decreased below AZN 12,942 thousand for the period of last three years.

Shareholders have been providing a continuous support to the Bank in the periods of problems with liquidity. As a result of management's assessment and the actions being undertaken, the management believes that the Bank will be able to cover its liquidity needs over the next twelve months.

The following tables detail the Bank'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 based on the earliest date on which the Bank can be required to pay. 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. The contractual maturity is based on the earliest date on which the Bank may be required to pay.

	Weighted average effective interest rate	Up to 1 month	1 month to 3 months	3 months to 1 year	1 year to 5 years	Over 5 years	December 31, 2014 Total
Fixed interest rate instruments							
Due to banks and other financial institutions	3.77%	11,162	6,444	15,064	10,262	39,519	82,451
Customer accounts	11.05%	8,765	24,835	125,402	58,029	95	217,126
Subordinated debt	12.00%	231	235	1,059	5,648	17,473	24,646
Total fixed interest bearing financial liabilities		20,158	31,514	141,525	73,939	57,087	324,223
Non-interest bearing instruments							
Due to banks and other financial institutions		338	-	-	-	-	338
Customer accounts		44,311	-	-	-	-	44,311
Other financial liabilities		609	-	-	-	-	609
Liabilities on financial guarantees		1,604	1,007	14,051	883	-	17,545
Commitments on loans and unused credit lines		1,035	1,033	3,690	3,675	-	9,433
Total non-interest bearing financial liabilities and commitments		47,897	2,040	17,741	4,558	-	72,236
Total financial liabilities and commitments		68,055	33,554	159,266	78,497	57,087	396,459

	Weighted average effective interest rate	Up to 1 month	1 month to 3 months	3 months to 1 year	1 year to 5 years	Over 5 years	December 31, 2013 Total
Fixed interest rate instruments							
Due to banks and other financial institutions	4.50%	5,142	5,148	8,670	2,196	27,204	48,360
Customer accounts	10.62%	7,860	21,546	98,671	45,870	100	174,047
Subordinated debt	12.00%	118	235	1,059	5,648	19,036	26,096
Total fixed interest bearing financial liabilities		13,120	26,929	108,400	53,714	46,340	248,503
Non-interest bearing instruments							
Due to banks and other financial institutions		117	-	-	-	-	117
Customer accounts		16,645	-	-	-	-	16,645
Other financial liabilities		218	-	-	-	-	218
Liabilities on financial guarantees		891	2,627	11,573	-	-	15,091
Commitments on loans and unused credit lines		267	504	3,485	1,656	-	5,912
Total non-interest bearing financial liabilities and commitments		18,138	3,131	15,058	1,656	-	37,983
Total financial liabilities and commitments		31,258	30,060	123,458	55,370	46,340	286,486

The amounts included above for financial guarantee contracts are the maximum amounts the Bank could be forced to settle under the arrangement for the full guaranteed amount if that amount is claimed by the counterparty to the guarantee. Based on expectations at the end of the reporting period, the Bank considers that it is more likely than not that no amount will be payable under the arrangement. However, this estimate is subject to change depending on the probability of the counterparty claiming under the guarantee which is a function of the likelihood that the financial receivables held by the counterparty which are guaranteed suffer credit losses.

The maximum amount the Bank could be forced to settle under the financial guarantee contracts if the fully guaranteed amount is claimed by the counterparty to the guarantee is AZN 17,545 thousand (2013: AZN 15,091 thousand).

Market risk

Market risk is that the risk that the Bank'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, currency risk, credit spreads, commodity prices and equity prices that the Bank is exposed to. There have been no changes as to the way the Bank measures risk or to the risk it is exposed or the manner in which these risks are managed and measured.

The Bank is exposed to interest rate risks as entities in the Bank borrow funds at both fixed and floating rates. The risk is managed by the Bank maintaining an appropriate mix between fixed and floating rate borrowings.

The ALMC also manages interest rate and market risks by matching the Bank's interest rate position, which provides the Bank with a positive interest margin. The Treasury Department conducts monitoring of the Bank's current financial performance, estimates the Bank's sensitivity to changes in interest rates and its influence on the Bank's profitability.

The majority of the Bank's loan contracts and other financial assets and liabilities that bear interest are either fixed and contain clauses enabling the interest rate to be changed at the option of the lender. The Bank monitors its interest rate margin and consequently does not consider itself exposed to significant interest rate risk or consequential cash flow risk.

Interest rate sensitivity

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

The sensitivity analyses below have been determined based on the exposure to interest rates for both derivatives and 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 100 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 100 basis points higher/lower and all other variables were held constant, the Bank's total profit or loss for the year ended December 31, 2014 would increase/decrease by AZN 413 thousand (2013: total profit or loss would increase/decrease by AZN 273 thousand). This is mainly attributable to the Bank's exposure to interest rates on its fixed rates borrowings.

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 Bank is exposed to the effects of fluctuations in the prevailing foreign currency exchange rates on its financial position and cash flows.

The ALMC controls currency risk by management of the open currency position on the estimated basis of AZN devaluation and other macroeconomic indicators, which gives the Bank an opportunity to minimize losses from significant currency rates fluctuations toward its national currency. The Treasury Department performs daily monitoring of the Bank's open currency position with the aim to match the requirements of the Central Bank of the Republic of Azerbaijan.

The Bank's exposure to foreign currency exchange rate risk is presented in the table below:

	AZN	USD USD 1 = AZN 0.7844	EUR EUR 1 = AZN 0.9522	Other currency	December 31, 2014 Total
Non-derivative financial assets					
Cash and balances with the CBAR	19,638	2,697	486	192	23,013
Due from banks	-	16,203	286	211	16,700
Loans to customers	206,344	86,914	4,883	-	298,141
Other debt securities	3,131	-	-	-	3,131
Available-for-sale investments	304	-	-	-	304
Other financial assets	601	547	-	-	1,148
Total non-derivative financial assets	230,018	106,361	5,655	403	342,437
Non-derivative financial liabilities					
Due to banks and other financial institutions	44,451	17,818	1,917	134	64,320
Subordinated debts	-	11,888	-	-	11,888
Customer accounts	154,545	80,132	5,385	156	240,218
Other financial liabilities	577	32	-	-	609
Total non-derivative financial liabilities	199,573	109,870	7,302	290	317,035
OPEN BALANCE SHEET POSITION	30,445	(3,509)	(1,647)	113	
Derivative financial instruments					
Forward contracts	(11,258)	8,306	2,952	-	
OPEN POSITION	19,187	4,797	1,305	113	
	AZN	USD USD 1 = AZN 0.7845	EUR EUR 1 = AZN 1.078	Other currency	December 31, 2013 Total
Non-derivative financial assets					
Cash and balances with CBAR	6,137	3,697	759	152	10,745
Due form banks	3,933	10,243	49	9	14,234
Loans to customers	167,129	51,729	5,398	-	224,256
Available-for-sale investments	304	-	-	-	304
Other financial assets	171	306	-	-	477
Total non-derivative financial assets	177,674	65,975	6,206	161	250,016
Non-derivative financial liabilities					
Due to banks and other financial institutions	19,786	12,584	4,595	-	36,965
Customer accounts	113,460	54,685	4,515	10	172,670
Other financial liabilities	84	133	-	1	218
Subordinated debt	-	11,897	-	-	11,897
Total non-derivative financial liabilities	133,330	79,299	9,110	11	221,750
OPEN BALANCE SHEET POSITION	44,344	(13,324)	(2,904)	150	
Derivative financial instruments					
Forward contracts	(13,724)	13,724	-	-	
OPEN POSITION	30,620	400	(2,904)	150	

Currency risk sensitivity

The following table details the Bank's sensitivity to a 35% (2013:10%) increase and decrease in the AZN against the relevant foreign currencies. 35% 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 35% change in foreign currency rates. The sensitivity analysis includes external loans as well as loans to foreign operations with the Bank 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 other equity where the AZN strengthens 35% against the relevant currency. For a 35% weakening of the AZN against the relevant currency, there would be a comparable impact on the profit and other equity, and the balances below would be negative.

	USD impact			EUR impact	
	2014	2013		2014	2013
Profit before tax	1,679	40	(i)	457	(290)

- (i) This is mainly attributable to the exposure outstanding on USD and EUR receivables and payables in the Bank at the end of the reporting period.

In management's opinion, the sensitivity analysis is unrepresentative of the inherent foreign exchange risk because the year end exposure does not reflect the exposure during the year.

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 Bank's assets and liabilities are actively managed. Additionally, the financial position of the Bank may vary at the time that any actual market movement occurs. For example, the Bank'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 Bank'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.

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 Bank cannot expect to eliminate all operational risks, but it endeavours 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.

30. TRANSACTIONS WITH RELATED PARTIES

Details of transactions between the Bank and related parties are disclosed below:

	December 31, 2014		December 31, 2013	
	Related party balances	Total category as per the financial statements caption	Related party balances	Total category as per the financial statements caption
Loans to customers		323,491		253,753
-key management personnel of the Bank or its parent	854		765	
Allowance for impairment losses on loans to customers		(25,350)		(29,497)
-key management personnel of the Bank or its parent	(6)		(1)	
Customer accounts		(240,218)		(172,670)
- shareholders and entities in which a substantial interest is owned by shareholders of the Bank	(1,966)		(2,646)	
- key management personnel of the Bank or its parent	(840)		(736)	
Due to banks and other financial institutions		(64,320)		(36,965)
- shareholders and entities in which a substantial interest is owned by shareholders of the Bank	-		(4,289)	
Subordinated debt		(11,888)		(11,897)
- shareholders and entities in which a substantial interest is owned by shareholders of the Bank	(11,888)		(11,897)	
Commitments on loans and unused credit lines		(9,433)		(5,912)
- key management personnel of the Bank or its parent	(113)		(58)	

The remuneration of the Bank's management was as follows:

	Year ended December 31, 2014		Year ended December 31, 2013	
	Related party transactions	Total category as per the financial statements caption	Related party transactions	Total category as per the financial statements caption
Key management personnel compensation:				
- short-term employee benefits (Note 23)	976	9,747	783	8,308
Total	976	9,747	783	8,308

Included in the statement of profit or loss and other comprehensive income for the years ended December 31, 2014 and 2013 are the following amounts which were recognized in transactions with related parties:

	2014		2013	
	Related party transactions	Total category as per the financial statements caption	Related party transactions	Total category as per the financial statements caption
Interest income		44,235		33,974
-key management personnel of the Bank or its parent	130		112	
Interest expense		(23,020)		(16,980)
- shareholders and entities in which a substantial interest is owned by shareholders of the Bank	(1,525)		(223)	
-key management personnel of the Bank or its parent	(90)		(92)	
(Provision)/recovery of provision on interest bearing assets		(230)		(1,126)
- shareholders and entities in which a substantial interest is owned by shareholders of the Bank	(5)		19	
-key management personnel of the Bank or its parent	-		19	

31. Subsequent events

One of the impacts of sharp drop of oil prices in the world market to Azerbaijan was reflected as devaluation of national currency. On February 21, 2015, the Central Bank of the Republic of Azerbaijan devalued the Azerbaijani Manat. As a result, the official exchange rate of AZN to the USD fell to AZN 1.05 per USD, and the official exchange rate of AZN to the Euro fell to AZN 1.19 per Euro, i.e. by approximately 34% from the exchange rates at the balance sheet date. To prevent the destabilisation of the financial market and economy as a whole, the Central Bank of the Republic of Azerbaijan plans to set a daily exchange rate for the AZN against a dual currency basket comprised of the USD and the Euro. This led to big migration of population's savings from AZN to USD, affecting country's banking sector, converting most of its liabilities in national currency to foreign currency. As a result, decline of liquidity of national currency drives to reduction of loan issuing in AZN, in addition, lending in USD is decreasing because of reluctance of population to take a loan in foreign currency. This has also led to deterioration in repayment of some loans which were subsequently restructured by the Bank.

Latest events concerning devaluation of national currency has also led to uncertainty about whether repayments of loans in foreign currency would be with rates before or after devaluation. This issue is expected to be reviewed by the state legal authorities.